

Audit and Assessment

Under Federal and Sindh Tax Law- Including time limitations

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Income Tax

TAX

A person wearing a dark suit and a striped tie is pointing their right index finger towards the word "TAX". The word "TAX" is rendered in large, white, 3D block letters with a bright blue glow. The background is dark blue with a bokeh effect of out-of-focus light circles.

The Origin

- Some theorist trace origin of audit back in 400 BC with ancient Egyptians and Babylonians;
- They had auditing systems for checking stores movement and including oral "audit reports"
- Widely believed that Industrial Revolution, from 1750 to 1850 leading to increased general public investment led to the concept of stewardship of resources and hence need for independent audit;
- There can be various forms of audit, widely known as statutory audit, internal audit, special purpose audit and tax audit;
- Each form has its own objectives which should be pivotal in execution if success is to be achieved;



The Tax Audit- Definition and objective

- An audit in simpler form is ‘examination of affairs of a person
- No formal definition of tax audit in the tax code or General clauses Act
- In common parlance ‘Tax Audit’ can be understood as:

audit of books of accounts maintained by the taxpayer under the tax laws with the purpose to ensure that the books of accounts maintained and the declaration filed reflect true amount of income and tax paid thereon.

- In all advanced taxation systems the core objective of tax audit is creating a system of deterrence



From Assessment to Audit- legislative Journey

Income Tax Act, 1922 [Adoption of Pre Partition Tax code]

- The return of income filed under section 22 of the Act
- Assessment by the Tax Officer in terms of section 23 of the Act.
- The section 38A of the Act provided the Director of Inspection, Commissioner, the Inspecting Assistant Commissioner or an Authorized Officer the powers to make an enquiry [No full scape audit]

Income Tax Ordinance 1979 [Now repealed law]

- Broadly the concept of Assessment borrowed;
- The return of income filed under section 22 of the Ordinance
- Assessment by the Tax Officer in terms of sections 59A and 62 of the Ordinance.
- Limited concept of Self Assessment schemes announced by the Board;
- Limited scope audit codes as well

The Income Tax Ordinance, 2001

- Addressing the emerging need to align with the global concepts;
- The Concept of Universal Self Assessment Scheme introduced
- The concept of audit in place of Assessment was introduced
- The Draconian law of GP Ratio based additions was no more in field

Audit vs. Assessment

Assessment is defined as *recording of TAX LIABILITY or Refund in the books*. If any discrepancy or transaction contrary to the INCOME TAX LAW or generally accepted ACCOUNTING procedure, during an Audit or otherwise, is detected and amended assessment is made on the basis of such detection.

Audit is different from assessment.

AUDIT DOES NOT AND SHOULD NOT NECESSARILY LEAD TO AN ASSESSMENT OR AMENDED ASSESSMENT IN EVERY CASE.

In general an audit has wider scope examination canvass as compared to Assessment.



From the Desk of Author- Professor Lee Burns

Commentary on USAS

“Paragraph (a) provides that when the taxpayer furnishes a return of income, the Commissioner is deemed to have made an assessment of the taxable income and tax payable thereon. These are the amounts of taxable income or tax payable shown in the taxpayer's return. Paragraph (b) provides that the taxpayer's return is treated as an assessment order issued to the taxpayer by the Commissioner on the day the return was furnished.

This section does not preclude the Commissioner from subsequently making an amended assessment under section 194, where the taxpayer has incorrectly calculated the amount of tax payable or on the basis of other information available to the Commissioner”.



From the Desk of Author- Professor Lee Burns- cont.

Concept of Audit

“Section 266 allows the Commissioner to select any person for audit of the person's income tax affairs. In selecting persons for audit, the Commissioner is expected to consider the person's history of compliance or non-compliance with the tax law; the amount of tax; the type of business; and any other factors the Commissioner regards as relevant.

The audit of a person in one year does not preclude the Commissioner from auditing that person again in the next year and following years, provided there are reasonable grounds for repeated audits”.



Various forms of Assessments

Description	Section
Deemed Assessment	120
Best Judgment Assessment	121
Amended Assessment	122
Amended assessment on account of revision of return by the taxpayer.	122(3)
Amended assessment on the basis of definite information acquired from as audit or otherwise	122(5)
If the assessment order is considered as erroneous and prejudicial in the interest of revenue.	122(5A)
Assessment giving effect to appellate order	124
Modified Assessment	124A
Assessment in case of disputed property	125

Dilution to the Concept of USAS

1. Underlying factors

- The tax authorities attribute it to misuse of USAS regime leading to sharp decline in Tax to GDP ratio;
- Lack of efforts to enforce new taxpayers and hence recourse to already registered persons

2. Underlying factors

- Insertion of section 122(5A) of the Ordinance- Right to audit in 2002;
- Insertion of Subsection 2A to section 114 vide Finance Act 2020 [Automated system to verify returns- currently suspended];
- Insertion of Subsection 2AA to section 177- Introduction of Industry benchmarks [The long withheld wish list of GP rates regime restored back]



Development of Law and disputes there-on

Progress in the Law

Unbridled powers to Commissioners to select and conduct 177 audit - Section.

