IN THE HIGH COURT OF SINDH, KARACHI

C.P.No.D-2358 of 2015

PRESENT:

MR. JUSTICE AQEEL AHMED ABBASI
MR. JUSTICE ARSHAD HUSSAIN KHAN

Petitioner	**ORI-TECH, Oils Private Limited** **Through Mr. Emad-ul-Hassan, Advocate.**
Respondent	**The Chief Commissioner, Inland Revenue, Regional Tax Office-I, Karachi.** **Through Mr. Muhammad Aqeel Qureshi, Advocate.**
Date of Hg:	**08-02-2017**
Date of Judgement	**08.05.2017**

JUDGMENT

ARSHAD HUSSAIN KHAN, J: The Petitioner through instant constitutional petition has sought following relief(s):-

- *Declare that the petitioner is engaged in the 'manufacturing process' through Toll Manufacturer' with the Tax Authorities.*
- *Permanently and till disposal of the instant petition, restrain the respondents, their servants, agents, attorneys, assignees or any other person acting under their behalf, from taking any action for levy or recovery of Additional Sales Tax under Rule 58-B of Sales Tax Special Procedure Rules, 2007 from the petitioner.*
- *Cost of petition may be awarded.*
- *Any other relief, which this Hon'ble Court may deem fit and proper under the circumstances may be awarded.*

2. Brief facts leading to the filing of instant petition as stated therein are that the petitioner is a private limited company incorporated in October, 2012, and engaged in the business of manufacturing of petroleum products under the brand name of 'Ori-Tech' through Toll Manufacturing Arrangement. The petitioner's brand and its trademark with NTN No.4039712-2, is registered with Sales Tax Authorities having Registration No.17004039712-12. It is averred that petitioner imports raw-material, that is, additives and base-oil for manufacturing of lubricants and for the purpose of manufacturing of the lubricant, that is, finished product the petitioner

entered into a Toll Blending Agreement with M/s. Orient Oils (Pvt.) Limited (Vendor) on 05.11.2012 to utilize Vendor's blending and testing facilities, for the blending of the petitioner's lubricating oils, as per the formulations / specifications advised by the petitioner from time to time. The petitioner provides raw-materials, that is, additives and base-oil along with packing material to vendor and the vendor is paid only a cost of blending (conversion charges) @ Rs.7.00/- per liter and petitioner issues sales tax invoice to its customers, only at the time of sale of the finished product and not to the vendor as the relationship is of 'Principal' and 'Vendor'. It is also averred that petitioner after incorporation and before commencement of the operations applied for registration with the sales tax authorities through PRAL as Manufacturer / Importer & Wholesaler on 15.11.2012, however, respondent registered the petitioner only as Importer, Wholesaler. On 23.01.2013, the petitioner wrote a letter to the Manager Registration Central Registration Office, PRAL (respondent No.1) for registering the petitioner's company as manufacturer. The respondent without any cogent reasons rejected the said application. The petitioner, thereafter held a meeting on 07.03.2013 with the Chief Commissioner, Inland Revenue RTO-1, Karachi (respondent No.2) for resolution of the issue of registration as manufacturer and pursuant to the discussion with the respondent No.2, the petitioner on 21.03.2013 wrote a letter to the Member Inland Revenue Operations FBR (respondent No.4) requesting therein to register the petitioner's company as manufacturer. Pursuant to the advice by the respondents the petitioner on 26.07.2013 once again applied for change in particulars, that is, registration as manufacturer as the petitioner is engaged in the business of manufacturing of petroleum products through Toll Manufacturing Arrangements, that is, utilizing the vendor's facilities. The said application was also rejected without assigning any reasons and the respondent No.1 informed the said rejection through email dated 18.09.2013. Further averred that the petitioner, after the said rejection, when visited the respondent No.2 to ascertain reasons for the said rejection, he was directed to contact Central Registration Office (CRO) for obtaining the rejection report for which petitioner applied in writing but neither any response was

