



Topics to be covered

- Sales Tax Audit
- Investigation
- Assessment of sales tax
- Audit observation, Show cause notice, and Order-in-Original



Tax Audits

Authority of Sales Tax Audit

- Routine/desk audit of records – Section 25 of STA
- Pre or Post Refund Audit – Chapter-III of Sales Tax Rules, 2006
- Investigation/Enquiry under Section-38 & 38B of STA
- Audit by Special Audit Panels under Section 32A of STA
- Investigation by Directorate General of Intelligence and Investigation-IR [refer SRO.116(I)/2015, dated 09 February 2015]

Tax Audit – Section 25 of STA

Departmental Audit – Section 25(1)

- CIR or his authorized Tax Officer can requisition statutory records or access the records / computers.
- On the basis of records, audit can be conducted once in a year.
- Records can be re-audited, if audited previously by Auditor General of Pakistan
- Order to be passed under Section 11 after completion of audit, as per procedure laid down under Para 39 of STGO No. 3 of 2004, dated 12 June 2004.

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Tax Audit – Provincial sales tax laws

Pre-audit desk review

- Analytical review
- Trends of input-output ratios, previous results, industry norms, etc.

Departmental Audit

- Not necessarily once a year
- On the basis of returns / records
- By an officer not less than Assistant Commissioner
- Criteria of selection prescribed in Audit Rules

Inquiry / Investigation

Special Audit

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Tax Audit

Basis of Departmental Audit [Rule 3 of Audit Rules-PRA]

- Irregular or abnormal fluctuations in input tax adjustments including carry forwards;
- Non or short payments of tax amounts declared on the monthly returns or other declarations;
- Unusual variations in inventories;
- Habitual tendency of filing short or misfiled returns;
- Sudden or unexpected downward changes in turnover; and
- Other cogent factor evident from the taxpayer's computer profile over doubts of tax evasion

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Investigations – S-38 of STA

- Section 25 itself provides authority of initiating investigation under Section 38 of STA in cases of tax frauds.
- Wide discretion of authorized officer acting on behalf of the Board or Commissioner to access business premises, stocks, records, etc.
- Onus lies on FBR / CIR to prove the tax fraud according to the definition of term 'tax fraud';
- Investigations are generally assigned to DG-I&I offices of FBR.
- Section 38 does not provide authority to adjudicate cases, as such assessment/recovery can be enforced through Section 11 of STA by the concerned LTU/CRTO/RTO.

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Selection of cases for audit by Board – S-72B

- Board is empowered to select cases for audit on random or parametric basis.
- Section 72B was under litigation where varied interpretations were given by Hon'ble Lahore and Islamabad High Courts. Hon'ble IHC held that Commissioner can exercise his authority independently to initiate audit without selection by the Board.
- Based on decision of LHC, the audit notices for the year 2011 were set aside and specific directions were given to the Board after framing parameters for selection of audit.

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Assessment of Sales Tax

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Assessment of tax and recovery – S-11 of STA

- Section 36 of STA was omitted vide FA-2012 and merged in S-11.
- Four situations are separately dealt u/s 11 of STA viz-a-viz:
 - ✓ If return is not filed and short-payment is occurred due to any miscalculation.
 - ✓ Non-payment or short payment of tax or claim of inadmissible refund for reasons other than miscalculation.
 - ✓ If tax shortfall or claim of inadmissible refund is due to some collusion or deliberate act.
 - ✓ If tax shortfall or claim of inadmissible is by reason of any inadvertence, error or misconstruction.
 - ✓ Non-withholding of sales tax (as per Sales Tax Withholding Rules)
- It's difficult for tax officer to distinguish the cases of willful & non-willful evasions

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Assessment of tax – S-11 of STA

- Show cause is mandatorily issued within 5 years of relevant date i.e. the time of payment of tax or when the refund was issued.
- Taxpayer must be awarded an opportunity of being heard.
- Order-in-Original must be issued within 120 days, extendable by CIR upto 90 days, excluding the time lapsed due to stay proceedings or ADRC or adjournment applied by the taxpayer [not beyond 60 days].
- If taxpayer fails to file a return, the tax officer is empowered to determine the tax liability of the registered person. Procedure for determination of minimum tax liability described under Sales Tax General Order No.3 of 2004, dated 12 June 2004.
- Definition of 'tax fraud' describes the cases which tantamount to deliberate evasion of tax. If conditions are not satisfied, the tax officer cannot impose excessive penalties on the registered person.

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Assessment of tax – Section 23 of Sindh Act

- AC-SRB makes assessment of SST liability on the basis of audit, inquiry, inspection or otherwise.
- In absence of information / return / records, AC-SRB can assess the SST liability on the basis of available information / material, determining the minimum tax liability.
- MTL is not final liability, which is determined as result of audit, special or forensic audit.
- Show cause notice can be issued within 8 years and Order is required to be passed within 180 days, extendable for 60 days excluding the time of adjournments.
- Amendment in assessment order is also authorized.
- Generally, SRB makes assessments on the basis of desk audits focusing on disclosures as per audited financial statements / accounts.

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**Audit observation,
show cause notice and
Order-in-Original**

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Key considerations

- Audit observation if issued is blessing in disguise. It helps to either avoid process of adjudication or restrict the quantum of demand to the extent of contentious / genuine issues;
- It is not obligatory upon tax officers to issue audit observation prior to issue of show cause notice.
- Show cause notice be examined first of all on technical grounds like time limitation, jurisdiction, guess work, proper opportunity of hearing, etc.
- Fact finding exercise should be comprehensive and rule of 'substance over form' could be vital.
- Imposition of default surcharge and penalties should always be challenged if the tax officer has not proved the malafide intent on the part of taxpayer to evade the tax.

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Key considerations

- Reply to show cause notice generally emerges as a vital source to build up a strong case before the appellate / litigation forums.
- Close coordinated efforts pay a lot during adjudication proceedings.
- Quality of presentation of documents and reconciliation help to avoid adverse orders.
- Documenting the hearing proceedings and attendance is also critical.
- Importance of taking global view.
- Use of connotation 'without prejudice' while arguing the grounds either factual or legal.
- Always determine the liability taking effect of input tax, if any, while responding to show cause notice or assessment notices.

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