



# TAXPAK

**Newsletter by**

**Tola Associates**

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## Chairman's Message

Asalam-o-alaikum everyone! Hope this monthly issue of TaxPak finds you in good spirits and immaculate health! We welcome you to another edition of TaxPak, our monthly publication the purpose of which is to provide a monthly update on the ongoing tax related developments in Pakistan. Alhamdulillah, so far, we have been successful in our mission to educate about, and keep the public-at-large updated of, these developments on a monthly basis.



Moreover, we would like to apprise the readers of what information you can expect in this document. This newsletter contains an elaboration of important notifications and circulars issued by the Federal Board of Revenue ("FBR") and its provincial counterparts. Moreover, Notifications from the corporate regulatory body i.e., SECP are discussed. As our main aim is to keep the masses updated regarding the developments in the Pakistani tax law, we usually discuss a (relatively) recent judgement passed by the courts of law. This edition of TaxPak consists a discussion of two judgments issued by the Appellate Tribunal Inland Revenue Islamabad. The first judgment pertains to a discussion on depreciation cost that was allowed on a turnkey project. The second judgment by the Appellate Tribunal Inland Revenue-Multan relates to the adding back of income from sale of sugarcane without considering expenses / cost of sales.

Towards the end of the newsletter, we have discussed our Topic of the month titled "Revocable Transfer of Assets". The said topic provides an insight on the taxability and treatment of income on part of the transferor and transferee.

All our readers are requested to visit our website [www.tolaassociates.com](http://www.tolaassociates.com), or download our mobile application in order to access previous published editions of TaxPak along with other publications, and to stay updated of future notifications. Lastly, we request our readers to circulate this e-copy within their circle, as our primary aim is to benefit the masses. Feedback is always welcomed.

Warm Regards,

**Ashfaq Yousuf Tola, FCA**

**Chairman**

**Tola Associates.**

# Tax Notifications

## A. FBR Notifications

### **1. Partial modification to the instructions regarding mode and manner for payment of tax u/s 7E of the Income Tax Ordinance, 2001 on sale or transfer of immovable property.**

The Finance Act 2023 (“Act 23”) introduced a new sub-section (2A) in Section 236C of the ITO, whereby no immovable property can be sold or transferred without providing evidence to the transferring authority that the seller / transferer has duly paid the deemed income tax liability on the said property under section 7E of ITO.

Thereafter, Circular No. 01 of 2023-24, dated 21st July 2023, was issued, wherein the mode and manner of payment of payment of tax under section 7E was provided (access link [Click here](#) for our detailed comments).

Now, the FBR vide Circular No. 03 of 2023-24, dated 15th August 2023 issued a partial modification to Circular No. 01 of 2023-24 dated 21st July 2023. In this circular, the following modifications have been issued:

1. Cases falling in the Jurisdiction of the Lahore High Court (“LHC”) will not be required to pay tax under section 7E until the judgment in WP No. 52559 of 2022 dated 06th April 2023 is reversed, suspended or vacated in an Intra Court Appeal or by the Supreme Court of Pakistan.
2. Non-resident persons shall not be required to pay tax, and therefore, while selling/transferring immovable property, (s)he shall furnish duly filled Form B along with a scanned copy of valid passport, copy of CNIC/NICOP/POC to the transferring authority. The transferring authority shall verify the credentials and ensure that the non-resident person’s stay in Pakistan is less than 183 days for each applicable tax year.
3. The following are exempted from tax on deemed income under Section 7E, therefore, the transferring or registering authority shall obtain evidence that the seller/transferor falls under the following categories and the property under sale/transfer has been allotted to them as an original allottee and is duly certified by the official allotment authority.
  - a. Shaheed or dependents of a Shaheed belonging to Pakistan Armed Forces:
  - b. A person who dies while in the service of the Pakistan Armed Forces or the Federal / Provincial Government.

