IN THE HIGH COURT OF SINDH, KARACHI

Present: ***Mr. Justice Muhammad Junaid Ghaffar***
Justice Ms. Sana Akram Minhas,

1.	**Income Tax Case No. 10 of 1994**	**M/s. Cotton Export Corporation of Pakistan (Pvt.) Ltd., Karachi. Vs. the Commissioner of Income Tax, Companies-III, Karachi.**
2.	**Income Tax Case No. 11 of 1994**	**M/s. Cotton Export Corporation of Pakistan (Pvt.) Ltd., Karachi. Vs. the Commissioner of Income Tax, Companies-III, Karachi.**
3.	**Income Tax Reference No. 137 of 1994**	**The Commissioner of Income Tax, Central Zone "A", Karachi Vs. M/s. Cotton Export Corporation of Pakistan (Pvt.) Ltd., Karachi.**
4.	**Income Tax Reference No. 95 of 2001**	**M/s. Cotton Export Corporation of Pakistan (Pvt.) Ltd., Karachi Vs. the Commissioner of Income Tax, Companies-III, Karachi.**
5.	**Income Tax Reference No. 193 of 2001**	**M/s. Cotton Export Corporation of Pakistan (Pvt.) Ltd., Karachi Vs. the Commissioner of Income Tax, Companies-III, Karachi.**
6.	**Income Tax Reference No. 194 of 2001**	**M/s. Cotton Export Corporation of Pakistan (Pvt.) Ltd., Karachi Vs. the Commissioner of Income Tax, Companies-III, Karachi.**

Applicant(s) / Respondent in ITR No.137/1994:	**M/s. Cotton Export Corporation of Pakistan (Pvt.) Ltd., Karachi Through Mr. Iqbal Salman Pasha Advocate.**
Respondent(s) / Applicant in ITR No.137/1994:	**The Commissioner of Income Tax, Companies-III, Karachi Through Mr. Faheem Ali Memon & Mr. Muhammad Taseer Khan, Advocates.**
Dates of hearing:	**09.08.2023 & 10.08.2023**
Date of Judgment:	**28.09.2023**

J U D G M E N T

Muhammad Junaid Ghaffar, J: In all listed cases the moot question in common is that "*Whether the subsidy granted by Federal Government to reimburse losses suffered by the tax-payer is a Capital Receipt or a Revenue Receipt".* Besides this, in some of the assessment years, though arguments have been made by the tax-payers Counsel on a subsidiary question; regarding jurisdiction of the Inspecting Additional Commissioner ("**IAC**") to revise the original assessment order under Section 66-A of the repealed Income Tax Ordinance, 1979 ("**Ordinance**") however, the question(s) proposed do not clearly spell out such objection, and would require its proper rephrasing at the conclusion of this opinion.

ITR No. 137 of 1994:

2. In this case assessment years involved are 1978-1979, 1979-1980 & 1980-1981; wherein, the then Income Tax Appellate Tribunal, at Karachi, ("**Tribunal**") vide its common Order dated 14.12.1985 was pleased to decide the controversy in favour of the taxpayer and against the department. The department being aggrieved preferred an application under Section 136(1) Ordinance proposing two questions of law[1] with a prayer that they be referred to the High Court for deciding such questions; The Tribunal while allowing the said request vide order dated 21.2.1987 has referred question No.(i) as proposed, whereas, question No.2 has been rephrased as under; however, learned Counsel for the department under instructions has not pressed the second question. The referred questions read as under: -

i. **Whether on the facts and the circumstances of the case the learned ITAT was justified in holding that the subsidy paid by the Federal Government to the assesse was not a Revenue receipt.**

ii. **Whether on the facts and in the circumstance of the case, the Appellate Tribunal was justified in holding that provision/liability for tax falls within the purview of the expression income retained for meeting working capital requirements as used in Para 'A' of Part-III of First Schedule to the Income-tax Ordinance, 1979, read with Section 10 of it and hence it is to be excluded from the total income for levy of surcharge?**

ITC No.10 & 11 of 1994

3. In the subsequent years i.e. Assessment years 1986-1987 and 1987-1988, the Tribunal had dismissed the taxpayer's appeal vide its order dated 01.09.1992 in respect of the same controversy and even refused their application under Section 136(1) of the Ordinance for a reference to this Court and being aggrieved, the taxpayer filed Income Tax Cases under Section 136(2) of the Ordinance and has proposed two questions, which read as under: -

