

IN THE HIGH COURT OF SINDH AT KARACHI

Present:
Muhammad Junaid Ghaffar, J.
Agha Faisal, J.

CP D 4970 of 2017

Sapphire Textile Mills Limited
Vs.
Federation of Pakistan & Others

(And connected petitions, particularized in the Schedule¹ hereto.)

For the Petitioners : Mr. Hyder Ali Khan, Advocate
Mr. Qazi Umair Ali, Advocate
Mr. Hussain Ali Almani, Advocate
Mr. Ovais Ali Shah, Advocate
Mr. Ahmed Hussain, Advocate
Mr. Amin Bandukda, Advocate
Mr. Hussain Shah, Advocate
Mr. Rizwan Ahmed, Advocate
Mr. Arshad Hussain Shehzad, Advocate
Mr. Rana Sakhawat Ali, Advocate
Mr. Abdul Ahad, Advocate
Mr. Abdul Qadir Mirza, Advocate
Mr. Naseer Nihal Hashmi, Advocate
Mr. Abbas Razvi, Advocate
Mr. Shoaib Khatian, Advocate
Mr. Ghulam Hussain Shah, Advocate
Mr. Yahya Iqbal, Advocate
Mr. Asad Iftikhar, Advocate
Mr. Rahim Khan, Advocate

For the Respondents: Mr. Kafeel Ahmed Abbasi
Deputy Attorney General
Mr. Ameer Bux Metlo, Advocate
Mr. Shahid Ali Qureshi, Advocate
Mr. M. Zubair Hashmi, Advocate
Ms. Naheed Akhtar, Advocate
Mr. Imran Ali Mithani, Advocate
Dr. Shahnawaz Memon, Advocate
Mr. Aqeel Qureshi, Advocate
Mr. Iqbal Khurram, Advocate
Dr. Raana Khan, Advocate

Dates of hearing : 13.10.2020; 03.11.2020; 16.11.2020;
17.12.2020; 03.03.2021; 24.03.2021.

Date of announcement : 30.04.2021

JUDGMENT

Agha Faisal, J. The present petitions have assailed the *vires* of section 5A (“5A”) of the Income Tax Ordinance 2001 (“Ordinance”) and seek for the same to be declared unconstitutional. The respective petitions were heard and reserved conjunctively and shall be determined vide this common judgment.

¹ The Schedule hereto shall be read as an integral constituent hereof.

Factual context

2. Briefly stated, 5A was initially inserted in the Ordinance, vide the Finance Act 2015 (“FA 2015”) and amended, relevant to the present *lis*, vide the Finance Act 2017 (“FA 2017”), ostensibly in order to induce certain (*not all*) public companies to distribute dividends among their shareholders². It is considered illustrative to reproduce the provision, under challenge, herein below:

“Tax on undistributed profits. (1) For tax years 2017 to 2019, a tax shall be imposed at the rate of five percent of its accounting profit before tax on every public company, other than a scheduled bank or a modaraba, that derives profit for a tax year but does not distribute at least twenty percent of its after tax profits within six months of the end of the tax year through cash:

(Underline added for emphasis.)

Provided that for tax year 2017, bonus shares or cash dividends may be distributed before the due date mentioned in sub-section (2) of section 118, for filing of a return.

(2) The provisions of sub-section (1) shall not apply to (a) a company qualifying for exemption under clause (132) of Part I of the Second Schedule; and (b) a company in which not less than fifty percent shares are held by the Government.”

3. In its original form³, as inserted per FA 2015, the tax was levied upon the reserves of a company; whereas, post FA 2017 the levy befell upon accounting profit before tax of a company.

Respective arguments

4. Petitioners’ learned counsel submitted that it was the duty of the Court to uphold the constitutionality of a statutory provision, within context⁴, and for a tax to qualify under the Federal Legislative List it had to be covered between entries 43 to 53 therein⁵, since the source and extent of the statutory taxing power had to be derived from a corresponding legislative entry⁶.

It was sought to be demonstrated that a plain reading of 5A suggests that it amounts to double taxation, as income received or taxed in the same hand ceases to be income⁷. Per learned counsel, double taxation could only be

² Per Circular 2 of 2015, numbered C.No.4(18)R&S/2015 and dated 24.07.2015, issued by the Federal Board of Revenue.

³ Tax on undistributed reserves. (1) Subject to this Ordinance, a tax shall be imposed at the rate of ten percent, on every public company other than a scheduled bank or a modaraba, that derives profits for a tax year but does not distribute cash dividends within six months of the end of the said tax year or distributes dividends to such an extent that its reserves, after such distribution, are in excess of hundred percent of its paid up capital, so much of its reserves as exceed hundred per cent of its paid up capital shall be treated as income of the said company...