- c. A war wounded person while in the service of the Pakistan armed forces or Federal / Provincial Government;
  - d. An-ex-serviceman and serving personnel of armed forces or ex-employees or serving personnel of Federal / Provincial Government;
4. Section 7E does not apply for properties in the first year of acquisition on which tax under section 236K has been paid. In this situation, the seller/ transferer shall furnish a Computerized Payment Receipt (CPR) bearing the seller/ transferer's name, CNIC Number, evidencing payment under section 236K, along with date of payment and tax year. If CPR shows that it was sold or transferred during the same tax year, then the transferring authority shall not require evidence of payment u/s 7E or Form A (in the Circular No. 01 of 2023-24) if the seller/ transferor is in the Active Taxpayers' List (ATL).
5. If the immovable property under sale or transfer is an agriculture property excluding farmhouse(s), as evidenced through the property documents, the transferring authority, will execute transfer without seeking evidence of payment of tax u/s 7E or the Form-A. However, if one or more than one farmhouse has been constructed on an agriculture property, then the conditions in Circular No. 1 of 2023-24 shall apply. A farmhouse house is a house constructed on a total minimum area of 2000 sq. yrds. with a minimum covered area of 5000 sq. ft used as a single dwelling unit with or without an annex. If there are more than one dwelling units in a compound and the average area of the compound is more than 2000 sq. yrds for a dwelling unit, then each dwelling unit shall be treated as a separate farmhouse.
6. If the seller or transfer is a local authority, development authority and builders or developers for land development and construction, then a certificate of registration with DNFBP and certificate from the authorities concerned that the property is being sold/ transferred after development or construction, shall be provided to the transferring authority of immovable property and the transferring authority shall not seek evidence of payment of 7E.

The Circular also stated that if any conflict between the Circular and the letter of the law arises, the law shall prevail.

It is pertinent to mention that the transferring authority of immovable property shall maintain a proper record of the data of the seller/transferor along with relevant documents and such records shall be shared with the concerned Chief Commissioner IR of Regional Tax Office having jurisdiction over the seller/transfer on a weekly basis.

For further reading: [FBR](#)

## **2. Amendments to the Income Tax Rules, 2002 – Record of Beneficial Owners**

The FBR, vide SRO 1117(I)/2023, dated 28th August 2023, has issued amendments to the Income Tax Rules, 2002 which were earlier published through SRO 229(I)/2023, dated 28th February 2023. The amendments pertain to records of beneficial ownership and have been summarized and presented as follows:

### **Applicability:**

Every company and association of persons (“AOP”) during the initial registration with FBR shall submit particulars online, while existing company and AOP shall do so by 31st December 2023 online. These records shall be updated within 30 days from the date when the change occurs. For a non-profit organization, the settlor, trustee, founder, promoter, beneficiary, class of beneficiary, shall be considered as the beneficial owners of the non-profit organization. However, where beneficiary or class of beneficiary is the general public, then it shall be exempted from the requirement of providing information of beneficial owners.

In case there is no change in the beneficial owners of the Company or AOP throughout the tax year, then a “Certificate of Confirmation for Beneficial Owner” shall be submitted online along with the Income Tax return to be filed for that tax year.

It is pertinent to mention that every company or AOP shall retain the records of all beneficial owners for 10 years from the date they become beneficial owners of that company or AOP, and cease to be the beneficial owners of that company or AOP.

Furthermore, the FBR shall retain the records of beneficial owners of all companies and AOPS registered with the FBR for 10 years from the date when that company or AOP ceases to be registered with FBR.

Cascading Process for recording of beneficial ownership information:

A three step test was established to identify beneficial ownership from the records of beneficial ownership provided by the persons mentioned above. It was also specified that these tests would be applied in succession i.e. it will be applied only after a previous test failed to identify the ultimate beneficial owner. In simple words, once test 1 fails, then test 2 shall be applied (because there is still a doubt or Beneficial Owner could not be identified), if it is still unidentifiable, then Test 3 shall be applied. The three steps are listed below:

**I. Test 1:** Rule 83C(1), 83C(2), 83C(3) and 83C(4)

a. **Test 1** shall include record of beneficial owner maintained as per the stipulated form for each of the below mentioned categories where ultimate effective control over a company or AOP is through:

- i. Direct ownership rights (through shareholding) of 25% or more;
- ii. Ownership rights of 25% or more through chain of ownerships ( all the legal entities and the legal arrangements are ultimately held by the natural person)
- iii. Joint control arrangement, meaning where 2 or more natural or legal persons in aggregate have 25% or more control despite individually having less than 25% control and that they exercise or may exercise control in the capacity of being associates to each other as per section 85 of the Income Tax Ordinance, 2001;
- iv. Exercise of ultimate effective control over the company or AOP through voting rights,

**II. Test 2:** Rule 83C(5) and 83C(6)

a. Test 2 shall include records maintained through contractual associations or through personal or family connections with the owners. Here, contractual association means. legal tie or contractual tie of 2 or more persons and/or legal entities, arrangements on the basis of a contract executed by the parties of the contract.