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[1] (i) Whether on the facts and the circumstances of the case the learned ITAT was justified in holding that the subsidy paid by the Federal Government to the assesse was not a Revenue receipt.
(ii) Whether on the facts and in the circumstance of the case the learned ITAT was justified in holding that surcharge should be restricted only and to the extent of the tax leviable on the difference between assessed and retained income and not on the entire tax levied.

i. **Whether in the facts and circumstances of the cases the learned Tribunal was justified in examining the taxability of subsidy, when this issue was outside the ambit of appeal proceedings and in confirming IAC's action in reopening the assessment under Section 66-A holding the sum in question to be subsidy as against IAC's treatment of the sum taxed to be share of loss and not subsidy?**

ii. **Whether in the facts and circumstances of the case the learned Tribunal was justified in not treating their order of exemption of subsidy for assessment year 1980-81 as a precedent on the ground that the order was passed long after the constitutional amendment made by Article 165-A on 24-2-1985?**

ITR Nos. 95, 193 & 194 of 2001:

4. These cases are in respect of assessment years 1990-1991, 1991-1992 & 1992-1993, wherein, the taxpayer's appeals were dismissed by the Tribunal vide order dated 13.09.2000 by following its order dated 01.09.1992 in respect of assessment years 1986-1987- & 1987-1988. Thereafter their Application under Section 136(1) of the Ordinance was also dismissed vide order dated 14.02.2001; and as a consequence thereof, the tax-payer has approached this Court under Section 136(2) of the Ordinance proposing the following questions of law: -

i. **Whether the subsidy granted by Federal Government to reimburse losses suffered by the applicant corporation is a Capital Receipt or a Revenue Receipt?**

ii. **Whether the learned Appellate Tribunal misdirected itself in law by holding that subsidy granted by the Federal Government to the Applicant Corporation on account of reimbursement of losses suffered by it was Revenue Receipt?**

5. Since the main controversy involved, in essence, is common, we intend to decide all listed cases through this common judgment. Learned Counsel for the taxpayer has contended that insofar as the order passed under Section 66-A of the Ordinance (*relevant only in ITC Nos.10 & 11 of 1994*) is concerned, the same was done without lawful authority and jurisdiction as it was neither a case of any erroneous assessment; nor it was prejudicial to the interest of the Revenue; hence could not have been revised or altered in terms of Section 66-A of the Ordinance and in support he has relied upon various precedents by arguing that IAC had no power to reopen the original assessment and pass the orders in question. As to merits of the case and subsidy granted by the Federal Government to reimburse

the losses suffered by the taxpayer, he has contended that the same was a capital receipt and not a receipt as a trading Revenue; hence was not liable to be taxed. According to him no conditions were attached to such subsidy; nor it falls in any of the heads of income under Section 15 of the Ordinance, and therefore, could not have been taxed. Per learned Counsel it was a voluntary payment by the Federal Government; hence was not taxable. He has relied upon a number of reported[2] and unreported[3] judgments of the Courts.

6. On the other hand, the department's Counsel has contended that insofar as the powers of IAC under Section 66-A of the Ordinance are concerned, the Tribunal has explained in detail that in passing the original assessment order, the IAC had no role; whereas, the order was not only erroneous; but also prejudicial to the interest of the Revenue; therefore, IAC was fully justified in invoking Section 66-A ibid. According to him, even in a return of loss, wherein no tax has to be paid, an erroneous assessment would be prejudicial to the interest of Revenue inasmuch the carry forward loss reduces the liability in the subsequent years; and therefore, both the conditions are simultaneously fulfilled and there is no reason not to invoke and exercise powers under Section 66-A of the Ordinance in such cases. As to the merits of the case he has contended that the arrangement was obligatory on the part of the Government and was also on regular basis; hence it was a Revenue Receipt liable to be taxed. He has further argued that there was a clear nexus between the subsidy paid by the Federal Government and the losses suffered by the taxpayer; hence it is to be treated as Revenue Receipt liable to tax. As to the observations of the Tribunal in respect of doctrine of mutuality, learned Counsel has argued that insofar as the taxpayer is concerned it is a separate juristic person and has been incorporated under a law which

