



OFFICE OF THE
DEPUTY COMMISSIONER INLAND REVENUE (AUDIT-II)
LARGE TAXPAYERS UNIT, ISLAMABAD

Plot No. 20, Khayaban-e-Suharwardy, Mauve Area, G-9/1,
Islamabad.

Tele. No .051-9106102

C. No. LTU/ST/Audit-II/53/2011/

Date: 28/02/2011

ORDER IN ORIGINAL NO. 14 OF 2010

Passed by: REEMA MASUD, DEPUTY COMMISSIONER INLAND REVENUE, LARGE
TAXPAYERS UNIT, ISLAMABAD

N.B. An appeal against this order lies to the Commissioner (Appeals) Inland Revenue, Plot No. 20, Khayaban-e-Suharwardy, Mauve Area, G-9/1, Islamabad within 30 days from the date of issuance of this order. Any such appeal should bear the original copy of the duly-paid challan fee of Rs.1000/- under the tax head-0220000 deposited in the Govt. Treasury and must be accompanied by a copy of this order bearing Court fee stamp as prescribed under Schedule-I item -6 of the Court fee Act, 1870. An extra copy of the written appeal should be simultaneously be sent to this office for information and record.

Date of Initiation of Case : 26/01/2011

Name of Respondent (s) : M/s Islamabad Electric Supply Company Ltd,
(IESCO)
8-B, 3rd Floor, Pacific Plaza, Sector F-8
Markaz, Islamabad.

Date (s) of Hearing : 04/02/2011 and 18/02/2011

Date of Judgment : 28/02/2011

Name of Persons
Appearing : Mr. Faisal Bandey (AR)
For Respondents : KPMG Taseer Hadi & Co. Chartered
Accountant

For Department : Mr. Mahr Aurangzeb, (Auditor)

Brief Facts of the Case


Brief facts of the case are that it has been reported by the auditor of Audit Division -II ,Large Taxpayers Unit, Islamabad that per Rule 58H(1)&(2) of Chapter XI of Special Procedure for Payment of Sales Tax by Steel Melters, Re-Rollers and Ship Breakers, of the Sales Tax Special Procedure Rules, 2007 issued vide SRO 480(I)/2007 dated 09/06/2007, it has been stated as under:-

"Payment of tax.-

- (1) Every steel-melter, steel re-roller and composite unit of steel melting and re-rolling (having a single electricity meter), shall pay sales tax at the rate of 33[six rupees] per unit of electricity consumed for the production of steel billets, ingots and mild steel (MS) products which will be considered as their final discharge of sales tax liability.
- (2) Payment of tax by steel melters, re-rollers and composite units of melting and re-rolling **shall be made through electricity bills along with electricity charges."**

2. Therefore, it was the responsibility of M/s Islamabad Electric Supply Company Ltd. (26-00-2716-001-91) to collect and deposit the Sales Tax collected from Steel Sectors and Re-Rollers. However, during scrutiny of the Sales Tax returns filed by M/s Islamabad Electric Supply Company Limited, it has been revealed that the registered person has collected Sales Tax from Steel Sector and Re-Rollers, however, it has illegally adjusted Sales Tax collected from Steel Sectors against its input tax (constituting final discharge of Sales Tax liability). Details are given as under for the period from July 2008 to December 2010:

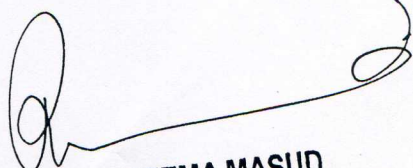
Months	Sales Tax Collected from Steel Sector
July, 2008	51,265,782
August, 2008	88,107,858
September, 2008	75,098,322
October, 2008	49,740,747
November, 2008	87,850,197
December, 2008	79,076,430
January, 2009	47,251,746
February, 2009	-
March, 2009	26,067,301
April, 2009	-
May, 2009	60,922,476


REEMA MASUD
DEPUTY COMMISSIONER (AUDIT-III)
INLAND REVENUE
ISLAMABAD

June, 2009	-
July, 2009	-
August, 2009	-
September, 2009	-
October, 2009	-
November, 2009	635,613
December, 2009	53,386,548
January, 2010	52,453,374
February, 2010	68,323,536
March, 2010	52,640,634
April, 2010	52,297,398
May, 2010	53,143,794
June, 2010	43,581,540
July, 2010	58,998,924
August, 2010	-
September, 2010	-
October, 2010	-
November, 2010	-
December, 2010	35,526,624
Total	1,036,368,844

03. Therefore, M/s Islamabad Electric Supply Company Limited has contravened sections 2((20)(a), 6, 7, 8, 22, 23 and 26(1) of the Sales Tax Act 1990 read with Chapter XI of sales Tax Special Procedure Rules 2007 issued vide SRO. 480(I)/2007, dated 09/06/2007. Accordingly Sales Tax amounting to **Rs. 1,036,368,844/-** is recoverable from M/s Islamabad Electric Supply Company Ltd, under section 36(1) alongwith default surcharge under section 34 apart from penal action available under section 33 of the Sales Tax Act, 1990.

