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List of Cases Presented for Discussion during FBR Seminars

1. Chain International Water and Electric Corporation Malakand 111 Hydro Project
2. Phoenix Aviation Pvt Ltd (Lahore)
3. Amjad Sandela, an expatriate employee of M/s ENI Pakistan (Karachi)
4. M/s CGL Line Pvt Ltd.(Karachi)

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1. Chain International Water and Electric Corporation Malakand 111 Hydro Project (Mohsin Khan Additional CIT, RTP Peshawar)

Facts (As reproduced from the hand written note**)** **ANNEX 1**

Chain International claimed Tax Refund of Rs.400 million for the year 2010 on the basis that the Return [not Statement under section 115(4)] was filed and on the basis of DTA they are entitled for refund.

The refund was rejected [u/s 17(4)] on the reason that as per Bye Law 1987 of Pakistan Engineering Council (page 7, 10, 17 and 29) M/S Chain(a) International Water and Electric Corporation has formed AOP with Pakistani company and u/s 84 they are resident Association of Persons. The taxability of Resident AOP is governed by section 92 and u/s 92 of the ITO (Income Tax Ordinance) only AOP is taxable and member is exempt and not required to file return. Under the circumstances, section 107 and 105 is not applicable. Further, the tax deducted from resident AOP u/s 153(3) is a final tax and is also covered by section 169(3).

They went to FTO and FTO after obtaining information from all LTUs and RTOs which revealed that different treatment is meted out directed the Board to formulate uniform policy for determining refund and assessment of non-residents.

To resolve the issue, two meetings were held in the FBR and the participants were: Member IR, Member Legal, Secretary Int. Taxes, Chiefs of all LTUs, and Chief RTO Islamabad, Rawalpindi and Peshawar. I also participated in these meetings. The consensus was not developed whether or not under the situation when the member is exempt/s 107 and 105 is applicable. Ultimately, it was decided to send the matter to the Law and Justice Division.

In the R.O 1979 (?) under section 69read with clause 9 of the Second Schedule, member of AOP was tax(ed) separately.

Advisory

1. The above facts are deficient in most important aspect – WHAT is the country of residence of Chain International Water and Electric Corporation Malakand 111 Hydro Project, and under which DTA Tax Refund was claimed.
2. Tax Authorities appear to have touched only the tax provisions under the Income Tax Ordinance 2002 in a manner as if the DTA between Pakistan and the Country of Residence of the Chain International doesn't exist.
3. Chain International approached the FTO who without appreciating the DTA Concepts and their applicability to cross border transactions directed FBR to develop a "uniform tax treatment to non-residents".
4. FBR has reviewed the matter at the highest level and decided to refer it to the Ministry of Law and Justice.
5. Mr. Mohsin Khan has not provided any details about the FTO Order, the minutes of FBR meetings, and FBR Reference to the Ministry of Law and Justice.
6. In view of the position stated at # 1 and 5 above, no advisory/opinion in the context of DTAs can be provided.

2. **Phoenix Aviation Pvt Ltd** (Reproduced from the Writ-up provided by Mr. Manzoor Hussain Shad Commissioner Inland Revenue) ANNEX 2

Facts

M/s Phoenix Aviation Pvt Limited derives income from providing transport services by air. The company applied for (tax) exemption certificate u/s 152(5A) stating that "M/s Phoenix Aviation Pvt Limited is getting technical services being flight training to its pilots from M/s Flight Safety International USA. It was claimed that the said company was non-resident having no permanent establishment in Pakistan so no deduction of tax was involved on payments to M/s Flight safety International, USA because of over-riding effect of the Convention between the Government of Pakistan and the United States of America for the Avoidance of Double Taxation".

The Commissioner Inland Revenue, in his order, observed that as per the Agreement between M/s Flight Safety International, USA and M/s Phoenix Aviation Pvt Limited, the former is to provide training services to the latter's personnel which are neither covered under Article II (l) (1) nor Article IX (3) of the Pakistan/US DTA; hence not tax exempt from Pakistan Tax.
The Order goes on and explains the matter in further details ------.

Advisory

1. The Commissioner was/is right in his conclusions. Technical services provided by a US Resident are not covered within the definition of 'Industrial and commercial profits'. Hence, whether the recipient maintains or not a permanent establishment in Pakistan, it makes no difference to its taxability or otherwise under the Pakistan/US DTA.
2. Technical services fees are also not covered in the definition of Royalties [Article IX (3)] of the Pakistan/USA DTA; hence these are not chargeable to tax exclusively in the Country of Residence of the recipient either.
3. As there is no Article on 'Other Income' which would have given the taxation right to one or the other treaty countries; hence 'Technical Services Fees' payable by a Pakistan Resident to a US Resident is taxable in the Payer's country i.e. Pakistan.

3. **Amjad Sandela, an expatriate employee of M/s ENI Pakistan** (Abid Aziz Memon DCIR) ANNEX 3

Facts

Mr. Amjad Sandela is an expatriate employee of M/s ENI Pakistan, a non-resident company engaged in the business of exploration and production of petroleum in Pakistan. The company conducts its operations by employing foreign nationals.

The issue is: Tax deducted on salary of Mr. Amjad by M/s ENI Pakistan has been claimed as refundable in tax year 2007 because Mr. Amjad believes that his salary is exempt from the tax in view of section 3B of the Regulation of Mines and Oilfields Mineral Development (Government Control) Act 1948 read with clause 13 of the schedule in the said Regulation and also read with clause 7 and 8 of Part 1 of 2nd Schedule to Repealed Income Tax Ordinance 1979.