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[2] Commissioner of Income Tax Vs. Asbestos Cement Industries [(1992) 66 Tax 140 (S.C. Pak)], Commissioner of Income-Tax Vs. Sandoz (Pak) Ltd. (1987 PTD 482), S.N.H. Industries (Pvt.) Ltd. Vs. Income Tax Department [(2004) 89 Tax 252 (H.C. Kar.)], Glaxo Laboratories Ltd Vs. Inspecting Assistant Commissioner of Income-Tax (1992 PTD 932), Assessee Vs. Department (1969) 20 Tax 51 (Trib.), Harmone Laboratories Pakistan Lt., Karachi Vs. Commissioner Income Tax, (2011 PTD 625), Addl. Commissioner of Income-Tax Delhi-II V. Handicrafts and Handloom Export Corporation (1982) 133 ITR 590 (DHC)

[3] Judgment dated 07.01.2011 in ITA Nos. 850 to 857 of 2000 (The Commissioner of Income Tax, Vs. M/s. Lloyd's Register of Shipping) by a Division Bench of this Court, Judgment dated 10.08.2011 passed by the Honourable Supreme Court in Civil Petitions No. 375-K to 382-K of 2011 (Commissioner of Inland Revenue (Legal Division), Karachi Vs. M/s. Lloyd's Register of Shipping, Karachi), Judgment dated 19.05.2022 passed by a Division Bench of this Court in ITRA No. 182/2007 (The Commissioner of Income Tax Vs. Cotton Export Corporation), unreported Order dated 19.02.2022 passed by a Division Bench of this Court in I.T.A No. 402/1999 (Commissioner of Income Tax Vs. Mr. M. Yahya Siddiqui).

is owned by the Government and is not by itself a Federal Government; hence doctrine of mutuality is not applicable. He has further argued that there is nothing on record to substantiate that it was ever a capital receipt as admittedly it is not to be repaid to the Federal Government; hence the treatment to such subsidy as a Revenue Receipt is fully justified. In support he has placed reliance on various precedents[4] of the Courts.

7. While exercising his right of rebuttal, learned Counsel for the taxpayer has argued that subsidy in question was never a part of the profit and loss account; but was separately shown in the appropriation account and was related to the balance sheet; hence could not be deemed to be an income liable to tax. According to him, at most it was a gift or a Capital Receipt by the Federal Government to the taxpayer; therefore, the proposed questions in the cases filed by the taxpayer be answered in their favour and against the department.

OPINION OF THE COURT:

(a) Whether IAC had any jurisdiction to exercise powers under Section 66-A of the Ordinance:

8. We have heard both the learned Counsel and perused the record. First we would like to deal with the subsidiary question so argued regarding lack of jurisdiction of the IAC to exercise powers under Section 66-A of the Ordinance. This is relevant only in respect of Tribunal's order dated 01.09.1992 for assessment years 1986-87 & 1987-88 and under challenge in Income Tax Cases No. 10 & 11 of 1994 filed by the taxpayer. It is the case of the taxpayer that after passing of the original assessment order under Section 62 of the Ordinance, it could not have been revised under Section 66-A of the Ordinance, as according to them, the original assessment order under Section 62 ibid was passed with the approval and consent of IAC, and therefore, he could not have reopened the said order. For that, it would be advantageous to refer to the finding of the Tribunal in its Order dated 01.09.1992, which reads as under: -

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[4] Sindh Industrial Trading Estate Ltd., Karachi Vs. Central Board of Revenue and 3 others [(1975) 31 TAX 114], Messrs West Pakistan Road Transport Board, Lahore Vs. The Commissioner of Income Tax, Lahore (PLD 1974 Note 9), Messrs Karachi Golf Club (Private) Limited through Manager Accounts and Finance and Others (2021 PTD 558), Messrs Nishat Mills Limited and another Vs. The Commissioner of Income / Wealth Tax, Companies Zone, Faisalabad (Now CIR, LTU, Lahore) (2021 P T D 1986) and Messrs. Pakistan International Airlines Corporation Vs. Commissioner of Income-Tax (PLD 1973 Kar. 189).