04. On the basis of the aforesaid facts ,a show cause notice ,vide C.No.LTU/ST/Audit -II/53/2011/239 dated 26.1.2011 was issued to M/s Islamabad Electric Supply Company Limited ,8-B,3rd Floor ,Pacific Plaza ,Sector F-8 Markaz ,Islamabad , under section 11(2) of the Sales Tax Act ,1990 and the registered person was asked to show cause as to why Sales Tax amounting to Rs.1,036,368,844/- due for the tax period July 2008 to June 2010 should not be recovered under section 36(1),alongwith default surcharge under section 34 of the Sales Tax Act,1990 and as to why a penalty under section 33 of the Sales Tax Act,1990, should not be imposed .The case was fixed for hearing on 4.2.2011.On 3.2.2011 Mr. Faisal Bandey and Mr .Ahmed (A.R) from KPMG Taseer Hadi and Co attended the office of the undersigned and submitted reply vide letter ITL-828-2011 dated 3.2.2011 which is being reproduced as under for the sake of convenience:-


REEMA MASUD
DEPUTY COMMISSIONER (AUDIT-III)
INLAND REVENUE
ISLAMABAD

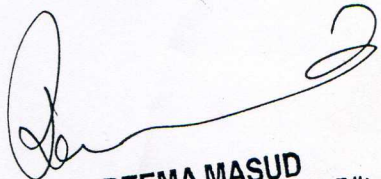
"This is with reference to your show cause notice No. C. No. LTU/ST/Audit-11/53 2011/239 dated 26 January 2011 [SCN] issued to Islamabad Electric Supply Company Limited [the Company] in relation to alleged non payment of sales tax on electricity supplied to steel sector and re-rollers amounting to Rs.1,036,368,844 during the period July 2008 to December 2010 [the Period] by the Company.

On behalf of the Company and on the basis of information provided to us by the management, our submissions on legal and factual grounds to rebut your observations made in the SCN are as follows:

Legal position

- 1.1 You have quite rightly pointed out in your SCN that the Rule 58H [the 58H Rule] covered under Chapter XI of the Sales Tax Special Procedure Rules, 2007 [2007 Rules] is applicable to Steel Melters, Re-Rollers and Ship Breakers [SMRR] only. Further in terms of sub-rules (1) and (2) of the Rule the sales tax collected at rate of six rupees per unit of electricity consumed by SMRR **is their final discharge of sales tax liability.**
- 1.2 However we disagree with your observation that the Company has illegally adjusted sales tax collected from SMRR against its input tax, emphasizing on the words **constituting final discharge of sales tax liability.** Please note that the final discharge of sales tax liability under the Rule is with respect to SMRR and nothing well as in the Sales Tax Act, 1990 [the ST Act] debars the Company (being an electric supply company) to adjust the sales tax collected from SMRR against the input tax credit available during a tax period. We would like to bring to your notice salient features of the sales tax regimes with respect to Fixed/Final tax and Normal tax under the ST Act as follows:

Fixed / Final tax regime
- 1.3 Please note that fixed tax regime was in field from 01 July 1996 to 30 June 1998 in the shape of section 3(2) (d) read with the omitted Fourth Schedule of the ST Act, which was omitted through the Finance Act 1998. Through the SRO.1247(I)/97 dated 18th December, 1997 the then Central Board of Revenue [Federal Board of Revenue 'FBR'] issued the Fixed Amount of Sales Tax Rules, 1997 [FST]. Under the FST it was specifically provided that a manufacturer paying fixed sales tax was not entitled for any rebate, adjustment or refund. The relevant portion of the FST is reproduced below for ease of reference:


REEMA MASUD
DEPUTY COMMISSIONER (AUDIT-II)
INLAND REVENUE
ISLAMABAD

9. Limitation for rebate, remission, refund, drawback or adjustment.—A manufacturer paying sales tax under these rules shall not claim any rebate, remission, refund, adjustment or drawback of sales tax under any provision of the Act or any other rules made there under.