**III. Test 3:** Rule 83C(7)

a. Test 3 shall include record of person who exercises ultimate effective control over the company or AOP as a senior managerial position or other indirect means.

For further reading: [FBR](#)

## B. Sales Tax on Services Notifications

### 1. Extension for filing July 2023 sales tax on services' return

The authorities listed below had provided extension for the e-payment and e-filing of the sales tax return on services for the tax period July 2023 for all registered persons and withholding agents. It is pertinent to mention that e-payment of the monthly returns should be made by or on 15th of the following month and e-submission should be made by or on the 18th.

Authorities	Circular/Notification	Tax Period- July 2023 e-payment	e-filing	Links
SRB	Circular No. 3/2023, dated 11th August 2023	17-08-2023	21-08-2023	<a href="#">SRB</a>
KPRA	Circular No. 2/2023, dated 11th August 2023	18-08-2023	21-08-2023	<a href="#">KPRA</a>
PRA	Notification No. PRA/Orders.06/2021/323, dated 11th August 2023	18-08-2023	18-08-2023	<a href="#">PRA</a>
BRA	Notification No. BRA/HQ/23-24/239, dated 17th August 2023	25-08-2023	30-08-2023	<a href="#">BRA</a>

### 2. Further extension for filing July 2023 sales tax on services return

The authorities listed below had provided further extension for the e-payment and e-filing of the sales tax return on services for the tax period July 2023 for all registered persons and withholding agents, in the following manner:

Authorities	Circular/Notification	Tax Period- July 2023 e-payment	e-filing	Links
SRB	Circular No. 4/2023, dated 17th August 2023	21-08-2023	24-08-2023	<a href="#">SRB</a>
KPRA	Circular No. 4/2023, dated 18th August 2023	22-08-2023	25-08-2023	<a href="#">KPRA</a>
PRA	Notification No. PRA/Orders.06/2021/325 dated 17th August 2023	24-08-2023	24-08-2023	<a href="#">PRA</a>



### **3. Exemption from Sindh Sales Tax on Services on taxable services to Water and Power Development Authority (WAPDA) for the purpose of construction and completion of Greater Bulk Water Supply Scheme of the K-IV Project (Phase-I)**

The SRB, vide Notification No. SRB-3-4/43/2023, dated 15th August 2023, granted an exemption to certain services provided to the Water and Power Development Authority (WAPDA) for the construction and completion of the Greater Bulk Water Supply Scheme of the K-IV Project (Phase-I), subject to conditions enumerated in the said Notification. Services provided or rendered in respect of the same shall be exempt only till the completion of the K-IV project (Phase-I), and are as follows:

1. By persons engaged in contractual execution of work or furnishing supplies;
2. Technical, scientific and engineering consultants;
3. Other consultants, including tax consultants, human resources and personnel development consultants; and
4. Construction services.

For further reading: [SRB](#)

## **Corporate Notifications**

### **1. Amendments with respect to Independent Directors**

The SECP issued regulations regarding the limitation of terms for Independent Directors in all capital market infrastructure institutions such as securities exchanges, clearing houses, CDC and future exchanges. The limitation was that an independent director could not hold office for more than three terms in total across these institutions. Furthermore, the Notifications enumerated below, clarified that a person nominated as a director would not be considered as an independent director and therefore this limitation shall not be applicable nominated directors. However, where independence of a person is in ambiguity, the decision of the Commission shall be final and binding. Furthermore, a Chief Executive Officer shall be appointed for a term of three years and may be renewed for one more term with prior approval of the Commission, however, this shall be based on exceptional performance substantiated by the board of directors through a rigorous review, subject to competitive hiring process and final review and approval by the Commission.