The Department View: As the clause 7 and 8 of Part 1 of the 2nd Schedule to the Repealed Income Tax Ordinance 1979 were deleted through SRO No. 1136/1 dated 07-11-1991; hence the aforesaid clauses have already become inoperative and no longer provide relief to the above employee. Even section 54 of the Income Tax Ordinance 2001 which deals with 'Exemptions and Tax Provisions in Other Laws' does not apply in the instant case as the said exemption was withdrawn before the promulgation of Income Tax Ordinance 2001.

It should be noted that before the amendment brought about vide Finance Act 2008, the proviso to section 54 provided exemption from income tax provided in any other law unless withdrawn. Further, the section 239(10) of the Income Tax Ordinance, 2001ensures the saving of any notification, notice or order issued or made under the repealed Ordinance.

In view of the above facts should department reject the claim of refund and tax salary?

Advisory

1. The above facts relate to an expatriate employee of a Pakistan company. It no where mentions the country of residents of Mr. Amjad Sandela.
2. The issue and Departmental view on the basis of review of the national taxation law provisions is given. There is, however, completely missing any mention to the applicable DTA provisions. In the absence of information about the country of residence of Mr. Amjad, it is not possible to identify as to which DTA is applicable in this case.
3. It is suggested that the present case may be seen in the context of both in the light of Income Tax Ordinance 2001 and the relevant DTA (after identifying the country of residence of Mr. Amjad).
4. As it appears, under the Income Tax Ordinance 2001, Mr. Amjad's salary is taxable in Pakistan, we must have a recourse to the relevant DTA to see whether it is taxable or not.
5. The general principle on taxation of 'Income from Employment' is contained in Article 15 of the Model Conventions. Under paragraph 2 of these MCs, salary income of a non-resident person is taxable in a state if the remuneration of such person derived in respect of employment exercised in that state if:
    a. He is present in that state for a period exceeding in aggregate 183 days in any 12 months period commencing or ending in the fiscal year concerned, or
    b. The remuneration is paid by or on behalf of an employer who is resident of that state, or
    c. The remuneration is borne by a permanent establishment which the employer has in that state.
6. Notwithstanding the above provisions of the Model Conventions, the Department must look at the relevant tax treaty before making decision in this case.

4. **M/s CGL Line Pvt Ltd.** (Abid Aziz Memon DCIR) ANNEX 4

Facts

M/s CGL Line (Pvt) Ltd is engaged in the business of freight forwarding in Pakistan. During the " tax year 2007, the company did not deduct the tax u/s 21(c) from payments to certain non- resident entities in terms of Section 152 amounting to Rs.3,519,534/-

The company claims that payments made to non-residents who belong to countries which have signed agreements for avoidance of double taxation with Pakistan. The contention examined and found correct as treaties prevail over local law or have overriding effect as per the provisions of Section 107 of the Ordinance.

The company also claim that it does not have any permanent establishment (PE) in Pakistan, hence the Section 101(3)(a) of the Income Tax Ordinance,2001 is not applicable. The contention examined and found correct.

The company also claims that clause (d) of the Section 101 (3) is not applicable, which refers to any business connection in Pakistan, in the following way:

"whenever a customer of the company contacts it for import of certain items and pays it the agreed amount the company contacts its non-resident principal who in turn collects the goods from the doorstep/godown/warehouse of the manufacturer and boards the same on the ship/airplane as the case may be. When the goods reach Karachi the company collects and gets them cleared and delivers to the concerned customer. The non-resident principal is paid in respect of the offshore services rendered by them. However, in this arrangement no part of the activity or operation is carried out by the non-resident principal in Pakistan meaning thereby that non-resident principal does not have any business connection in Pakistan."

It should be noted that the above company has not complied with the legal requirement of seeking approval from non-deduction of tax in terms of section 152(5) of the Ordinance. In view of the above facts should department pass the order for non deduction of tax u/s 161 read with section 205 of the Ordinance,2001 or pass an order u/s 122 by disallowing related expenses u/s 21(c) read with Section 152(2) of the Ordinance.

Advisory

1. The above facts only state that M/s CGL Line Pvt Ltd is engaged in the business of freight forwarding in Pakistan. It further states that the company does not have a permanent establishment in Pakistan. It however states that M/s CGL has non-resident principal; hence it may be a subsidiary of the non-resident principal.
2. While a subsidiary in itself cannot be a permanent establishment of its non-resident principal (e.g. parent company) if its acting in normal course of business, it could be deemed as permanent establishment of the non-resident principal if it acts identical to a ‘dependent agent’ i.e. it acts exclusively for or on behalf of its principal and has the powers to bind the principal to a contract with third parties, and frequently exercises that right. We cannot offer any comments based on the above facts.
3. It is also stated that the company makes payments to non-residents whose countries of residence have operative DTAs with Pakistan. Agreed that the services for carrying the freight are performed in international waters, the question remains as to the provisions of the relevant tax treaties.
4. Pakistan has a mix bag of DTA provisions i.e. exclusive taxation in the country of residence of the non-enterprise, primary right of taxation in the country of residence but the source country applying its limited tax based on gross billing or net income basis, and finally 100% taxation in source country.
5. Hence; it is important to visit the relevant DTA taxation provisions