1.4 Sub section (5) was inserted through the Finance Act, 1999 under section 8 of the St Act, wherein it is provided that the person paying fixed tax is not entitled to claim input tax credit. The relevant sub section is produced below for ease of reference:


(5) Notwithstanding anything contained in any other law for the time being in force or any decision of any Court, for the purposes of this section, no input tax credit shall be allowed to the persons who paid fixed tax under any provisions of this Act as it existed at any time prior to the first day of December, 1998.

1.5 You will also appreciate that under sub rule 6 to the 58H Rule of the 2007 Rules only SMRR paying sales tax on fixed rate are not entitled to claim adjustment for input tax credit against their sales tax liability.

1.6 In view of the legal position discussed in Paragraphs 1.3 to 1.5 we understand that the restriction to claim adjustment for input tax paid against a taxpayer's sales tax liability is with respect to those persons who are specifically covered under the ST Act and the rules provided there under. However the fixed tax regime was abolished from the statute effective 01 July 1998 but the restriction to claim adjustment of input tax credit against the units that existed before 01 December 1998 is still intact.
Normal tax regime

1.7 Kindly note that under section 7 of the ST Act, it is provided that a registered person subject to the conditions in section 8B and 73 of the ST Act shall be entitled to deduct input tax from output tax provided he holds a tax invoice in his name and bearing his registration number. Similarly, section 73 of the ST Act provides that certain transactions are inadmissible if payment whereof is made otherwise than through crossed cheque or other crossed banking instruments. The combined reading of section 7 and section 73 of the ST Act depicts that a registered person is entitled to adjust input tax credit against output tax of the same tax period if he holds sales tax invoice issued under section 23 of the ST Act and payment thereof is being made through crossed banking instrument to the supplier.

1.8 We would like to bring to your notice that Chapter III covering Rules 11 to 18 ['Rules 11-18'] of the 2007 Rules are applicable to the electric power companies. These rules provide the procedures for collection and payment


REEMA MASUD
DEPUTY COMMISSIONER (AUDIT-II)
INLAND REVENUE
ISLAMABAD

of sales tax on electric power. You will appreciate that the 'Rules 11-18' are to be applied on the Company; being an electric distribution company. Hence the sales tax liability of the Company should be determined on the basis of the Rule 15 of the 2007 Rules which is reproduced hereunder for ease of reference:

15. Determination of sales tax liability in respect of WAPDA and KESC.—
(1) Any person, except WAPDA and KESC, which supplies electric power shall be entitled to claim admissible input tax adjustment in the manner specified in section 7 of the Act, read with sections 8 and 8B thereof


It is crystal clear from legal position discussed in the Paragraphs 1. 1 to 1.8 above that the Company falls under the normal tax regime as provided under the ST Act: has rightly adjusted output tax collected from SMRR against available input tax of the same tax period under the relevant provisions of the ST Act read with the relevant 2007 Rules which are applicable to the Company.

Facts of the case

With out prejudice to the legal position discussed in the above Paragraphs we would like to further bring to your notice factual position as follows:

- 1.9 Kindly note that the Company has filed all its sales tax returns through the web Portal [Portal] of the FBR. You will appreciate this fact that the monthly sales tax liability of a registered person is calculated by the pre defined formulas on the web based sales tax returns. These formulas are developed by the FBR after taking into account the relevant provisions of the ST Act read with 2007 Rules and the Sales Tax Rules. 2006.
- 1.10 Please note that monthly sales tax liability of the Company for the Period was also calculated by the Portal duly taking into account of input tax credit and after adjusting the same against output tax liability of the Company which comprised of sales tax collected from SMRR (also disclosed as such in the respective returns) and other sales of electricity to its customers. Please note that your observation for illegal adjustment of input tax credit is also against the understandings of the FBR as no such restriction has been imposed at the time of preparation and filing of the monthly sales tax returns by the Company.

We trust that in the light of the above legal and factual position the query raised through the SCN is satisfactorily addressed and we requested you to kindly drop the proceedings by withdrawing the SCN. However in case you do


REEMA MASUD
DEPUTY COMMISSIONER (AUDIT-II)
INLAND REVENUE
ISLAMABAD


not concur to our understanding you are requested to provide us a personal hearing so that we can explain Company's view point."

