IN THE HIGH COURT OF SINDH AT KARACHI

Special Sales Tax Appeal No.148 of 2005

Present:
Mr. Justice Irfan Saadat Khan
Mr. Justice Zulfiqar Ahmad Khan

The Collector of Customs.....Appellant.
Vs.
M/s. Matiari Sugar Mills.....Respondent.

Date of hearing: 28.01.2021 .

For the appellant: Mr. Shakeel Ahmed, Advocate. .

For the respondent: Nemo. .

J U D G M E N T

IRFAN SAADAT KHAN, J. The instant Special Sales Tax Appeal **(SSTA)** was admitted for regular hearing vide order dated 23.12.2005 to consider the following question of law:

> *"Whether the Customs, Excise and Sales Tax Appellate Tribunal was justified in holding that the aforesaid supply to the residential colony of the registered person is a part of manufacturing process and shall be deemed as taxable activity in terms of Section 2(35) of the Sales Tax Act 1990?"*

2. Briefly stated, the facts of the case are that the respondent is a Sugar Mill engaged in manufacturing of sugar. During the course of the audit it revealed that input adjustment amounting to Rs.37,128/- on account of the electricity charges consumed in residential colony of the mill was claimed. The department was of the view that input adjustment of the said electricity consumed was not admissible under the provisions of Section 8(1)(a) of the Sales Tax Act, 1990 **(the Act)**, hence called upon the respondent, vide

Show Cause Notice dated 19.07.2002, to show as to why the said amount may not be disallowed in the assessment of the mill. Reply whereof was submitted by the respondent however the same was not found satisfactory and thereafter vide Sales Tax Order-in-Original No.167 of 2002, dated 25.10.2002, the said amount of Rs.37,128/- was disallowed and a penalty of Rs.5,000/- was also imposed upon the respondent. An appeal thereafter was filed against the said order and the Collector of Appeals, vide order dated 10.02.2003, dismissed the appeal filed by the respondent. Thereafter an appeal was preferred before the Customs, Excise & Sales Tax Appellate Tribunal **(the Tribunal)** bearing Sales Tax Appeal No.K.75/03/9786 and the Tribunal was pleased to allow the appeal of the respondent, vide order dated 19.12.2003, by setting aside the Order-in-Original and Order-in-Appeal. It is against this order of the Tribunal that the present SSTA has been filed.

3. Mr. Shakeel Ahmed, Advocate, has appeared on behalf of the department (appellant) and stated that the Tribunal was not justified in directing that the respondent was entitled to claim input tax on the electricity consumed in residential colony of the mill's labourers. He stated that since the said electricity was not used in any manufacturing activity hence as per the relevant provisions of the law, sales tax input adjustment was not allowable to the respondent. The learned counsel in this regard invited our attention to Section 2(35) and Section 8(1)(a) of the Act as well as SRO 124(I)/2000 and SRO 344(I)/2002, dated 15.06.2002, to show that electricity power consumed on non-taxable activity was not allowable and since, according to him, the electricity was consumed in the residential colony of the mill by the respondent, the said electricity consumed by no stretch of imagination could be considered as taxable activity, hence, the

Tribunal erred in allowing the appeal by observing that supplying electricity to the labourers who were part of the manufacturing process will be deemed as taxable activity and the appellant was entitled to deduct input tax in respect of the electricity consumed in this regard. He, therefore, states that answer to the question raised may be given in "Negative" i.e. in favour of the department and against the respondent.

4. Nobody has appeared on behalf of the respondent. However, the objections filed by the respondent previously were taken into consideration while giving the present judgment.

5. We have heard Mr. Shakeel at some length and have also perused the record.

6. Before proceeding further, we deem it expedient to reproduce herein below the relevant provisions of the law applicable in the instant matter:

> ***Section 2(35) of the Sales Tax Act, 1990:***
>
> ***"taxable activity"****, means any economic activity carried on by a person whether or not for profit, and includes--*
>
> *(a) an activity carried on in the form of a business, trade or manufacture;*
>
> *(b) an activity that involves the supply of goods, the rendering or providing of services, or both to another person;*
>
> *(c) a one-off adventure or concern in the nature of a trade; and*
>
> *(d) anything done or undertaken during the commencement or termination of the economic activity,*
>
> *but does not include—*
>
> *(a) the activities of an employee providing services in that capacity to an employer;*
>
> *(b) an activity carried on by an individual as a private recreational pursuit or hobby; and*

(c) an activity carried on by a person other than an individual which, if carried on by an individual, would fall within sub-clause (b).