Sr. No	SRO	Regulation	Earlier SRO	Link
1	Notification No. 1062(I)/2023 dated 10th August 2023	Securities Exchanges (Licensing and Operations) Regulations, 2016	SRO 652(I)/2023 dated 01 June 2023	<a href="#">SECP</a>
2	Notification No. 1063(I)/2023 dated 10th August 2023	Futures Exchanges (Licensing and Operations) Regulations 2017	SRO 654(I)/2023 dated 01-06-2023	<a href="#">SECP</a>
3	Notification No. 1064(I)/2023 dated 10th August 2023	Central Depositories (Licensing and Operations) Regulations 2016	SRO 653(I)/2023 dated 01-06-2023	<a href="#">SECP</a>
4	Notification No. 1065(I)/2023 dated 10th August 2023	Clearing Houses (Licensing and Operations) Regulations, 2016	SRO No. 651(I)/2023 dated 01-06-2023	<a href="#">SECP</a>

## 2. Requirements for Lending NBFCs providing digital nano-lending

The SECP, through Circular No. 10 of 2023, dated 07th August 2023, issued requirements for lending NBFCs providing digital nano-lending. Through this circular, various exposure limits and additional disclosure to borrowers and additional requirements for digital lenders were enumerated such as NBFC shall extend maximum of Rs 25,000/- as nano lending to a borrower at any point in time with a tenor of up to 90 days. For further reading: [SECP](#)

## 3. Electronic transmission of Annual and Quarterly Financial Statements of Listed Companies to the Commission and Registrar of Companies

The SECP, through Circular No. 11 of 2023, dated 11th August 2023, directed all listed companies to file their annual and quarterly financial statements along with the reports as required through eService of SECP within the timeframe provided under the Companies Act, 2017. The Circular also stated that the filing shall be considered a compliance to the requirement of dispatching/transmitting financial statements to the Commission and Registrar. For further reading: [SECP](#)

## **CASE LAW: DEPRECIATION ALLOWANCE ON TURNKEY PROJECT ALLOWED BY THE HON'BLE APPELLATE TRIBUNAL INLAND REVENUE.**

### **INTRODUCTION:**

The Hon'ble Appellate Tribunal Inland Revenue, Islamabad ("ATIR") was moved by M/s. Punjab Ring Road Infrastructure Management & Engineering (Pvt.) Limited ("Appellant") against the Order passed by the Commissioner Inland Revenue, Zone, LTO, Islamabad ("Respondent") in respect of applicability of tax depreciation under section 22 and 23 of the Income Tax Ordinance, 2001 ("ITO") on the capitalized cost of the Concession Assets. It is pertinent to mention that the Appellant had filed multiple appeals before the ATIR which pertained to Tax years 2018 to 2021. However, due to the similarity in the nature and facts, all the appeals were decided through a common order.

### **BRIEF FACTS OF THE CASE:**

The Appellant, being a company, had signed a formal Concession Agreement with the Lahore Ring Road Authority ("LRRRA") and had claimed that it was the owner of the Concession Assets and the entire cost incurred for construction was capitalized during the process of construction. Since the first year itself was tax year 2018 for the project, the Appellant claimed depreciation on the same and filed all necessary details of the claim of depreciations. The case of the Appellant was selected for audit in the tax year 2018, whereby it had been confronted that the Appellant had wrongly claimed depreciation in the tax year 2018 by capitalizing cost of the concession assets against the provisions laid down under section 23 of the ITO. The audit proceeding culminated after issuing a show cause notice, and the Additional Commissioner Inland Revenue, thereby, issued notices for subsequent tax years i.e. 2019-2021 and passed orders against all the notices by making addition to the total income on account of disallowance of tax depreciation on concession assets. Therefore, the Appellant filed an appeal before the Commissioner Inland Revenue (Appeals-I), Islamabad ("CIRA") which was again unsuccessful as the CIRA upheld the decision of the Additional Commissioner. Being aggrieved of the decisions passed by the earlier authorities, the Appellant approached the Hon'ble ATIR for adjudication against the matter on a number of grounds. However, the ATIR considered the issue involving the disallowance of depreciation on concession assets as the only pivotal issue.