Thereafter, a letter ITL-858-2011 dated 12.2.2011 was received from the authorized representative of the registered person wherein it was submitted that the matter at hand has been taken up by IESCO with the WAPDA authorities in relation to disclosure of output tax collected from steel sector and adjustment of input tax thereagainst in a tax period and it was requested that the proceedings may be kept in abeyance till the information is received. In the interest of justice and to provide the taxpayer due opportunity of being heard a letter No.254 dated 12.2.2011 was issued to the registered person wherein a final opportunity to submit explanation /comments in respect of the show cause notice was granted till 18.2.2011. In response the A.R of the taxpayer made the following additional submissions:-

"This is in continuation of our earlier letter No. ITL-828-2011 dated 03 February 03, 2011 in response to your show cause notice No.C.No.LTU/ST/Audit-II/53/2011/239 dated 26 January 2011 [the SCN] issued to Islamabad Electric Supply Company Limited [the Company] in relation to alleged non payment of sales tax on electricity supplied to steel sector and re-rollers amounting to Rs.1,036,368,844 during the period July 2008 to December 2010 [the Period] by the Company.

On behalf of the Company and on the basis of information provided to us by the management, our additional submissions are as follows:

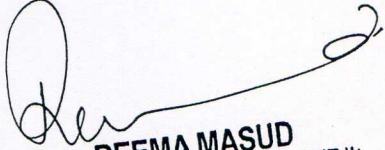
- 1.1 You will appreciate this fact that the Company is following the same disclosure procedure with respect to Steel Melters, Re-Rollers and Ship Breakers [SMRR] which was previously followed by WAPDA while working out its sales tax liability in terms of the monthly sales tax returns and were duly accepted by the taxation authorities till today.
- 1.2 Without prejudice to the Para 1.1. above please note that special procedures for collection of sales tax on electric power are introduced through the SRO 480(I)/2007 dated 09 June 2007 which are effective from 01 July 2007. Please further note that special procedures for payment of sales tax by SMRR covered under Chapter XI of the Sales Tax Special Procedure Rules, 2007 [the 2007 Rules] were introduced through SRO 687(I)/2007 dated 06 July 2007 [the SRO]. You will appreciate this fact that it is a well settled principle of law that introduction or changes to a law are made after taking into account implications of such change on the existing laws, rules or procedures. If there is anything contrary to the existing law, rule or procedures then it is specifically and separately addressed in the


REEMA MASUD
DEPUTY COMMISSIONER (AUDIT-II)
INLAND REVENUE
ISLAMABAD

later changes. Our this understanding finds support from the special procedure of Sales Tax (Withholding) Rules, 2007 which were introduced through the SRO 660(I)/2007 dated 30 June 2007 under which it has been specifically given that the tax withheld will be deposited by the withholding agent through his monthly sales tax return. You will further appreciate that the sales tax return of the FBR also reflects the same understanding and tax withheld amount is reflected as a payable amount by a registered person even if there is a brought forward balance available for adjustment against such withheld amount.

- 1.3 You will further appreciate this fact that the monthly sales tax liability of a registered person is calculated by the pre defined formulas on the web based sales tax returns. These formulas are developed by the FBR after taking into account the relevant provisions of the ST Act read with the 2007 Rules and the Sales Tax Rules, 2006. It is crystal clear from the above that if the understanding of the FBR is not in conformity with that of the Company then the FBR while issuing special procedure rules for SMRR through the SRO much later than the existing 2007 Rules under Chapter III covering Rules 11 to 18 ['Rules 11-18] which are applicable to the electric power companies should definitely have addressed the understanding as show caused under the SCN and simultaneously this understanding could also be reflected in the format of monthly sales tax return given on the web portal of the FBR as it is done in case of withholding sales tax rules.
- 1.4 We would also like to bring to your notice that there are no instructions in the shape of General Order, SRO or notifications which explain mechanics of payment of sales tax collected from the SMRR which again supports our understanding that there was no need of such instructions as the relevant rules applicable on the electric distribution companies circumstantially address to it, that the tax is payable by these companies in terms of section 7 of the ST Act irrespective of the tax charged on the SMRR or other tax payers.

We trust that in the light of the above and our earlier submissions the query raised in the SCN is satisfactorily addressed and we request you to kindly drop the proceedings by withdrawing the SCN. Even if you feel that there is still any doubt then we would like to request you to kindly keep in mind the Golden Rule of interpretation of fiscal statutes that in case there are two interpretations possible then the one beneficial to the taxpayer should be preferred; and in this case the beneficial interpretation is that the Company is required to calculate its tax liability in terms of the Rules 11 – 18 of the 2007 Rules and there is no restriction what so ever on the Company to deposit the sales tax calculated from SMRR separately."