<u>Section 7 of the Sales Tax Act, 1990:</u>

Determination of tax liability.*--(1) Subject to the provisions of sections 8 and 8B, for the purpose of determining his tax liability in respect of taxable supplies made during a tax period, a registered person shall, subject to the provisions of section 73, be entitled to deduct input tax paid or payable during the tax period for the purpose of taxable supplies made, or to be made, by him from the output tax, excluding the amount of further tax under sub-section (1A) of section 3, that is due from him in respect of that tax period and to make such other adjustments as are specified in Section 9:*

Provided that where a registered person did not deduct input tax within the relevant period, he may claim such tax in the return for any of the six succeeding tax periods.

(2) A registered person shall not be entitled to deduct input tax from output tax unless,--

(i) in case of a claim for input tax in respect of a taxable supply made, he holds a tax invoice in his name and bearing his registration number, in respect of such supply, or in case of supply of electricity or gas, a bill bearing his registration number and the address where the connection is installed:

Provided that from the date to be notified by the Board in this respect, in addition to above, if the supplier has not declared such supply in his return or he has not paid amount of tax due as indicated in his return;

(ii) in case of goods imported into Pakistan, he holds bill of entry or goods declaration in his name and showing his sales tax registration number, duly cleared by the customs under section 79, section 81 or section 104 of the Customs Act, 1969 (IV of 1969);

(iii) in case of goods purchased in auction, he holds a treasury challan, in his name and bearing his registration number, showing payment of sales tax;

*[(iv) * * *]*

(3) Notwithstanding anything in sub-sections (1) and (2), the Board, with the approval of the Federal Minister-in-charge, may, by a special order, subject to such conditions, limitations or restrictions as may be specified therein allow a registered person to deduct input tax paid by him from the output tax determined or to be determined as due from him under this Act.

(4) Notwithstanding anything contained in this Act or rules made thereunder, the Federal Government may, by notification in the official Gazette, subject to such conditions, limitations or restrictions as may be specified therein, allow a registered person or class of persons to deduct such amount of input tax from the output tax as may be specified in the said notification.

(5) Notwithstanding anything contained in this Act or the rules made thereunder, the Board, by notification in the official Gazette, may impose restrictions on wastage of material on which input tax has been claimed in respect of the goods or class of goods.

Section 8(1)(a) of the Sales Tax Act, 1990:

Tax credit not allowed.*--(1) Notwithstanding anything contained in this Act, a registered person shall not be entitled to reclaim or deduct input tax paid on—*

(a) the goods or services used or to be used for any purpose other than for taxable supplied made or to be made by him;

S.R.O. 124(I)/2000 *--- Input Tax Adjustment against Electricity Charges: - In case, a registered consumer is consuming Electric power for both the taxable as well as non-taxable activity and he is in a position to ascertain the correct amount of Electric power consumed in such taxable activity and non-taxable activity separately, he shall be entitled to claim input tax adjustment in respect of Electric power consumed for taxable activity in terms of the Apportionment of Input Tax Rules, 1996.*

S.R.O. No.344(I)/2002 *dated: 15-06-2002 says that, "In case, a registered consumer is consuming electric power for both the taxable as well as non-taxable activity, he shall ascertain the correct amount of Electric power consumed in taxable activity and adjust the input tax in accordance with the Apportionment of Input Tax Rules, 1996.*

7. From the facts it is clear that the respondent is engaged in manufacturing of the sugar, which claimed input adjustment on consumption of electricity in the residential colony situated within the premises of the mill. The facts also reveal that the workers residing in the colony were the persons who were directly involved in making the mill workable for its manufacturing activities. It is a settled proposition of law that any tax paid on the manufacturing activity is considered as input of the

taxpayer liable to be adjusted against the output. It has nowhere been shown by the department that the electricity consumed in the colony of the labourers was used outside the mill or for any other purpose but for input claim of the respondent for the electric power consumed in the said residential colony which was spent exclusively on the labourers residing in the colony who were instrumental in the manufacturing activities of the mill. The stance of the department, in our view, is not correct that the amount was spent on a non-taxable activity, as the department has simply failed to prove with cogent material that the amount of electricity consumed in residential colony was either for those who were not engaged in the manufacturing activities or has been consumed outside the mill. It is also a known fact that any amount spent on manufacturing, if not legally inadmissible, is considered to be the part of cost of sales. In the instant matter also the amount of electricity consumed has been included in the cost of manufacturing of goods and hence appears to be in accordance with the legal norms and principles of accountancy.