> "2. The facts of the case are that original order was passed under normal law under section 62 of the Income Tax Ordinance. Subsequently, the action was taken by the IAC under section 66A because the subsidy received by the assesse from the Government had not been included in the receipt and taxed.
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> 3. First argument given by the learned. A.R. of the assessee was that the assessment done by the ITO should be impliedly taken as having been done with the approval of the IAC. So it was asserted that it was case of change of opinion when the relevant facts were the same. We have considered this argument but have seen from the records that the ITO had sent the draft order to the CIT(A) through IAC for approval but the same was returned back with the comments that the ITO should decide the cases on his own responsibility. So when the assessing officer has passed the assessment order on his own responsibility that does not mean that the assessment order passed alongwith the quantum of income determined was done with the approval of the IAC. This plea is rejected a having no legal force behind it. More particular so because there was no evidence on record to show that the IAC had applied his mind which is must for approval of an order."

9. From perusal of the aforesaid finding of facts, it reflects that though, initially the Income Tax Officer had sent a draft order to the Commissioner Income Tax through IAC for approval; but the same was retuned back with the comments that ITO should decide the case on its own responsibility. This factual position has not been controverted on behalf of the tax-payer. Resultantly, in view of the above, when the original assessment order was passed under Section 62 of the Ordinance by the concerned ITO, it could not be assumed that it was passed with the approval of the IAC; rather was done by him without involvement of his superior officer. In fact, even if some assistance has been sought by an assessing officer from the IAC, this would not in itself is sufficient to preclude the IAC from invoking section 66-A of the Ordinance in relation to that particular case[5]. It would also further have to be shown, as a matter of fact, that the degree of involvement was of such intensity that it would make subsequent recourse to section 66-A impermissible[6]. This is so because, as observed above, the mere fact of consultation or even approval was not enough. The degree and intensity of the consultation (itself a question of fact) had also to be established and shown to have been of such level that it would preclude the subsequent exercise of powers under section 66-A[7]. Therefore, if subsequently, the IAC had revised the order by exercising

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[5] Nishat Mills Limited v Commissioner of Income Tax (2021 PTD 1986)
[6] Nishat Mills Limited v Commissioner of Income Tax (2021 PTD 1986)
[7] Nishat Mills Limited v Commissioner of Income Tax (2021 PTD 1986)

his powers under Section 66-A (ibid), it cannot be presumed that he had no jurisdiction to do so and was an illegality on this ground alone.

10. As to the second limb of argument raised by the learned Counsel for the taxpayer that the order under Section 62 of the Ordinance, may have been erroneous at best; but was not prejudicial to the interest of the Revenue inasmuch as the assessment order was an order showing losses in its return; hence, Section 66-A could not have been invoked, we may observe that we are not impressed by this argument at all. There is no cavil to the proposition that for invoking the provisions of Section 66-A of the Ordinance (Section 122 of the Income Tax Ordinance,2001) it is a must that both the ingredients i.e. an assessment order being erroneous and prejudicial to the interest of the Revenue, are fulfilled. Per settled law a mere erroneous order of an Income Tax Officer without causing prejudice to the interest of the Revenue will not authorise IAC to exercise powers under Section 66-A of the Ordinance and these ingredients must be satisfied before invoking section 66-A ibid[8]. However, in the present case, in our considered view both conditions are fulfilled. Firstly, in terms of Section 2(24) (b)[9] of the Ordinance, the income includes any loss of such income and profits or gains, and therefore, even if a Return is showing losses, assessment can still be prejudicial to the interests of the Revenue and once it is not denied that the original assessment order was erroneous, then by merely arguing that the second condition (to the effect that it was not prejudicial to the interests of the Revenue) is not fulfilled, cannot be sustained. In this case, in our considered view, both the preconditions for invoking the provision of Section 66A of the Ordinance are fulfilled. There is one more reason to arrive on this conclusion as the loss, if any, in one income year is carried forward to the next income year, and while computing the income of the subsequent year(s), these losses are permitted to be deducted. Therefore, any such carry forward loss pursuant to some erroneous assessment order will always remain prejudicial to the interest of the Revenue; being liable to correction / amendment of the original assessment order after reopening of the same. Therefore, this

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[8] Glaxo Laboratories Limited v Inspecting Assistant Commissioner (PLD 1992 SC 549=1992 PTD 932)

[9] (24) income includes: -

(a)……..