REEMA MASUD
DEPUTY COMMISSIONER (AUDIT-II)
INLAND REVENUE
ISLAMABAD

552

ORDER


05. I have gone through the case record and examined the submissions, written as well as verbal of the respondents and the prosecution and have reached the following conclusion:-

In response to show cause notice the registered person mainly agitated that final discharge of sales tax liability is with respect to steel melters and re-rollers (as per sub-Rules (1) and (2) of Rule 58H of Chapter XI of the Sales Tax Special Procedure Rules, 2007 applicable to Steel Melters, Re-Rollers and Ship Breakers [SMRR only] and that the registered person i.e. M/s IESCO being an Electric Supply Company is not debarred under the law from adjusting sales tax collected from Steel Melters and Re-Rollers against the input tax credit available during a tax period.

It has also been put forth by the AR of the registered person that it falls under the normal tax regime and that its tax liability should be determined on the basis of Rule 15 of the 2007 Rules wherein it has been stipulated that any registered person (except WAPDA and KESC) which supplies electric power shall be entitled to claim admissible input tax adjustment in the manner specified in section 7 of the Sales Tax Act, 1990 read with sections 8 and 8B thereof. It was concluded by the R.P that it falls under the normal tax regime as provided under the Sales Tax Act and has rightly adjusted output tax collected from SMRR against available input tax of the same period under the relevant provisions of the Sales Tax Act, 1990 read with Chapter III of the Sales Tax Special Procedure Rules, 2007. In other words it has been asserted by the registered person that in light of Rules 11-18 of Part -III of the Sales Tax Special Procedure rules for collection and payment of sales tax on electric power there is no restriction on the registered person to deposit the sales tax collected from Steel melters and re-rollers separately and that tax is payable by the registered person in terms of section 7 of the Sales Tax Act, 1990 irrespective of the charge on steel melters and re-rollers.

It has also been asserted by the registered person that pre-defined formulas existing on the web-based sales tax returns permitted/ enabled it to compute its monthly sales tax liability by adjusting its output tax (including sales tax collected @ Rs.6 per unit from Steel Melters and Re-Rollers) against its input tax available for the relevant tax period.

First and foremost the A.R of the Registered Person has emphasized that it has not illegally adjusted Sales Tax collected from Steel Melters and Re-Rollers @ Rs.6 per unit of electricity consumed against its input tax as the same constitutes final discharge of tax liability for the steel sector, however, M/s IESCO has not been debarred as per law/rules from adjusting sales tax collected @ Rs.6 per unit


REEMA MASUD
DEPUTY COMMISSIONER (AUDIT-II)
INLAND REVENUE
ISLAMABAD

of electric from SMRR against the input tax credit available during a tax period. **This argument of the registered person is based /centered upon the premise/assumption that the component of sales tax collected from Steel Melters & Re-Rollers @ Rs.6 per unit of electricity consumed constitutes (a portion of) the output tax of M/s IESCO, therefore the same can be adjusted against its input tax whilst determining its tax liability in accordance with section 7 of the Sales Tax Act, 1990.**

In other words for M/s IESCO to be able to adjust tax collected from SMRR @ Rs.6 per unit of electricity consumed against its available input tax in accordance with section 7 of the Sales Tax Act, 1990. **It is first and foremost vital to examine whether or not such tax collected from SMRR represents the output tax of M/s IESCO.**

In this regard, it would be beneficial to reproduce definition of **output tax** under sub-section (20) of section 2 of the Sales Tax Act, 1990 as under: -

"(20) "Output tax", in relation to a registered person, means: -

- (a) **Tax levied under this act on a supply of goods, made by the person;**
- (b) Tax levied under the Federal Excise Act, 2005 in sales tax mode as a duty of excise on the manufacture or production of the goods, or the rendering or providing of the services, by the person;
- (c) Provincial sales tax levied on services rendered or provided by the person.....

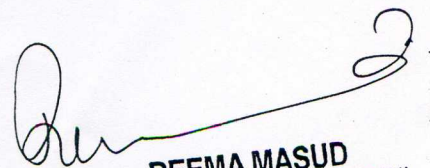
Furthermore as per section 3(1) of the Sales Tax Act, 1990 it has been stated as under: -

"3. **Scope of tax:-** (1) Subject to the provisions of this Act, there shall be charged, levied and paid a tax known as sales tax at the rate of [seventeen] percent of the value of:-

- (a) **Taxable supplies** made by a registered person in the course or furthermore of any [taxable activity] carried on by him, and
- (b) goods imported into Pakistan.....

In turn, the term "**taxable supply**" has been defined in section 2(41) of the Sales Tax Act, 1990 as under: -

"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 percent under section 4;....."