given nor the rejection report was provided. The petitioner, though in October, 2013, had filed an appeal with the Commissioner Inland Revenue (Appeals-III), Karachi against the rejection of petitioner's application, however, the said appeal was subsequently withdrawn as there is no provision in Sales Tax Act to file appeal before the Commissioner (Appeals) against the rejection report of PRAL. After withdrawal of the appeal from the Commissioner (Appeals), the petitioner on 01.11.2013 filed Complaint bearing No.525/KHI/ST(274)/1677/2013 with the learned Federal Tax Ombudsman (FTO) against not disclosing the reasons for rejection of petitioner's application as required under Rule 5(3) of the Sales Tax Rules, 2006, however, on the assurance of the respondent that petitioner's application will be duly considered after verification, the petitioner withdrawn said complaint. Thereafter, petitioner received a letter dated 16.12.2013 from the office of respondent No.2 informing the reasons that as there is no machine installed at the petitioner's premises as well as the toll manufacturing arrangement is not mentioned in the Memorandum, hence the petitioner was not registered as Manufacturer. In response to the said letter, the petitioner through its letter dated 19.12.2013 to the respondent No.2, explained that under the Memorandum of Association the petitioner is entitled for manufacture of petroleum products itself or enter into agreements in this respect. After explaining the position, the petitioner on 31.03.2014 again applied to the respondent No.1 for registration as Manufacturer. In response to the above said application, the petitioner received a letter dated 22.04.2014 whereby the petitioner was called upon to provide certain information for verification of the business premises under Sales Tax Rules, 2006. The petitioner submitted required information to the respondent, however, the petitioner's application was again rejected. The petitioner having no other alternate remedy filed the present petition.

3. Upon notice of the present petition, the respondent No.2 filed its para-wise comments, wherein while refuting the allegations in the memo of petition, it is stated that the application of the petitioner for change of particulars/addition of manufacturing category through

Token No.34177728 at their declared premises located at 204/A, 2nd Floor, Block -2, PECHS, was forwarded to Local Registration Office [LRO] with the remarks "RTO to verify the manufacturing premises". Accordingly, physical verification was conducted at declared premises whereat neither machinery was found installed nor any manufacturing of goods were found in process. Resultantly, a report as 'not verified' was submitted to CRO. Further stated that the terms and conditions of Toll Bending Agreement are not clear to establish the right of the petitioner on the goods being manufactured by the vendor as M/s. Orient Oils (Pvt.) Ltd. and the vendor is also registered as manufacturer/importer/exporter and is involved in manufacturing and supply of same product. Further stated that during the course of scrutiny of the Memorandum of Association, it was found that there was no clause, which authorizes the petitioner company to enter into agreement for toll manufacturing or get its goods manufactured from any other concern. The clauses 1 to 9 of Memorandum provides the details of objects for which company has been established and nothing has been mentioned in these clauses regarding manufacturing of goods from others/toll manufacturing. It is also stated that the prime function of the department is to safeguard the government revenue and accordingly, it is very much relevant to put on record the impact on tax collection. Further stated that perusal of clauses 1 to 9 of Memorandum of Association of the petitioner reveals that applicant will conduct business (import/local) in variety of commodities/items, therefore, his request for sales tax registration as manufacture of refined petroleum products without any manufacturing facility cannot be entertained as it will adversely affect the revenue collection and will award undue advantage to the petitioner. It is also stated that the petitioner failed to establish the status as "manufacturer" therefore, after considering all the facts of the case, the petitioner's application for registration as "manufacturer" was rightly rejected. The respondent also sought dismissal of the present petition being frivolous.