## **ARGUMENTS BY THE LEARNED APPELLANT:**

The Learned Appellant argued that it was the owner of the concession assets and the entire cost incurred for the construction had been rightly capitalized in the year when the project became operational. Thus, the depreciation claimed under section 23 of the ITO was in place and a note was appended to the depreciation schedule that the right to claim depreciation was reserved by the revenue department. The Learned Appellant also referred to the concession agreement wherein it was stated that the legal and beneficial rights and ownership would be with the Appellant till the transfer date. The Learned Appellant also argued that the assets fell under the purview of the section 23 of the ITO, and that the argument that the transferor could not be held to be an owner of an immovable property unless the transferor has unrestricted and absolute right to transfer the property to everybody does not fit in Pakistan. Furthermore, the Learned Appellant submitted that just because they didn't have the right to destroy the concession assets could not be held that they were not the owner and argued that it would be an objective against public policy and would result to criminal consequences (destruction of road intended for general public). The Learned Appellant contended that the restriction on demolishing was made to protect and benefit the project.

With respect to the contentions regarding inheritance, the learned Appellant argued that inheritance of a corporate entity was regulated by the provisions of the legislation governing the dissolution of corporate entities in Pakistan and determining ownership on this basis was against the facts and law.

Moreover, the learned Appellant also argued that it had been an established principle that inadequate consideration did not render the sale or transfer invalid thus, the Learned Appellant contended that inadequate consideration should not be a factor of hinderance when establishing ownership in the instant case.

## **ARGUMENTS BY THE LEARNED RESPONDENT:**

The learned Respondent contended that the Appellant could not be termed as an owner because it did not have permanent and heritable ownership rights to pass the concession assets to someone else as in inheritance / through sales, neither did the appellant have the right to dispose, convey or destroy the assets. The learned Respondent referred to the Concession Agreement whereby it was categorically specified that the concession assets would be transferred to the LRRRA against Re. 1/- only,, which was malafide against the provisions of the law related to stamp

duty, which would mean that the Appellant was barred from selling or disposing the assets to any other party other than the LRRRA after 25 years, and if the Appellant had “complete ownership” then it would have had absolute right to sell them to any other entity, which in this scenario didn’t exist.

Hence, the learned Respondent argued that the Appellant had wrongly claimed the unlawful depreciation and computed the wrong taxable income under the tax years in question, thereby, the additions were made to total income on account of tax depreciation on concession assets were in order.

### **FINDINGS OF THE ATIR:**

The ATIR accepted the appeal and annulled the orders passed by the lower authorities to the extent of subject matter in appeal. However, the ATIR, considered the following questions the crux of the instant proceeding, which have therefore, been answered accordingly:

- (i) Whether the Appellant is the owner of the “Concession Assets” within the meaning of sub-section (15) of Section 22 of the Income Tax Ordinance, 2001 and it is entitled to claim depreciation thereon?

The ATIR held that in order to claim depreciation, ownership should be valid, and therefore utilized the test developed by the Indian Supreme Court ((1997) 226 ITR 625) and ((1999) 239 ITR 775) after perusing the terms of the Concession Agreement of the Appellant. In order to be an owner, the following 3 conditions were supposed to have been fulfilled:

1. Holding the property to the exclusion of others;
2. Exercising dominion over the property; and
3. Having the right to use and occupy the property.

As the above criteria was duly applicable in this case, the ATIR held that the Appellant was entitled to an allowance of depreciation as claimed, as the Appellant had the right to occupy, control and usufruct for a period of 25 years and therefore can be termed as “Owner”.

- (ii) If the answer to the above question is in the negative, against the appellant then whether the Appellant was entitled to amortize the expenses incurred for the “concession assets” within the meaning of Section 21(n) read with section 24 of the Income Tax Ordinance, 2001?