REEMA MASUD
 DEPUTY COMMISSIONER (AUDIT-II)
 INLAND REVENUE
 ISLAMABAD

From the aforementioned definitions of "output tax" and "Scope of tax" delineated as per the Sales Tax Act, 1990 it is clear that output tax is a tax on the supply of goods made by a registered person i.e. in the case of the registered person M/s IESCO output tax is represented by tax levied @ 17% on the value of supply made by the registered person. In a nutshell the output tax of M/s IESCO is represented by sales tax charged @ 17% on the electricity supplied to its consumers (including steel melters and re-rollers) whereas the tax collected from SMRR @ 6 per unit of electricity consumed does not constitute a portion of the output tax of M/s IESCO (not being a tax on the value of electricity supplied by the registered person.) The sales tax charged @ Rs.6 per unit of electricity from SMRR is, infact, representative of the output tax of steel sector which was introduced through Sales Tax Special Procedure Rules 2007 for payment of sales tax by Steel Melters, Re-Rollers and Ship Breakers issued vide SRO 480(1)/2007 dated 09.06.2007. The relevant portion of Rule 58H of Chapter XI of the Sales Tax Special Procedure Rules, 2007 is reproduced as under: -

"Payment of tax:-

- (1) Every Steel-Melter, Steel Re-Roller and composite unit of steel melting and re-rolling (having a single electricity meter), shall pay sales tax at the rate of [six rupees] per unit of electricity consumed for the production of steel billets, ingots and mild steel (MS) products **which will be considered as their final discharge of sales tax liability.**
- (2) Payment of tax by Steel Melters, Re-Rollers and composite units of melting and re-rolling shall be made **through electricity bills along with electricity charges."**

It would be pertinent to specify at this juncture that there are two components of sales tax being collected by IESCO from the steel sector through electricity bills: -

- (1) Sales tax @ 17% of the value of electricity supplied: as well as
- (2) Sales tax @ Rs.6 per unit of electricity consumed by the steel units against production and supply of steel billets, ingots and mild steel (ms) products.

Examination of electricity bills issued by M/s IESCO to the steel Sector also confirms that sales tax charged by IESCO through the issuance of electricity bills from the steel sector consists of two components i.e. sales tax charged @ 17% of the value of electricity supplied which is being paid by all consumers of electricity (including steel melters and re-rollers) and sales tax charged @ Rs.6 per unit of electricity consumed by the steel sector. Both the components mentioned/delineated above are being charged/appeal separately in the


REEMA MASUD
 DEPUTY COMMISSIONER (AUDIT-II)
 INLAND REVENUE
 ISLAMABAD


electricity bills issued to Steel Melters and Re-Rollers. As per the relevant provisions of the Sales Tax Act, 1990 it is clear that sales tax charged by IESCO from Steel melters and re-rollers @ 17% of the value of electricity supplied, in fact, constitutes the output tax of M/s IESCO against supply of electricity and by virtue of the same is rightly being adjusted by IESCO's against its input tax on taxable purchases for determination of its tax liability u/s 7 of the Sales Tax Act, 1990.

However, it is of paramount importance to stress that sales tax charged by M/s IESCO from SMRR @ Rs.6 per unit of electricity through issuance of electricity bills (wherein such component of sales tax is indicated separately) does not constitute a portion of its output tax and is merely being collected by M/s IESCO on behalf of the Federal Board of Revenue as the Final and net discharge of tax liability by Steel Melters and Re-Rollers. It is therefore apparent that as sales tax charged by M/s IESCO from SMRR @ Rs.6 per unit of electricity consumed does not constitute a portion of its output tax, therefore in light of Section 7, 8 and 8B of the Sales Tax Act, 1990, M/s IESCO is not entitled to adjust its input tax against final tax paid by SMRR @ Rs.6 per unit of electricity through electricity bills.

In light of the comprehensive discussion made in the foregoing paragraphs it is clear that the argument of the registered person that sales tax @ Rs. 6 per unit of electricity collected from SMRR through electricity bills constitutes final discharge of tax liability for Steel melters and re-rollers and not for IESCO and that IESCO is not barred under the law from adjusting sales tax collected from steel melters against its available input tax credit is not acceptable for the simple reason that the tax collected from SMRR @ Rs.6 per unit of electricity through electricity bills **does not constitute the output tax of M/s IESCO**, therefore, obviously the same cannot be adjusted against its available input tax for a certain tax period.

However, as discussed earlier the sales tax charged by IESCO from SMRR through electricity bills @ 17% of the value of electricity supplied does constitute (a portion of) its output tax and therefore the aforementioned component can legally be adjusted against its available input tax for a certain tax period.