4. The learned counsel for the petitioner during the course of his arguments while re-iterating the contents of the petition has contended that as per the definition of "manufacturer" as contained

in Section 2(17)(c) of the Sales Tax Act, 1990, the petitioner is a manufacturer as it owns, holds, claims, uses patents, proprietary, and other right to goods, being manufactured at the vendor's premises having such facility. Per learned counsel, petitioner being the manufacturer, fixes the retail price of the manufactured goods as per the terms of Section 2(27) of the Sales Tax Act, 1990, whereas, according to learned counsel, as per the Federal Excise General Order No. 02 of 2008 dated 06.10.2008 both the Principal, who owns and supplies the raw-material, as well as the vendor (Toll Manufacturer) both fall under the definition of manufacturer. However, the vendor is liable to pay Federal Excise Duty [FED] only on his gross conversion charges, while the Principal is required to pay the duty on the basis of the retail price. It has been further contended that petitioner sells the refined petroleum products, which are manufactured from the raw materials imported by the petitioner and as such at the time of import the petitioner cannot be termed as wholesaler or retailer. It is also contended that the raw material, that is, additives and base-oil for manufacturing of the finished product imported are not sold in its form, but are further manufactured/processed, that is, the raw-material changes shape into a different product using a manufacturing process. Further contended that blending and converting the raw material into finished lubricants for industrial use is a process of manufacture or produce as per Section 2(16)(c) of the Sales Tax Act, 1990. Further contended that the manufacturing process has been defined under Section 2(g) of the Factories Act, 1934 under which the manufacturing of lubricants by the petitioner using the vendor's plant and machinery is also manufacturing. Further contended that the petitioner like commercial importers does not supply the raw material to the vendor; there is no disposal, neither any price is charged from the vendor on the basis of Value Addition in terms of Section 2(33) of the Sales Tax Act, 1990. It is also contended that the raw material being processed under toll arrangement is in-house consumption and not a sale transaction like is the case with other manufacturers, wherein the concept of value-addition works. At the time of supply of the raw material to the vendor, no sales tax is charged, as it is not a taxable supply in terms of Section 2(41) of the Sales Tax Act, 1990 i.e. only raw-material is

provided without any payment involved for the raw-material and later on the raw material is received back in the form of the finished product, that is, the lubricant. Further contended that as per the definition of "Wholesaler" given under Section 2(47) of the Sales Tax Act, 1990, the petitioner is not a wholesaler as it is not buying the finished goods in wholesales and selling the same in bulk, but is buying raw-material just like any other manufacturer and converting it into finished lubricants using manufacturing facilities of the vendor. Furthermore, Sub-clause (1) of Clause-III of the Memorandum of Association clearly authorizes the company to engage in manufacturing activity of specially products including refined petroleum products. Further Clause 10(xi) of the Memorandum specifically authorizes the company to enter into contracts, hence the petitioner can enter into manufacturing of petroleum products through toll manufacturing arrangements. As per the provisions of Section 2(13) of the Sales Tax Act, 1990, petitioner is importer but not a commercial importer, hence can be liable for payment of the normal sales tax under Section 3(1)(b) of the Sales Tax Act, 1990, but is being prejudiced by levy of the Additional Sales Tax of 3% under Chapter-X of the Sales Tax Special Procedure Rules, 2007, read with Section 7A(1) of the Sales Tax Act, 1990, that is, paying a total of 20% (17% normal + 3% additional) at the import stage, while the manufacturers as well as service providers are exempt from such levy in terms of the proviso to rule 58-B of the Sales Tax Special Procedure Rules, 2007, or paying only 17% normal Sales Tax. That the objective of the Additional Sales Tax on the pretext of value-addition was initially for commercial importer and was optional, that is, the minimum value addition had to be declared to obtain waiver from the requirement of audit or scrutiny of records as per the provisions of Section 7A(2) of the Sales Tax Act, 1990. Further contended that under Rule 5(4) read with rule 7(2) of Sales Tax Rules, 2006, the purpose of verification of the manufacturing facility is to check that a manufacturing process is being applied for conversion of the raw material into finished goods. It is not necessary that a manufacturer must own manufacturing facility as according to learned counsel, manufacturer is a person, who is engaged in manufacturing process

whether himself or through someone else, i.e. through vendors. While concluding the arguments, learned counsel contented that the petitioner is a manufacturer for all legal purposes, hence entitled to Sale Tax Registration as a Manufacturer.

