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.

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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*

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department officials with regard to reopening of assessment, revision etc. in cases where the department is of the view that certain income had escaped from the chargeability of tax, ***but for exercising powers under section 221 of the Ordinance there must be a mistake apparently floating on the surface which is so obvious to strike one's mind without entering into long drawn process of reasonings, detailed deliberation etc.***

15. A perusal of the above decisions will leave no room for doubt that only those mistakes are rectifiable which are apparent from the record and floating on the surface and which do not require any long drawn process of reasonings, deliberation on a moot or debatable point. It is seen that the issue with regard to the taxability on the services rendered by the respondent outside Pakistan has been a contentious issue between the DCIR and the respondent hence, in our view, the same falls outside the scope of mistake apparent from the record. ***Moreover as seen from the above decisions it was already held in a number of decisions quoted supra that in cases where there could conceivably be two views/opinions the same falls outside the scope and ambit of rectification of mistake.*** *In the instant case also the view of charging tax on the impugned receipts as per the view of DCIR was liable to tax whereas as per the views of CIR(A) and ATIR the same is exempt under the relevant provisions of law, meaning thereby that there were two views/opinions and hence the issue was a moot point requiring detailed deliberation, lengthy arguments which could not be considered to be a mistake apparent from the record or a mistake floating on the surface."*

In another case of National Foods reported as 1992 PTD 570, the Hon'ble Supreme Court of Pakistan interpreted the same provision of the Income Tax Act, 1922. The relevant part of which is as under:

"Section 35 of the repealed Income Tax Act, 1922 confers a power to rectify any mistake in the order which is apparent from the record. Such power can be exercised suo motu or if it is brought to the notice by an assessee. ***Therefore, essential condition for exercise of such power is that the mistake should be apparent on the face of record; mistake which may be seen floating on the surface and does not require investigation or further evidence. The mistake should be so obvious that on mere reading the order it may immediately strike on the face of it. Where an officer exercising power under section 35 enters into the controversy, investigates into the matter, reassess the evidence or takes into consideration additional evidence and on that basis interprets the provision of law and forms an opinion different from the order, then it will not amount to "rectification" of the order.*** *Any mistake which is not patent and obvious on the record, cannot be termed to be an order which can be corrected by exercising power under section 35. "*

9- Hence an undesired action or the follow up on the notice by the commissioner offices would be without sanction of lawful jurisdiction and would be miscarriage of justice.

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existence. As a corollary of this fact, we can safely hold that all the proceedings conducted in pursuance of completion of assessment should be considered to have been made along with the actual assessment, which stands completed on the day complete return is filed.

6- It is evenly critical to mention her that the adjustment of such tax refundable against tax liability in the return of income for later tax years has also been the due cognizance by the Board itself whereby a separate TAB has been provided for the purpose in the Return of Income as follows

Refund Adjustment of Other Year(s) against Demand of this year	92101			

Your office would therefore that it is hence completely unwarranted to seek inference or to permit any re invention of though on the matter. The adjustment made, therefore, is not a mistake in the first place.

The "Mistake" should squarely fit in the definition of "Mistake"

7- It is a trite law, which the superior courts have held time and again that only those mistakes, of either fact or law, pointed out in the Assessment Order will be treated as mistake liable for rectification for which no further argument or further investigation is required. In case of any controversy, whether factual or legal, exists or where are more than one opinion on the matter, the same does not fit squarely in the definition of "Mistake" liable for rectification as enunciated by courts.

8- Therefore once after it has been cleared that a Deemed Order cannot be rectified and then the Courts and consequently the Board itself has allowed to adjust the refunds, the mistake pointed in the Notices cannot be called as A "Mistake". A plain perusal of notices reveals that the Commissioners have embarked upon verification and further investigation or to put in other words necessitates verification and further investigation before any conclusion is drawn. It cannot simply be called a case of Rectification of Mistake. Hence, it falls out of the scope of rectification of mistake given under section 221 of the Ordinance. A very relevant judgement in this regard would be that given by SHC wherein the ratio has been settled. The SHC has held in the case of Siemens Pakistan Engineering Co. Ltd. reported as 2017 PTD 903, as under.

"14. It would not be out of place to mention that section 35 of the Income Tax Ordinance, 1922 (repealed), section 156 of the Income Tax Ordinance, 1979 (repealed) and section 154 of Indian Income Tax Act, 1961 are para-materia to section 221 of the Ordinance, 2001. The powers of DCIR under section 221 of the Ordinance, as stated above, ***are quite limited to the extent of mistakes apparent from record*** *since there are other provisions of law which deal with the authority of*

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The way forward for the disposition of the Cases

10- At this juncture we feel it imperative to reposition the stance of our Tax BAR that we completely endorse that any short fall of payment of tax is ought to be made at full and where there has been proved any erroneous adjustment of tax refunds, the same should very much be recovered and paid without any resistance, but only and strictly according to the given and due process of law.

11- Be that as it may, if there was any shortfall in the return including a short payment of tax and/or incorrect adjustment of tax or incorrect adjustment previous year refund, the correct course of action should have been issuance of notice under sub-section (3) of section 120 of the Ordinance, which provides that where a return is not complete, the CIR shall issue a notice to the taxpayer informing him of the deficiencies in the return of income including short payment of tax payable and asking him to provide such information. You would appreciate that where no such notice has been issued in the first place, the Tax Return filed will be taken to be complete and without any deficiencies and, therefore, any assumption of jurisdiction under Section 221 of the Ordinance would fundamentally be incorrect.

Based on above, it should be abundantly clear that the current exercise is without due sanction of law and against the reported judgments of Superior Courts. We at the Karachi Tax Bar earnestly hope that your good office will urgently look into in the matter factually and judicially to get these notices vacated by the field officers, which in our opinion is certainly creating unnecessary agony and distress to the complaint taxpayers of the country who are regularly contributing their due share of taxes into the Government Exchequer as their moral, social and legal obligation and need due facilitation instead of Litigation.

Yours sincerely,

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