In response to show cause notice issued it was asserted by the AR of the registered person that it falls under the normal tax regime and that its tax liability should be determined on the basis of Rules 15 of Chapter III of the Sales Tax Special Procedure Rules, 2007 i.e. Special Procedure for collection & payment of sales tax on Electric Power wherein it has been stipulated that any person supplying electric power shall be entitled to claim admissible input tax adjustment in the manner specified in section 7 read with sections 8 and 8B of the Sales Tax Act, 1990.


REEMA MASUD
 DEPUTY COMMISSIONER (AUDIT-II)
 INLAND REVENUE
 ISLAMABAD

The detailed discourse made by the AR of the registered person in its rebuttal regarding fixed/final tax regime which was abolished from the statute elective from 1.7.98 is of no relevance in the instant case as it was nowhere alleged in the show cause notice that IESCO falls under the fixed/final tax regime wherein the person paying fixed/final tax was not entitled to claim input tax credit or any rebate, adjustment of refund.


Furthermore, there is no disagreement with the assertion of the registered person that it falls under the normal tax regime and that its tax liability should be determined on the basis of Rules 15 of Chapter III of the Sales Tax special procedure Rules, 2007 according to which IESCO can claim admissible input tax adjustment in the manner specified in section 7 read with Sections 8 and 8B of the Sales Tax Act, 1990. For the sake of convenience section 7 of the Sales Tax Act, 1990 is reproduced as under: -

"7. Determination of tax liability.—

(1) [Subject to the provisions of section 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 that is due from him in respect of that tax period and to make such other adjustments as are specified in Section 9....."

A perusal of section 7 of the Sales Tax Act, 1990 on the basis of which tax liability of the registered person is to be determined shows that a registered person shall be entitled to deduct input tax paid for the purpose of taxable supplies made, or to be made by him from the output tax that is due from him in respect of that tax period. In other words the registered person shall not be entitled to reclaim or deduct input tax paid on the goods used or to be used for any purpose other than for **taxable supplies** made or to be made by him. A few case laws in this regard are being reproduced as under:-

*" Registered person is entitled to deduct input tax in the manner specified in section 7(1) of Sales Tax Act, 1990, **paid on the goods used or to be used for any purpose for manufacture or production of taxable goods or for taxable supplies made or to be made by such person.** Federal Government may by a Notification in Official Gazette under the provisions of section 8(1)(b) of Sales Tax Act, 1990, specify any other goods on which a registered person is not entitled to reclaim or deduct input tax. **Once a registered person establishes that the goods in question on which input tax has been paid were used or to be used for the purpose of manufacture or production of taxable goods or for taxable supplies made or to be made by him, then subject to the terms of section 7 of***


REEMA MASUD
 DEPUTY COMMISSIONER (AUDIT-II)
 INLAND REVENUE
 ISLAMABAD

Sales Tax Act, 1990, such registered person becomes entitled to the deduction of the input tax paid by him for the purpose from the output tax that is due from him in respect of the particular tax period."

[Sheikh Spinning Mills Limited vs. Federation of Pakistan, [2002] 2002 PTD 2959, Lahore High Court]

'Provisions of section 7 of Sales Tax Act, 1990, leave little to imagination and **it is only the input tax paid during the tax period and for the purpose of taxable supplies made**, that a registered person is entitled to adjust the same from the output tax that is due from him in respect of the said tax period. Subsections (2)(i) of section 7, further conditions the said entitlement upon possession of tax invoices in respect of the supply for which a return is furnished.'

[Hamza Sugar Mills Ltd. through General Manager vs. Collector of Sales Tax ad 2 others, [2005] 2005 PTD 1131, Lahore High Court]

It is clear from the principle(s) enunciated as per section 7 of the Sales Tax Act, 1990 that M/s IESCO is only entitled to claim input tax against its taxable supplies which are represented by supply of electricity to consumers (including SMRR) subject to sales tax @ 17%. **However, in violation of section 7 of the Sales Tax Act, 1990, M/s IESCO has illegally adjusted its input tax against sales tax collected @ Rs.6 per unit of electricity supplied to Steel Melters and Re-rollers which does not constitute its taxable supply.**

Without prejudice to the fact that there is no disagreement with regard to IESCO falling under the normal tax regime and determination of its tax liability being governed under section 7 (read with sections 8 and 8B) of the Sales Tax Act, 1990, **the contention of the registered person that it has rightly adjusted sales tax collected @ Rs.6 per unit of electricity from SMRR against its available input tax under the relevant provisions of the Sales Tax Act, 1990 is not acceptable for the simple reason that the aforementioned component of sales tax collected from SMRR does not represent the output tax of M/s IESCO not being a tax on the supply of electricity to the steel sector and therefore the same obviously cannot be adjusted against its available input tax during a tax period as per section 7 of the Sales Tax Act, 1990.** The output tax of M/s IESCO is, infact, represented by sales tax charged @ 17% on the value of electricity supplied to steel sector as well as other consumers and the said component is rightly being adjusted by IESCO against available input tax for a tax period in accordance with section 7 of the Sales Tax Act, 1990.