5. On the other hand, learned counsel for the respondents during the course of his arguments, while reiterating the contents of the para-wise comments and referring to various provisions of Sales Tax Act, 1990, has contended that since the petitioner has failed to establish its status as manufacturer, therefore, the respondent / department after having examined the entire facts of petitioner's case, has rightly rejected the petitioner's application seeking registration as a Manufacturer. Per learned counsel, Toll Manufacturing cannot be considered as self-manufacturing.

6. We have heard the learned counsel for the parties and perused the record, and have also examined the relevant law on the point subject controversy.

7. Before dilating upon the concept of Manufacturing and Toll Manufacturing, it will be appropriate to reproduce hereunder, the various definitions of related terms as defined under the Sales Tax Act 1990, Federal Excise Act 2005 & Sales Tax Registration Rules. The relevant provisions for the purposes of just decision on the subject controversy, are reproduced as follows: -

Sales Tax Act 1990

"2. Definitions. ―

(16) **'Manufacture'** or **'produce'** includes –

(a) any process in which an article singly or in combination with other articles, materials, components, is either converted into another distinct article or product or is so changed, transformed or reshaped that it becomes capable of being put to use differently or distinctly and includes any process incidental or ancillary to the completion of a manufactured product;

(b) Process of printing, publishing, lithography and engraving; and

(c) process and operations of assembling, mixing, cutting, diluting, bottling, packaging, repacking or preparation of goods in any other manner;

(17) **'manufacturer'** or **'producer'** means a person who engages, whether exclusively or not, in the production or manufacture of goods whether or not the raw material of which

the goods are produced or manufactured are owned by him; and shall include–

(a) a person who by any process or operation assembles, mixes, cuts, dilutes, bottles, packages, repackages or prepares goods by any other manner;

(b) An assignee or trustee in bankruptcy, liquidator, executor, or curator or any manufacturer or producer and any person who disposes of his assets in any fiduciary capacity; and

(c) any person, firm or company which owns, holds, claims or uses any patent, proprietary, or other right to goods being manufactured, whether in his or its name, or on his or its behalf, as the case may be, whether or not such person, firm or company sells, distributes, consigns or otherwise disposes of the goods:

Provided that for the purpose of refund under this Act, only such person shall be treated as manufacturer-cum-exporter who owns or has his own manufacturing facility to manufacture or produce the goods exported or to be exported;

(27) **'retail price'**, with reference to the Third Schedule, means the price fixed by the manufacturer, inclusive of all duties, charges and taxes (other than sales tax) at which any particular brand or variety of any article should be sold to the general body of consumers or, if more than one such price is so fixed for the same brand or variety, the highest of such price;

(33) **'supply'** means a sale or other transfer of the right to dispose of goods as owner, including such sale or transfer under a hire purchase agreement, and also includes: -

(a) Putting to private, business or non-business use of goods produced or manufactured in the course of taxable activity for purposes other than those of making a taxable supply;

(b) Auction or disposal of goods to satisfy a debt owed by a person; and

(c) Possession of taxable goods held immediately before a person ceases to be a registered person:

Provided that the Federal Government, may by notification in the official Gazette, specify such other transactions which shall or shall not constitute supply;

(41) **'taxable supply'** means a supply of taxable goods made by an importer, manufacturer, wholesaler (including dealer), distributor or retailer other than a supply of goods which is exempt under section 13 and includes a supply of goods chargeable to tax at the rate of zero per cent under section 4

Sales Tax Registration Rule 2006:

5. Application for registration. — (1) A person required to be registered under the Act shall, before making any taxable supplies, apply on the computerized system through owner, authorized member or partner or authorized director, as the case may be, in the Form STR-1, as annexed to these rules. Such application will specify the RTO in whose jurisdiction the registration is sought, as per criteria given below, namely: -

(a) in case of listed or unlisted public limited company, the place where the registered office is located;
(b) in case of other companies—
(i) if the company is primarily engaged in manufacture or processing, the place where the factory is situated; and
(ii) if the company is primarily engaged in business other than manufacture or processing the place where main business activities are actually carried on;
(c) in case of a person not incorporated, the jurisdiction where the business is actually carried on, and
(d) In case of a person not incorporated, having a single manufacturing unit and whose business premises and manufacturing unit are located in different areas, the jurisdiction where the manufacturing unit is located:

Provided that the jurisdiction of Large Taxpayers Units shall remain as specified by the Board:
Provided further that the Federal Board of Revenue may transfer the registration of any registered person to a jurisdiction where the place of business or registered office or manufacturing unit is located.

(2) The applicant shall submit the following documents namely: -

(a) CNIC of all owners, members, partners or directors, as the case may be, and the representative, if any, and in case of non-residents, their passports;
(b) In case of a company or registered AOP, the Registration or Incorporation Certificate, along with Form III or Form A as prescribed in the Companies Ordinance, 1984 (XLVII of 1984);
(c) In case of a partnership, the partnership deed, if available;
(d) Bank account certificate issued by the bank, in the name of the business;
(e) Lease or rent agreement, if the premises is on rent, along with CNIC of the owner of the premises;
(f) Ownership documents of the premises, such as registered sale deed or registered transfer deed;
(g) Latest utility bills (electricity, gas, land-line telephone, and post-paid mobile phones, as the case may be);
(h) List of machinery installed, in case of manufacturer;
(i) distribution certificate from the principal showing distributorship or dealership, in case of distributor or dealer;
(j) balance sheet/statement of affairs/equity of the business;
(k) particulars of all branches in case of multiple branches at various locations; and
(l) particulars of all franchise holders in case of national or international franchise, if applicable.

Federal Excise Act 2005

2. Definitions. – In this Act, unless there is anything repugnant in the subject or context, —

(16) **Manufacture** includes, – **(a)** any process incidental or ancillary to the completion of a manufactured product;
(b) any process of re-manufacture, remaking, reconditioning or repair and the processes of packing or repacking such product, and, in relation to tobacco,

> includes the preparation of cigarettes, cigars, cheroots, biris, cigarette and pipe or hookah tobacco, chewing tobacco or snuff, or preparation of unmanufactured tobacco by drying, cutting and thrashing of raw tobacco, and the word "manufacturer" shall be construed accordingly and shall include,–
>
> (i) any person who employs hired labour in the production or manufacture of goods; or
>
> (ii) any person who engages in the production or manufacture of goods on his own account if such goods are intended for sale; and
>
> **(c)** any person who, whether or not he carries out any process of manufacture himself or through his employees or any other person, gets any process of manufacture carried out on his behalf by any person who is not in his employment: Provided that any person so dealing in goods shall be deemed to have manufactured for all purposes of this Act, such goods in which he deals in any capacity whatever;

> **Toll Manufacturing** is defined as under:
>
> An arrangement in which a company (which has specialized equipment) process raw material or semi-finished goods for another company. Also called toll processing. Ref:htt:/www.businessdictionary.com/definition/toll-manufacturing.html

8. From perusal of the record, it appears that the petitioner had applied for sales tax registration as Manufacturer / Importer and Wholesaler, however, the petitioner was registered only as Importer and wholesaler. Upon which the petitioner applied for its sale tax registration as manufacturer but its application was turned down by the respondent on the ground that neither machinery was found installed nor any manufacturing of goods were found in process at the declared premises. Record also reveals that the petitioner is engaged in the manufacturing of its product, that is, lubricant in the brand name of 'Ori-Tech' through toll manufacturing arrangement and in this regard entered into a Toll Blending agreement with M/s. Orient Oil (Pvt.) Ltd. for the sake of ready reference relevant clauses of the said Toll blending agreement are reproduced as under:

> "Whereas Principal is desirous of utilizing Vendor's Blending and testing facilities for the blending of Principal's Lubricating Oils, in accordance with standard blending procedure and Principal relies in Vendor's technical knowledge and organizational capabilities for the successful performance of the blending of Finished Lubricating Oils as per Formulation/specifications advised by the Principal from time to time.