(b) any loss of such income, profits or gains; and

objection as to the original assessment order not being prejudicial to the interest of Revenue pursuant to a return of loss, and short of meeting the requirement of Section 66-A of the Ordinance is hereby repelled. Accordingly, we conclude that in the given facts and circumstances IAC had jurisdiction to exercise powers under Section 66-A of the Ordinance.

(b) Whether the subsidy paid by the Federal Government to the taxpayer was a Revenue receipt or a Capital receipt.

11. Coming to the main issue in hand (which is common in all listed cases) it appears that the dispute firstly arose in assessment years 1978-1979 to 1980-1981 when Tribunal vide its order dated 14.12.1985 (in ITR No.137 of 1994) came to the conclusion that the subsidy in question was paid by the Federal Government due to losses suffered by the taxpayer and in the public interest to reimburse those losses, which in no way could be treated as trading receipt. It was further observed by the Tribunal that the taxpayer has purchased cotton at a certain price fixed by the Government and since the export price is generally lower than the purchase price, the taxpayer necessarily suffered losses; whereas, it is 100% owned by the Federal Government, and therefore re-imbursement of such losses to the taxpayer could not be considered as a trading receipt. It was further observed that all receipts, which are not capital receipts are not necessarily income within the meaning of the Ordinance. Lastly it was also observed that all receipts are not always capital receipts or Revenue receipts as some receipts may be neither; but at the same time it may not be income either.

12. However, with respect we may observe that the Tribunal in the order under challenge in ITR No.137 of 1994, appears to have misdirected itself in making the above observations as these were never supported, either by any law nor precedents of the Superior Courts. Though in the said order, some reference has been made to the cases of ***West Pakistan Road Transport Lahore***[10] and ***Sind Industrial Trading Estate***[11]. However, from perusal of these

[10] West Pakistan Road Transport Board, Lahore Vs. The Commissioner of Income Tax (PLD 1974 Note 9)
[11] Sindh Industrial Trading Estate Ltd., Karachi Vs. Central Board of Revenue [(1975) 31 TAX 114]

judgments, it clearly reflects that they have no relevance with the controversy in hand and the Tribunal has failed to appreciate the dissimilarity in the facts as are presently before us, therefore, in our considered view insofar as the Tribunal's order in respect of these assessment years dated 14.12.1985 (under scrutiny in ITR No.137 of 1994) is concerned, it cannot be sustained in any manner.

13. As to the argument that subsidy paid by the Federal Government year after year to cover up the losses sustained by the taxpayer was a capital receipt and at most a gift; but not a Revenue receipt is concerned, it may be observed that again there is a finding of fact in the Order of the Tribunal; wherein, their Counsel took a plea that if at all it is so, then the subsidy received is a capital receipt and the ground taken by them was that 100% shares of the taxpayer were held by the Federal Government and was kind of a subsidiary created by the Federal Government; hence should be treated as capital receipt. However, it may be observed that if that was so, then induction of this subsidy as a capital would have resulted in the increase of shareholding by way of extra capital; but this is not the case of the taxpayer. By merely arguing that this subsidy was never shown in profit and loss account; but in the appropriation account; hence it was not a Revenue receipt would not *ipso facto* make it so. Per settled law the question has to be decided by a consideration of the true nature and purpose of the payment and the facts and circumstances of the case as there is no single or infallible test which can be applied to resolve the question; neither the form of the transaction giving rise to the payment, nor the name, which is given to it is relevant in determining the liability of tax[12]. In general, it may be said that what is received for loss of capital is a capital receipt and what is received as profit in trading transaction, is taxable income[13]. As per accounting practice(s) the appropriation account contains both, capital receipts and unappropriated profits usually based on accumulated profits already subjected to tax or untaxed capital gains remaining undistributed during the preceding years till the date of preparation of the appropriation accounts. These could be capital receipts or Revenue

[12] Commissioner of Income Tax v Forbes Campbell & Co Ltd. (PLD 1978 Karachi 1047)
[13] Commissioner of Income Tax v Forbes Campbell & Co Ltd. (PLD 1978 Karachi 1047)

receipts and the nature of such receipts has to be looked into. Appropriation is primarily an act of setting aside money for a specific purpose. It is correct to suggest that for a Government (in accounting terms) it shows the funds a Government department has been credited with. But at the same time, here it is not the Government itself who is the taxpayer; rather a Corporation created by law, which is owned by the Government. The taxpayer is a concern which operates to make profits, and if any amount is shown as an appropriation, then it has to come from its profits; or as retained earnings; or from its reserves or something which has been kept for debt repayment and to finance capital expenditures. None of these are present in this case. Here, an amount has been received, and when questioned as to its treatment, an argument is being made that it is an item in the appropriation account; hence, cannot be taxed. This analogy of the taxpayer appears to be incorrect and against the settled accounting principles even if it was to be shown as an item in the appropriation account.