Powers bestowed to Board to establish selection criteria for audit.- Section 177
Commissioner allowed to select the cases as per Board's criteria- Section -177

Board given explicit powers to select cases for audit- Section 214C

Both Board and Commissioner can select the taxpayer for audit- Section 177 [Explanation]
Board allowed to keep selection parameters confidential- Section 214C(1A)

2001 - 2004



2004

2004 - 2010

2010

2010 - 2013

2013

2013 - 2017

2017 - 2020

2020 - 2023

2023 - 2026

2026 - 2029

2029 - 2032

2032 - 2035

2035 - 2038

2038 - 2041

2041 - 2044

2044 - 2047

2047 - 2050

2050 - 2053

2053 - 2056

2056 - 2059

Challenges by Taxpayers

Selection power should rest with the Board.
Commissioner should only conduct the audit.

Power bestowed to Board are without necessary enabling provision in law.

Resentments in FBR for restricting Commissioner function to administration only.
Taxpayers questioned the selection as less vivid and anonymity of criteria for selection.

The courts have held in several cases that Board and Commissioners both have independent powers to audit the taxpayers.

Enabling provisions

1. POWERS TO SELECT

- Section 177 – Selection for audit by the Commissioner
- Section 214C - Selection by the FBR through random or parametric computer balloting

2. Conduct of audit

- Officer has to allow opportunity u/s 177(6) before embark upon amendment u/s 122.
- CIR may assign Audit conduct to
- Sec 210:-
 - Officer of Inland Revenue
 - Charter Accountant appointed by him or by the Board
 - Audit panel appointed by the Board



The Audit Process

- Selection of case under section 214C/ 177
- Intimation to the Taxpayer by the Commissioner- Section 177
- Information Document Request- Section 177
- Collection of further information – Section 176;
- Issuance of Audit Report – Section 177(6)- Mandatory
- Issuance of Show cause notice – Section 122(5)/122(9)
- Order under section 122(5) of the Ordinance;
- The ensuing appeal process



Attending The Audit Process

- Ensure timely compliance to IDR
- The details submitted should be conspicuously mentioned [10 bank statements, complete ledgers listed, x number of box files received]
- Any indication of intended inference for e.g. details required to invoke section 111(1) or section 174(2) should be refuted then and there
- Submit the soft copies in PDF [we are not meant to ease data mining for the tax authorities];
- Issuance of Audit Report under section 177(6) is mandatory. Keep track of it.
- The Show cause notice if issued should be refuted with full comprehension.
- Emphasis should be that the details were submitted in audit whenever required. Additional details cannot be required in show cause notice;
- All legal observations should be submitted at proceedings stage;
- The preparations for ensuing appeal process should start here.
- The tendency to agreed assessments – Advance agreement of payment under section 137(2)- Related matters.



Definite information- *The pivotal aspect*

Inclusive definition at section 122(8)

- Surmises, presumptions and difference of opinion cannot be a definite information.
- In full bench decision of honorable Supreme Court of Pakistan reported as 1993 SCMR 1108 = 68 TAX 1 (SC) it has been held that 'definite information' could not mean mere difference of opinion or further reasoning or other exercise of logic or even drawing conclusions.
- In a case law reported at 2012 PTD 1775 the honorable Tribunal has held that '*fishing inquiries is not allowed while exercising jurisdiction under section 122(5)*'. It is held that mere inquiries are being conducted through the notice without any definite information.

In case of non-compliance by taxpayers, the courts have given stricter verdicts on this matter.

2017 PTD 1731 in case of CIR, Zone-I, RTO, Rawalpindi versus Messrs. Khan CNG Filling Station dated 4th April 2017



Direct Recourse to the Court

A Constitutional Petition Under Article 199 of the Constitution can be considered in case of audit proceedings violates taxpayers fundamental rights.

Following can be certain instances where such rights can be considered as been violated

- A notice is issued without jurisdiction
- The case time barred in terms of section 122 or 174
- Amending an already amended assessment
- Intrusion into Commissioner's power to select cases for audit [sectoral audit selections]

Representation before tax authorities during the interim/ transitional period should be done carefully.