Whereas Vendor in order to blend Finished Lubricating Oils for Principal has agreed to supply or utilize the Raw-Materials provided by the Principal for blending of their brands in safe, efficient and economical manner.

And whereas the parties have agreed that blending of Lubricating Oils by Vendor on the order of Principal shall take place on the terms and conditions given hereunder:

- Principal will place blending order on Vendor, giving formulations/specifications/API quality level/grades along with quantities/volume for blending of Lubricating Oils together with up-liftmen schedule on monthly and weekly basis.
- Principal will provide Lube Base Oils, additives, Empty Drums/Cans etc. to Vendor's plant/Factory at Korangi Industrial Area, Karachi whereas Vendor will provide even Lube Base Oils if desired by the Principal and storage space for the material provided.
- Vendor will ensure that Lubricating Oils are blended strictly in accordance with the Formulation/specification /API quality level/color specified by the Principal in the formulation sheet. Vendor will take appropriate care to keep Empties, Additives and all material supplied by principal in good condition.
- Vendor/Principal will maintain record of inventory of materials supplied by principal, which will be reconciled on monthly basis or whenever required movement of inventory and balance in hand.
- Principal will have a right to collect samples at any stage of blending or packaging and have it tested jointly at the testing facilities of Vendor or any outside laboratory capable of conducting tests on Lubricating Oils. In case any dispute regarding quality, joint sampling will be carried out and samples will be sent to HDIP, whose results will be final and binding on both Vendor & Principal. In case of product is found to be Off-specification in HDIP, Principal will have a right to reject the complete batch.
- Since the Toll Blending falls under the definition of manufacturing, therefore Sales Tax is payable at the specified rates by the Vendor to Federal Board of Revenue (FBR) and on the actual consideration in money received i.e. Gross Conversion Charges/Blending Fee and in case of Lube Base Oils is provided by the Vendor, the cost of Lube Base Oils in the blend of finished Lubricating Oils shall be charged in addition to the Gross Conversion Charges/ Blending Fee.

    - Cost of blending =Rs.7.00 per Liter (Gross Conversion Charges/Blending Fee)
    - Cost of Lube Base Oils in the blend of Finished Lubricating Oils = In case of Lube Base oil is provided by the Vendor
    - Sales Tax = at the specified rate"

[Underlining is to add emphasis]

9. The record of the present case also shows that petitioner, exclusively for the purposes of manufacturing of its own products, used to import raw materials, that is, additives and base oil. The petitioner provides said raw material together with packing materials to the vendor M/s. Orient Oil (Pvt.) Ltd. to manufacture petitioner's products for consideration i.e. fees / charges as mentioned in the toll