14. It is also of relevance to note that as a matter of fact the Federal Government's policy in respect of purchase of cotton requires the taxpayer to purchase it from the grower on fixed notified prices. At times, the cotton is purchased at a higher price as against the price on which it is exported; resulting in losses, and the Federal Government on regular basis, was making payments to the taxpayer to run its affairs smoothly and efficiently. It is also a matter of admitted position that these subsidies were given year after year; were not refundable to the Federal Government; whereas, any capital induction is always a liability and it is to be repaid to the contributor. As to the arguments that 100% shares are owned by the Federal Government and it is a case, wherein, doctrine of mutuality would apply, it may be of relevance to observe that such doctrine is only applicable when the participants are earning the profits and the beneficiaries are the same. Here it is not so inasmuch as mere ownership of 100% in the taxpayer company would not make it a Federal Government. Admittedly, the taxpayer is a company incorporated by way of some law having its own identity, different to that of the Federal Government. It is not in dispute that the taxpayer is a Company paying taxes all along on its profits and losses. This issue in somewhat similar circumstances was earlier raised by

Trading Corporation of Pakistan[14] claiming itself to be Federal Government for the purposes of taxation and it was decided against them by this Court. In that case *TCP* claimed an exemption, on the premise of being a Government owned company, whilst admitting that such exemption was not available thereto under any statute, however, the same may be prescribed by this Court. This Court was pleased to observe that it was neither assisted with any such law that empowers it to grant such an exemption and that too in its reference jurisdiction; nor any exception was made to Article 165A of the Constitution which is very clear regarding taxability of Government owned corporations and there is plethora of case law[15] that follows in such regard. Moreover, it has never claimed any exemption under the doctrine of mutuality; nor such a plea was ever raised; rather, the Tribunal in its order dated 14.12.1985 has raised and decided the issue from nowhere and at the same time while making a reference to this Court under Section 136(1) of the Ordinance, never proposed any such question for opinion of this Court. At the same time the taxpayer has also failed to propose any such question in cases filed by it.

15. Insofar as the judgments of the Honourable Supreme Court as well as this Court in the cases of ***Smith Kline & French of Pakistan Limited***[16] and ***Harmone***[17] by the taxpayer's Counsel, we may observe that these judgements have no relevance to the facts as are before us. In fact, they are more akin to what were available in ***PIAC*** (supra) relied upon by the department's Counsel. The facts in ***PIAC*** were that under Section 26 of Pakistan International Airlines Corporation Act (Act No. 19 of 1956), the Central Government under took to make good any losses sustained by the Corporation during the three years next after 30th September 1953, to cover up its losses resulting due to fixed prices of its tickets for certain routes for a certain limited period as per directions of the Federal Government. PIAC's losses were then reimbursed by way of subsidy and for the year 1956-57 it paid a sum of Rs. 1,05,13,609.00 and PIAC claimed this payment as a replenishment of its capital on the ground that it stood reduced to the extent of the amount received by it. This plea was rejected by the Income-tax

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[14] Unreported judgment dated 10.3.2023 in ITR No.211 of 1991
[15] *2019 PTD 1734*; *2019 PTD 587*.
[16] The Commissioner of Income Tax v Smith Kline & French of Pakistan Limited (1991 SCMR 2374)
[17] Harmone Laboratories Pakistan Limited v Commissioner Income Tax (2011 PTD 627)

Officer, by treating it as a revenue amount being taxable, whereas, a direct Appeal before the Tribunal against the decision of the Income-tax Officer also failed. The question of law dealt with in that case (though in respect of the 1922 Act) is identical to the case in hand, that *"Whether the amount of Rs. 1,05,13,609.00 paid by the Government the assessee under section 26 of the Pakistan International Airline Corporation Act, 1956 for making good the loss sustained by the assessee is in the nature of income receipt liable to tax under the Income-tax Act, 1922."* The learned Division Bench of this Court after taking into consideration various judgments of the Courts in Pakistan as well as India, finally agreed with the observations of the department and went on to hold that the view canvassed on behalf of PIAC cannot be sustained upon consideration of the facts and the interpretation of section 26 of the Act, and as a consequence thereof, the amount in question paid by the Government to PIAC for making good the loss sustained by it, was found to be in the nature of income receipts being liable to tax. In view of the similarity of facts in both these cases we are of the view that the present case of the taxpayer is fully covered by the dicta laid down in the case of ***PIAC*** (supra).