Furthermore, the A.R of the taxpayer also put forth that special procedure for payment of sales tax by SMRR covered under chapter XI of the Sales Tax Special Procedure Rules, 2007 was introduced through SRO 687(1)2007 dated



REEMA MASUD
 DEPUTY COMMISSIONER (AUDIT-II)
 INLAND REVENUE
 ISLAMABAD

06.07.2007 subsequent to Special Procedure for collection of sales tax on electric power through SRO 480(I)/2007 dated 09.06.2007 (effective from 01.07.2007). However, there was no contradiction with the existing law which was addressed whilst introducing Special Procedure for payment of sales tax by SMRR under Chapter XI of the Sales Tax Special procedure Rules, 2007.

The argument of the AR is misconstrued/irrelevant as no change/amendment was necessitated in the Sales Tax Special Procedure rules for collection of Sales Tax on Electric Power as a result of the introduction of Sales Tax Special Procedure rules for payment of Sales Tax by SMRR covered under chapter XI of the Sales Tax special procedure Rules, 2007. As detailed in the foregoing paragraphs there are no two opinions about the fact that sales tax liability in the case of M/s IESCO is to be determined in accordance with section 7 of the Sales Tax Act, 1990 (read with section 8 and 8B thereof) as stipulated under rule 15 of the Sales Tax Special Procedure Rules, 2007. As explained above the introduction of sales tax special procedure rules for Steel Melters, Re-Rollers and Ship Breakers did not necessitate any changes in the special procedure rules for payment of sales tax on electric power as there is no conflict amongst the same. The argument of the AR of the registered person in this regards is therefore of no relevance.

Lastly, the AR of the registered person has argued that the pre-defined formulas existing on the web based sales tax returns enabled it to adjust the component of sales tax @ Rs.6 per unit of electricity collected from Steel Melters and Re-Rollers against its available input tax i.e. there was no restriction imposed by the pre-existent formulas on the web-based sales tax returns in respect of adjustment of tax collected @ Rs.6 per unit of electricity against available input tax.

The fact that web based pre-existent formulas on the web based sales tax returns enabled the registered person to illegally adjust sales tax collected @ Rs.6 per unit of electricity from SMRR against its input tax cannot override the substantive provisions of law in this regard. The tax collected from steel sector @ Rs.6 per unit of electricity, not representing the output tax of the registered person (as detailed above) can under no circumstances be adjusted against its input tax as per principles enunciated in section 7 (read with section 8 and 8B of the Sales Tax Act, 1990). Such illegal adjustment can in no way be condoned/defended on the pre-text that web based formulas enabled such treatment/adjustment to be adopted by the registered person as substantive provisions of law in respect of this issue shall obviously reign supreme. In other words existence of pre-defined formulas on the web based sales tax returns can in no way be used as an excuse/made a scapegoat for illegal adjustment of tax collected @ Rs.6 per unit of electricity from SMRR against available input tax.


REEMA MASUD
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 INLAND REVENUE
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06. In light of the above discussion I order M/s **Islamabad Electric Supply Company Limited** to deposit **Rs. 1,036,368,844/-** alongwith default surcharge (to be calculated at the time of payment) under section 34 apart from penal action available under section 33 of the Sales Tax Act, 1990.

07. This order consists of sixteen (16) pages and each page bears my official seal and signature.

(Reema Masud)
Deputy Commissioner Inland Revenue
(Audit-II)

Registered/ AD
The Director Finance,
Islamabad Electric Supply Co. Ltd.,
3-B, Pacific Plaza, F-8, Markaz, Islamabad.

Copy to:

1. The Commissioner (Audit), Large Taxpayers Unit, Islamabad.
2. The Additional Commissioner (Audit, Large Taxpayers Unit, Islamabad.
3. The Assistant Commissioner (Enforcement-II), Large Taxpayers Unit, Islamabad.
4. Office copy.

(Reema Masud)
Deputy Commissioner Inland Revenue
(Audit-II)

REEMA MASUD
DEPUTY COMMISSIONER (AUDIT-II)
INLAND REVENUE
ISLAMABAD