manufacturing agreement. The vendor performs manufacturing process to manufacture the product of the petitioner strictly as per the specification/formulation provided by the petitioner. The petitioner being manufacturer of its products owns the proprietary rights over its brand name and fixes the retail price and sell the finished product, hence the petitioner is engaged in the taxable supply being manufacturer. As is clear from Section 3 of the Act, sales tax can only be charged/levied against a person who makes a taxable supply which has been defined in Section 2(41) of the Act, which specifically and unequivocally provides that it is supply of taxable goods by, inter alia, a manufacturer. According to Section 2(17) of the Act a manufacturer is a person who engages in the manufacture of goods as per the definition of manufacture provided in the act. It is settled that a definition clause provides a foundational basis while construing the provisions of law and reference to ordinary dictionary meaning of the word is avoided. The definition given in the Act should be so construed as not to be repugnant to the context and would not defeat or enable the defeating of the purpose of the enactment. It must be read in its context, keeping in view the scheme of the statute and the remedy intended by it. Furthermore, Taxing laws are not to be extended by implication beyond the clear import of the language used. To hold otherwise, would violate another principle of interpretation of taxing statutes that tax laws should be construed strictly, whereas, in case of any ambiguity or doubt in the charge, it should be resolved in favour of the subject citizen and against the revenue. Reference in this regard can be made to the case of *CHAIRMAN, FEDERAL BOARD OF REVENUE, ISLAMABAD Vs. Messrs AL-TECHNIQUE CORPORATION OF PAKISTAN LTD. and others* **(PLD 2017 Supreme Court 99).**

10. A bare reading of the definition of Section 2 (17) suggests that manufacturer is a person who engages, whether exclusively or not, in the production or manufacture of goods whether or not the raw material of which the goods are produced or manufactured are owned by him and shall include a person any person, firm or company which owns, holds, claims or uses any patent, proprietary,

or other right to goods being manufactured, whether in his or its name, or on his or its behalf, as the case may be, whether or not such person, firm or company sells, distributes, consigns or otherwise disposes of the goods. There appears no provision in sales tax act, which could exclude a person who does not possess its own facility of manufacturing and get his products manufactured from toll manufacturing from claiming himself as manufacturer. Conversely, the Federal Excise General Order No.2 of 2008 dated 06.10.2008, issued by Central Board of Revenue in respect of Federal Excise duty on the goods produced by the vendors (Toll Manufacturers) from the raw material supplied by the principals, states that both vendor and the principal fall in purview of the definition of manufacturer. For the sake of ready reference, the Federal Excise General Order No.2 of 2008 dated 06.10.2008, is reproduced as under:-

Government of Pakistan
(Revenue Division)
Central Board of Revenue

C.No. 3(15) ST-L&P/99(Pt-I), Islamabad, the 6th October 2008
Federal Excise General Order No. 02/2008

Subject: FEDERAL EXCISE DUTY ON GOODS PRODUCED BY VENDORS (TOLL MANUFACTURERS) FROM THE RAW MATERIALS SUPPLIED BY THE PRINCIPALS

Federal Excise General Order No.2 of 2005 dated 15.08.2005, in its para (vi), addresses some issues relating to payment of federal excise duty (FED) in cases where a vendor (toll manufacturer) manufactures goods from the raw material provided by the principal. In view of further queries received in this respect, following clarifications are made:

- Both vendor and principal fall in purview of the definition of manufacturer as provided in the Federal Excise Act 2005 and both shall discharge their liability to pay duty under the law.

- The assessable value for excise duty payable by the vendor shall be the actual consideration in money received i.e. the gross conversion charges received.

- The aforesaid principle will also apply to cases where the goods so manufactured by the vendor are otherwise chargeable to FED on the basis of retail price. The principal will pay duty on the basis retail price, inclusive of all duties, charges and taxes other than sales tax, whereas the vendor will be liable to pay duty only on his gross conversion charges.

- The vendors shall not be entitled to any adjustment in case of duty-paid input goods used in the manufacturing process are owned by

the principal. However, the vendor shall be adjusted FED paid by him on direct input goods which are purchased by him on payment of duty.

- The principal shall be entitled to adjust FED paid by him to the vendor against conversion charges as well as the duty paid by him on the raw materials owned by him, as were supplied to the vendor for manufacturing, against the final liability of the principal.

- The vendors shall comply with all the applicable provisions of the Federal Excise law and the principals will not be required to pay any duty on the movement of such raw materials or inputs from their possession to the vendors for the purposes of manufacture or production of excisable products on their behalf though they will properly account for such movements in their records.