16. On the other hand, in the case of ***Smith Kline & French of Pakistan Limited***[18] which has been vehemently relied upon by the learned Counsel for the taxpayer, the facts were entirely different. In that case the primary issue was with regard to the fact that whether the contribution made by foreign shareholders to cover up the losses of local company would amount to income or capital; and whether if there is any income at all, will it be exempt under Section 4(3)(vii) of the Income Tax Act, 1922. In that case there was a local resident entity in which the principal shareholder was a foreign non-resident entity. The local company made losses which were recouped by the non-resident parent company, without however, there being any contractual or other obligation to do so. Further, such contribution was not a permanent arrangement. That was precisely the situation in the relevant appeal decided by the ***SK&F*** case (which was a common judgment whereby three sets of appeals were disposed of). The Supreme Court held that the remittances in question "... *could be termed as mere windfall, for,*

[18] The Commissioner of Income Tax v Smith Kline & French of Pakistan Limited (1991 SCMR 2374)

the foreign shareholders/companies were- under no obligation to remit these amounts or to make good the losses incurred by the Pakistani companies and for the further reason that they could contribute these amounts as capital if there was no prohibition in increasing the capital." (see para 25). These facts are not germane to the facts of the present taxpayer before us; hence, the ratio settled in the case of ***SK&F*** (Supra) is not attracted in the present matter. Here, admittedly, the contribution by the government is as an obligation; and is also of a permanent nature. These facts have not been denied before us. Therefore, any reliance placed on the case of ***SK&F*** (supra) is misplaced. Not only this, the Supreme Court further held that *"It may not be out of place to observe that even a receipt by an assessee of voluntary payment, on certain facts and in certain circumstances, may constitute income provided it arises from business or the exercise of a profession, vocation or occupation, in other words, if there is nexus between the receipt and the business or the exercise of profession or vocation or occupation."* (See para 26). So it is not that in each case it is to be treated as a capital receipt and at the same time it is not always an income. It entirely depends on the peculiar facts of the case while applying the above principle of law.

17. Next case relied upon in this regard is the case of ***Harmone*** (Supra) a decision of this Court, wherein, the facts were once again similar to that of ***SK&F*** (supra) and the learned Bench held that in the facts and circumstances of the case the remittances were precisely what the applicant claimed they were: a mere windfall, which could not be regarded as *"a periodical monetary return coming in with an expected regularity"*, and consequently the Court held that the Tribunal erred in its conclusion that the remittances constituted the taxpayer's income.

18. In essence, the law is that if the payments received are voluntary without there being any legal obligation upon them to do so, or without there being any liability or obligation to that effect, then in a certain set of facts, it can be held to be anything other than an income. It could be a capital receipt or against any share consideration. In the present case it is not so. In judging the nature of a receipt, the Courts have to take into account all the circumstances under which the taxpayer may

have received the money particularly the purpose for which it was given to the taxpayer[19]. In the instant matter the payment by the Government was thus specifically for the purpose of covering losses and it was for that very purpose that the subsidy had been demanded by the taxpayer; consequently, this amount received was a trading receipt and must be held to be income arising from the business of the taxpayer so that it is taxable as such[20]. The payment was no doubt called a subsidy, but it is clear that it was made specifically with the object of compensating the taxpayer for the loss of certain profits which might have arisen if the cotton was not purchased on the price as directed by the Government. This was, therefore an income or receipt by the company which was inseparably connected with the conduct of the business of the company and it arose from that business[21].