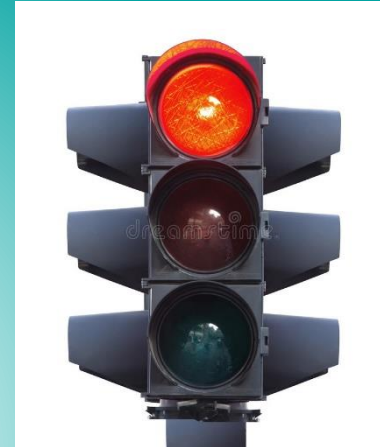


Best Judgement Assessment

In case of non-furnishing of return, in response to Notice u/s 114(3) or 114(4), non-furnishing of statement in compliance of notice u/s 115(5) or 143, 144 or 116 or as per 177(1) for failing to produce accounts, documents and records required to be maintaining u/s 174, during audit, the Commissioner may make assessment to the best of his judgment u/s 121 based on information or material on record.

For making best judgment:-

- a. History should be followed - 2009 PTD 638 Trib.
- b. There must be a speaking order - 99 TAX 329 Trib.
- c. Should not be passed for single default - 29 TCR 100, 1987 PTD 39
- d. Should be proper, fair and not dishonest- 1959 PTD 100 H.C.

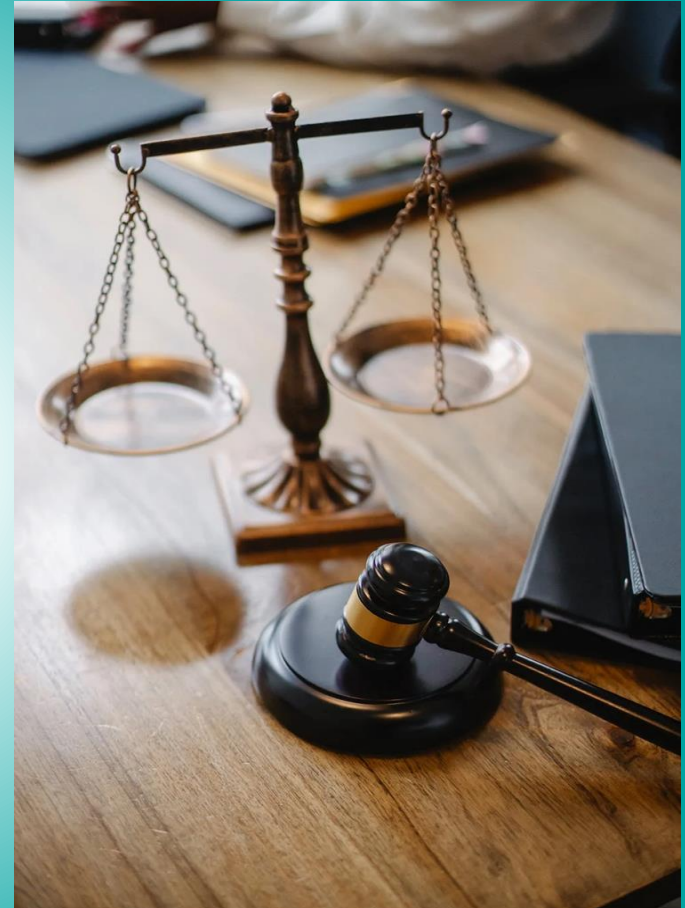


The Time limitations- *The concept of vested right*

The various provisions prescribing time limitation are

- The section 122(4)
- The section 174(2)
- Clause 105 Part IV 2nd Schedule [July 2018 to June 2019];
- Clause 105A Part IV 2nd Schedule to the Ordinance [w.e.f 1 July 2022]

Once achieving this time limitation, the subsequent changes cannot take away this vested right.



Indirect Taxes Under Federal and Provincial Laws

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TAX

Audit, Assessment and Time limitation

Description	Sales Tax Act 1990	Federal Excise Act 2005	Sindh Sales Tax of Services Act 2011
Selection of audit- By Commissioner	Under Section 25. By Officer of Inland Revenue , once in a year after approval of Commissioner.	Under Section 46. By Officer of Inland Revenue, once in a year after approval of Board/Commissioner.	Under Section 28 By Officer of SRB/ Auditor, once in a year, after approval of Board/Commissioner
Selection by the Board	Under Section 72B	Under Section 42B	
Time limit for assessment	Under Section 11. Show cause notice must be issued within 5 years of the end of financial year in which the relevant date fall. Under Section 11 order shall be issued within 120 days of the notice	Under Section 14. Show cause notice must be issued within 5 years of the relevant date Under Section 14 order shall be issued within 120 days of the notice	Under Section 47, Show cause notice must be issued within 8 years of the relevant date Under Section 47 order shall be issued within 180 days of the notice
Keeping of record	As per Section 24 For six years after the end of tax period	As per Section 17 For six years after the end of tax period	As per Section 27 For ten years after the end of tax period

THANK YOU