8. From the reading of above referred provisions of law the only restriction is with regard to adjustment of electricity charges on non-taxable activity. However, in the instant matter the department has failed to prove that the electricity consumed was on any non-taxable activity rather it is an admitted position that the electricity consumed pertains to the residential colony of the labourers, which took active participation in manufacturing of taxable items of the mill and this aspect of the matter has remained uncontroverted. The provisions of law relied upon by Mr. Shakeel, in our view, do not support him rather supports the stance of the respondent that the electric charges consumed in the labourers’ colony is allowable under the provisions of Section 7 of the Act, reproduced supra. The SROs bearing Nos.124 and 344 also do not support the contention of the department as

these SROs talk about disallowance of the electric power on non-taxable activity, whereas the labourers employed in the mill very much take part in the manufacturing of the goods and hence, in our view, the company was entitled to make adjustment of the above referred amount. It may further be noted that "consumer" is the person who uses the power for its own purposes and do not sale the same to others. In the instant case also it is not a case of the department that the electricity has neither been consumed nor has been sold outside the mill, hence for all practical purposes the mill has to be considered as a "consumer of electricity". Had the electricity been consumed either outside the mill or in those areas not engaged in the manufacturing activities it could be said that the electricity has not been consumed in a manufacturing and taxable activity but it is an admitted position that the amount of electricity was consumed within the mill premises in respect of the colony for labourers. At this juncture it would not be out of place to mention that residential quarters in mill's colonies are only given in the occupation of the labourers on temporary basis and the eventual responsibility of settling utility bills remains with the owners of the mill. In most of the cases not even individual electric connections are given to the occupants, as usually supply to entire colony is made through one or two meters or sub-meters that too at non-domestic rates. The very purpose of placing labourers next to a manufacturing facility is to ensure that mill's operations are carried out round the clock achieving efficient production hence directly connected with the manufacture. It may further be noted that only a registered person is entitled to deduct input tax for the taxable supplies made by him. In the instant matter also the amount of electricity consumed on the taxable activity remains for the benefit of the labourers involved directly in the manufacturing process of the mill and hence, in our view, mill could claim the input tax adjustment in the hands

of the company as the above provisions of the law have to be given liberal interpretation rather than pedantic, isolated or narrow meaning.

9. We were also able to lay our hands on a decision given in the case of *Collector Sales Tax and Federal Excise, Peshawar Vs. Messrs Flying Kraft paper Mills (Pvt.)* ***(2020 PTD 776)*** wherein under identical circumstances a Divisional Bench of the Islamabad High Court has observed as under:

> *Keeping in view the above, record has been examined which shows that the residential accommodation to the workers has been provided by the Respondent Company within the premises of the factory which premises have been duly registered with the department for manufacturing activities. These residences in the factory premises have been provided to the workers who are engaged in the process of manufacturing of the taxable goods thus, the cost of consumption of the electricity and gas of these workers used in the accommodation are directly connected with the taxable activity of the Respondent Company and are considered to be a direct manufacturing expenditure in relation to the cost of the goods. Moreover, the meters for the utilities are installed in the Respondent Company's name and at commercial rates which are higher than the residential rates. The respondent company thus while determining its sale tax, deducted input tax paid on the utility bills under section 7(1) of the Sales Tax Act, 1990. Input tax is a tax paid by the registered person on the purchases while the output tax is calculated on sale of goods. The provision of section 7(1) of the Sales Tax Act, 1990, provides the facility to the registered person as a legal right to deduct tax paid on purchases from the tax calculated on the sale of its taxable supplies so that the said registered person may not be vexed twice and saves the taxpayer from unnecessary hardship. Reliance is placed on case titled as Karachi Shipyard and Engineering Works Limited v. Government of Pakistan 2010 PTD 1652. The Hon'ble Supreme Court of Pakistan Court in the case re: Shiekoo Sugar Mills v. Government and Pakistan and others 2001 PTD 2097 = reported as 2001 SCMR 1376 has held that provision of section 7 is a beneficial provision of law in nature providing facility to the registered person to adjust input tax at the time of making payment of output sales tax. Thus the provision of section 7 would be interpreted liberally in favour of the tax payer. Consequently, all the tax invoices in respect of the taxable supplies, including the electricity and gas utility bills, on which the sales tax is paid by Respondent Company, are legally entitled to be adjusted as input tax for determination of tax liability under section 7(1) of the Sales Tax Act, 1990.*

10. The upshot of the above discussion is that in our view the respondent was entitled to claim input adjustment on the amount of the electricity

consumed in the residential colony of the labourers. We, therefore, answer the question raised in the present SSTA in "Affirmative" i.e. against the department and in favour of the respondent.

11. Let a copy of this judgment be sent to the Registrar of the Tribunal for doing the needful in accordance with law.

JUDGE

JUDGE

Karachi:
Dated:______.02.2021.
(Tahseen, PA)