- The aforesaid procedures shall also be applicable to Special Excise Duty (SED) payable under SRO 655(I)2007 dated 29.06.2007. However, as regards adjustment, it is clarified that adjustment of SED can only be made against SED and the same principle applies to FED payable under First Schedule of Federal Excise Act, 2005.

(Abdul Hameed Memon)
Secretary (ST&FE-L&P)"

[Underlining is to add emphasis]

11. It may be pointed out at this juncture that in today's corporate environment, many companies consider toll manufacturing arrangements in emerging market countries to reduce costs while maintaining access to a highly educated and technologically advanced work force. Toll manufacturing is generally a preferred route opted by manufacturing companies to start with because of inherent advantages at both ends viz. No high investment at local entity level, provision of basic raw materials by principal manufacturer, non-local sourcing requirements, etc. Under a toll manufacturing arrangement, the principal manufacturer engages a local entity (often termed as Toller) owning the manufacturing facility, to manufacture / process raw materials /semi-finished goods for a manufacturing / processing fee. The principal manufacturer shares its technology with the local entity and also monitors the quality standards through its employees.

12. Similar controversy came up for decision by a Divisional Bench of this Court in the case of ***Messrs Amie Investment (Pvt) Ltd. vs. Additional Collector-II and 4 others (2006 PTD 1459),*** wherein, Divisional Bench of this Court while examining the nature of the transaction relating to manufacturing for 3rd party has been pleased to hold as under:-

"The transaction between the appellants and its Principal can by no stretch of imagination be termed as sale or lease as such it requires no deliberations. Now it is to be examined as to whether the transaction, as above, amounts to "other disposition of goods in or furtherance, of business carried out for consideration". There can be no denial of the fact that the business of the Appellant is carried out for consideration, but the question which needs to be examined is as to whether the returning of goods by the Appellants after processing would amount to "disposition of goods". The term "disposition" has not been defined in the Act and the ordinary meaning of the word `disposition' as defined in various Dictionaries are as under:-

Black's Law Dictionary (Six Edition)	*'act' of disposing, transferring to the care or the possession of another. The parting with, alienation with or giving up property'.*
Concise Oxford Dictionary (10th Edition)	*The action of disposing or transferring property or money to someone, in particular by bequest. The power to deal with something as one pleases'.*

The expression `disposition' further was considered by the Supreme Court of India in the cases of Goli Eswarian v. Commissioner of Gift Tax AIR 1970 SC 1722 and it was held that `the word disposition is not a term of law'. Further it has no precise meaning. Its meaning has to be gathered from the context in which it is used".

"The processing of goods by the Appellant surely is a manufacturing process. However, the pre-condition to include the goods acquired, produced or manufactured in the course of business is the `use' of the goods by the person who acquired, produced or manufactured the goods and in the present case the Appellant did not use the goods to attract the consequences of supply".

"The logical consequence is that the Sales Tax Department has wrongly received the sale tax on conversion charges which is in the nature of consideration for providing services. The Department has no moral or legal justification to retain this amount paid by appellant on account of ignorance of law, which should be returned/refunded."

13. Reverting back to the case in hand, from the facts of the present case it is manifest that the petitioner gets its products manufactured through toll manufacturing by providing them its raw and packing materials. Furthermore, the petitioner is also having the proprietary rights over its brand name and it fixes the retail price and sells the finished product, thus keeping in view all the aforementioned definitions in their legal and usual context makes it clear that the petitioner falls within the meaning of "Manufacturer"

as provided in Section 2(17) and is making a 'taxable supply' as per Section 2(41) Sales Tax Act 1990.

14. The upshot of the above discussion is that we are of the considered view that the petitioner is engaged in the manufacturing of its products through Toll manufacturing arrangement and thus eligible to be registered as ‘Manufacturer’ with Tax authority. Accordingly, this petition is allowed.

JUDGE

JUDGE

Karachi
Dated: 08 .05.2017

Jamil//*