19. In the case of ***Raghuvanshi Mills Ltd***[22] the issue before the Supreme Court of India was that whether the amount insured against loss of profit(s) would be taxable or not. In that case the tax-payer had certain insurance policies, including that for a loss of operational profits, if any. A fire broke out, resulting in operating losses and certain amounts were paid by the insurance companies in lieu of loss of profit. The department held that it was taxable; and a reference before the Bombay High Court was also dismissed. An appeal was preferred before the Supreme Court of India and it was argued on behalf of the assessee that it cannot be called profits because the money is only payable if and when there is a loss or partial loss and that something received from an outside source in circumstances like these is not money which is earned in the business and if there are no earnings and no profits there cannot be any income. The Indian Supreme Court was not impressed with this argument and held that it only concentrates on the word "profits", and this may not be a "profit" but it is something which represents the profits and was intended to take the place of them and is therefore just as much income as profits or gains received in the ordinary way. It was further observed that Section 4 of the Income Tax Act, 1922 [analogous to Section 2(24) (a) of the Ordinance] is so widely worded that everything which is received by a

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19 The Ratna Sugar Mills Ltd v The Commissioner of Income Tax (AIR 1958 Allahabad 633)
20 The Ratna Sugar Mills Ltd v The Commissioner of Income Tax (AIR 1958 Allahabad 633)
21 The Ratna Sugar Mills Ltd v The Commissioner of Income Tax (AIR 1958 Allahabad 633)
22 Raghuvanshi Mills Ltd. Vs.Commissioner of Income Tax, Bombay City (AIR 1953 SC 4)

man and goes to swell the credit side of his total account is either an income or a profit or a gain. It would also be advantageous to refer to Para 17 thereof which reads as under;

> 17. "The assessee is a business company. Its aim is to make profits and to insure against loss. In the ordinary way, it does this by buying raw material, manufacturing goods out of them and selling them so that on balance there is a profit or gain to itself- But it also has other ways of acquiring gain, as do all prudent businesses, namely by insuring against loss of profits. ***It is indubitable that the money paid in such circumstances is a receipt and in so far as it represents loss of profits, as opposed to loss of capital and so forth, it is an item of income in any normal sense of the term.*** It is equally clear that the receipt is inseparably connected with the ownership and conduct of the business and arises from it. Accordingly, it is not exempt.

20. In the case of ***Lincolnshire Sugar***[23], advances made under the British Sugar Industry (Assistance) Act, 1931, to a company carrying on business as manufacturers of sugar beet were held to be trading receipts of the company and liable to income tax. It was observed by Lord Macmillan, with whom the other four Lords agreed; that *"it was with the very object of enabling them to meet their trading obligations that the advances were made; they were intended artificially to supplement their trading receipts so as to enable them to maintain their trading solvency"*. We do not see any reason as to why the ratio of this case would not apply to the case in hand as the intent and purpose behind paying subsidy to taxpayer in the instant matter is to reduce its losses.

CONCLUSION:

21. In view of hereinabove facts and circumstances including the law and precedents so discussed, this Court is of view that the subsidy paid by the Federal Government to the taxpayer was a revenue receipt and was liable to income tax. The question of law referred to us for opinion in ITRA No.137 of 1994 i.e. *"Whether on the facts and the circumstances of the case the learned ITAT was justified in holding that the subsidy paid by the Federal Government to the assesse was not a Revenue receipt"* is answered in ***negative***; against the Taxpayer and in favour of the

[23] Lincolnshire Sugar Co. v Smart ((1937) 20 Tax Case 643

Department. This question is rephrased in all remaining cases and stands adopted and is also answered accordingly, against the taxpayer and in favour of the department. The remaining question in ITC Nos.10 and 11 of 1994 is rephrased i.e. *"Whether in the facts and circumstances of the cases, the IAC had jurisdiction in the matter to revise the original assessment order under Section 66-A of the Ordinance"* and the same is answered in the ***affirmative***; against the taxpayer and in favour of the department. As a consequence, thereof, all listed cases filed by the taxpayer stand ***dismissed***, whereas, the only reference for and on behalf of the department is ***allowed***. Let copy of this order be sent to the Registrar of Inland Revenue Tribunal, Karachi, in terms of Section 136(5) of the Ordinance.

22. Before parting we would like to observe that ordinarily, and barring exceptions, the level of assistance provided to this Court by Counsel representing FBR has remained disappointing and much below the minimum expected level; however, in this case involving complexed legal and factual questions, the learned Counsel for the department has assisted us in a befitting manner; compelling us to record our appreciation of his performance.

Dated: 28.09.2023

J U D G E

J U D G E

Ayaz