In case it was found otherwise, there was no dispute to the fact that costs capitalized by the Appellant under the head “License to collect toll” were incurred for the development and construction of the infrastructure facility (Road). The ATIR also held that the Appellant was supposed to build, operate and transfer the said infrastructure within the context of the agreement made with the Government of Punjab, (“GOP”) and expenses ancillary to the project were funded by the Appellant and upon the lapse of the specified period, the Appellant was to transfer the said infrastructure facility to the GOP free of charge. The ATIR also held that the GOP had granted the Appellant the right to use the project site during the concession period. Therefore, the Appellant had rightly claimed the deduction of depreciation.

The ATIR rejected the submission of the learned Respondent and found that the word “contractual rights” and its interpretation did not entail application of the rule of ejusdem generis (of the same kind.) to limit the meaning of “contractual rights”.

(iii) Whether a plea not taken below by the appellant can be raised before this Tribunal?

The ATIR held that there was no estoppel against the law and that it was the duty of the court to apply the correct law. In the absence of any statutory provision, the appellate authority has been vested with all the plenary powers which the subordinate authority may have in the matter. The Appellant was entitled to raise not merely additional legal submissions before the appellate authorities but was also entitled to raise additional claims before them, but it could not be considered that appellate courts had no jurisdiction to consider the same. It was not disputed or contested by the Respondent that the Appellant was not entitled to any deduction. Thus, the ATIR, by relying on various judgments, declared that the taxpayer was indeed entitled to raise additional claims before them. The ATIR referred to the judgement of the Supreme Court of Pakistan (2017 SCMR 1006) wherein it was held that in tax matters, a question not raised below could be agitated before the appellate forum. Therefore, the ATIR held that the plea of amortization and finding can be given by the ATIR, and since it is a statutory forum, it is under a duty to pass factual and legally correct orders.

# **CASE LAW: The Appellate Tribunal Inland Revenue held that it is the gross profit, and not purchases, which should be treated as income.**

## **INTRODUCTION:**

The Hon'ble Appellate Tribunal Inland Revenue, Multan Bench ("ATIR") was moved in the case of Mehboob Hussain ("Appellant") versus The Commissioner Inland Revenue (Appeals-I), Multan ("Respondent") in respect of unexplained investment in purchase of sugar, and thereafter tax had been imposed under Section 111 (1) (d) of the Income Tax Ordinance, 2001 ("ITO") amounting to Rs. 6,986,029/-.

## **BRIEF FACTS OF THE CASE:**

The Appellant was a business individual and had received a notice under section 122(9) of the ITO after the department had received definite information that the Appellant had made investment in purchase of sugar from various sugar manufacturers despite filing his annual return for the tax year under assessment as a business individual for tractors and motors and as a commission agent. The assessing officer did not accept the explanations of the Appellant and thereafter passed an order against the Appellant. Being aggrieved of the said Order, the Appellant filed an appeal before the Respondent who then seconded the Order and thus, resulted to an appeal before the ATIR.

## **ARGUMENTS BY THE COUNSEL FOR THE APPELLANT:**

The counsel for the Appellant argued that the Orders passed by the Assessing officer and the Respondent were bad in law and contrary to the facts. Furthermore, the Appellant contended that the sugar they received was in exchange of the sale price of sugarcane supplied to the sugar mill. The Appellant also argued that the Assessing officer had erred in adding back the income without taking into consideration the cost of sales in case of undeclared sales/purchase which vide a recent judgement had been made mandatory.

### **ARGUMENTS BY THE COUNSEL FOR THE RESPONDENT:**

The counsel for the Respondent argued that the Appellant had failed to provide documentary evidences which would have been acceptable or could have substantiated that the receipts of sugar were made in consideration of the supply of sugarcane to the sugar mills. Therefore, the Respondent argued that the Orders passed were well reasoned and according to the facts and thus, prayed for upholding of the Orders.

### **FINDINGS OF THE ATIR:**

The Hon'ble ATIR held that both Orders passed by the lower authorities were not sustainable in the eyes of law as they did not consider the fact that the Appellant was a farmer and sold sugarcane in exchange of an equal sugar from the sugar mill and had furnished a certificate issued by the sugar mill in this regard. The ATIR also found that the assessing officer and Respondent had failed to inquire whether the agricultural land was under the ownership of the Appellant or not in the first place.

Secondly, regarding the alleged false claim of receiving sugar raised by the Respondent, the ATIR found that the difference between the records known to the tax authorities and actual declarations made by the Appellant were due to the cost of sales and therefore the Respondent was not valid in charging income without taking the cost of sales into consideration. The ATIR also found that the actual suppressed income should have been the gross profit admittedly derived by the Appellant. Moreover, the ATIR found that the Appellant did not declare the purchase of sugar in his tax return for the said year but to add the total amount of undeclared sales/purchases without allowing the cost of sales was directly countering the recent ruling of the Supreme Court of Pakistan. Therefore, both Orders were set aside and the case was remanded back with the directions to the Appellant to provide all evidences and record to support this claim, and to the assessing officer that he should communicate in writing to the taxpayer before making a fresh decision if any observation of any incongruity in evidence and record is found.



# Topic of the month- Revocable Transfer of Assets

## **INTRODUCTION:**

Transfer of assets is one of the methods utilized by the taxpayers to minimize their tax liability. However, there are also other intentions behind such transfers and tax avoidance is not the only motive.

## **General Rule:**

Section 90 of the Income Tax Ordinance (“ITO”) provides about the treatment of the income generated out of transferred assets. The general rule as per section 90 is that in case of a revocable transfer of assets, the income generating from such asset will be treated to be the income of the transferor and not the transferee. For example, Mr. A transfers shares valuing Rs. 3 million to his friend Mr. B on the condition that Mr. B will retransfer the shares to Mr. A whenever Mr. A wants. The shares generate a dividend income of Rs. 420,000 per year. This dividend income will be deemed to be the income of Mr. A and not Mr. B.

There are also certain exceptions to this general rule which we will discuss in the coming paragraphs. But first let us discuss some of the terms used in the section to better understand the tax implications.

## **Definitions:**

- **Revocable asset:**

A transfer of an asset shall be treated as revocable if:

- There is any provision in the agreement for the re-transfer, directly or indirectly, of the whole or any part of the asset; or
- The transferor through any way has the right to resume power directly or indirectly over the whole or any part of the asset.

- **Transfer of asset:**

Transfer of asset includes:

- o Disposition;
- o Settlement;
- o Trust;
- o Covenant;
- o Agreement; or
- o Arrangement

- **Minor Child:**

A minor child, for the purpose of section 90, means child of the transferor below the age of 18 years except a married daughter.

## **Exceptions:**

The general rule as discussed above will not be applicable to the following exceptions:

1. In case the transferor makes a revocable transfer but the terms of the revocation such that the revocation is not exercised during the life time of the transferee and the transferor does not derive any benefit, directly or indirectly, from the income of such transferred asset.

**For example**, Mr. A, living in United States of America, transfers his flat in Pakistan in the name of his mother so that the rent from such flat is received by his mother. There is also a provision in the agreement to transfer that such flat will be retransferred to Mr. A in case of death of his mother. Mr. A also does not derive any benefit from such rent. In such a case, the rental income will not be deemed to be the income of Mr. A, even though the transfer is revocable.

2. Where there is a transfer of asset but the asset remains the property of the transferor, any income arising from the asset will be treated as income of the transferor. **For example**, Mr. A owns shares in XYZ limited and transfers such shares to Mr. B as a security for a loan he has obtained from Mr. B. In such a case, even though the shares have been transferred but they remain the property of the transferor and any dividend from such shares will be deemed to be the income of the transferor.

3. In case there is a transfer of asset to:
  - a. The spouse of the transferor;
  - b. Minor child of the transferor; or
  - c. Any other person for the benefit the spouse or minor child of the person, the income arising from such asset will be treated as income of the transferor irrespective of the fact whether the transfer was revocable or not.

However, in case the above transfer is for adequate consideration or the transfer is in connection with an agreement to live apart, the income from the asset will not be deemed as income of the transferor. The transferor will be required to show the evidence of transfer of asset by way of its registration or mutation in the relevant records.

Conversely, in case the asset is transferred to the person's minor child or spouse for an adequate consideration, but the funds for such consideration have been provided, by the transferor either directly or indirectly, such transfer will not be treated as a transfer for adequate consideration and, consequently, income from such asset will be treated as income of the transferor.

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