⁴ *Abdul Aziz vs. Province of West Pakistan* reported as *PLD 1958 SC 499*; *Inamur Rehman vs. Federation of Pakistan* reported as *1992 SCMR 563*; *Pakistan vs. Hazrat Hussain* reported as *2018 SCMR 939*.

⁵ *Federation of Pakistan vs. Durrani Ceramics* reported as *2014 SCMR 1630*.

⁶ *Pakistan International Freight of Forwarders Association vs. Sindh* reported as *2017 PTD 1*.

⁷ *Pakistan Industrial Development Corporation vs. Pakistan* reported as *1992 SCMR 891*; *Keshav Mills Ltd vs. Commissioner Income Tax* reported as *23 ITR 230*; *In Re: B.M Kamdar* reported as *14 ITR 10*; *Sambhaji Rao vs. State*

imposed in clear specific language and the law precluded the presumptive imposition of the same⁸.

Per petitioners' counsel, the regulation of companies is undertaken *inter alia* vide the Companies Act 2017 ("Act"), being special in nature, and any attempt at such regulation by inserting penal provisions into the Ordinance, routed through a money bill, was *prima facie* unmerited.

5. Learned counsel for the respondents submitted that 5A did not amount to double taxation as it contemplated an independent levy. It was argued that 5A identified a class to be taxed, hence, could not be considered discriminatory. It was concluded that the legislature had ample power to regulate economic behavior and 5A was merely one specie of exercise of such power.

The learned deputy attorney general unequivocally stated that the purpose of inserting 5A into the Ordinance was to incentivize the distribution of profits by companies and to keep companies compliant with the requirements of company law. Specific reference was made to sections 240 and 243 of the Act to argue that distribution of dividends was a mandatory requirement of the law and 5A of the Ordinance was a supplemental provision thereto. It was submitted that the levy was analogous to super tax; hence, valid in respect of the same income.

Scope of this determination

6. The petitioners' contention, that 5A was inserted in the Ordinance to regulate matters pertaining to company law, appears to have been seconded by the learned Deputy Attorney General.

While the departmental counsel articulated no cavil in such regard, the same is also manifest from Circular 2 of 2015, numbered C.No.4(18)R&S/2015 and dated 24.07.2015, issued by the Federal Board of Revenue. It is considered illustrative to reproduce the pertinent constituents of the circular herein below:

"GOVERNMENT OF PAKISTAN
REVENUE DIVISION
FEDERAL BOARD OF REVENUE

C.No. 4(18)R&S/2015

Islamabad, the 24th July, 2015

of MP reported as *ILR 1975 MP 475*; *Commissioner Inland Revenue vs. Frank Bernard Sanderson* reported as *1921 8 Tax cases 38*.

⁸ *Haji Muhammad Shafi vs. Wealth Tax Officer* reported as *1992 PTD 726*; *Pakistan Industrial Development Corporation vs. Pakistan* reported as *1992 SCMR 891*; *HBL Stock Fund vs. Pakistan & others* reported as *C.P. No.D-1849 of 2016*; *D.G Khan Cement Company vs. Pakistan* reported as *2018 PTD 287*; *D.G Khan Cement Company vs. Pakistan* reported as *2020 PTD 1186*; *Tennessee vs. Whitworth* reported as *117 US 129*.

Circular No.2 of 2015
(Income Tax)

SUBJECT: FINANCE ACT, 2015 – EXPLANATION REGARDING IMPORTANT AMENDMENTS MADE IN THE INCOME TAX ORDINANCE, 2001.

Important amendments made in the Income Tax Ordinance, 2001 through Finance Act 2015, are explained as under...

2. Tax on undistributed reserves [Section 5A] Through Finance Act, 2015 a new section 5A has been introduced whereby in order to persuade the public companies to distribute dividend among their shareholders and to encourage investment in stock market, tax at the rate of ten percent has been imposed on every public company except scheduled bank or a modaraba that derives profits in a tax year but does not distribute cash dividend within six months of the end of the tax year or where the said company distributes dividend in such a way that after distribution of the dividend, the company's reserves are in excess of hundred percent of its paid up capital..."

(Underline added for emphasis.)

7. The Federal Board of Revenue issued another circular, being Circular 04 of 2017, to explain the amendments in the Ordinance brought in vide the FA 2017. The circular expressly states that the basis of the levy, envisaged vide 5A, is solely dependent upon the extent to which a company distributes its profits. It may be beneficial to reproduce the pertinent constituent of the aforementioned circular herein below:

"GOVERNMENT OF PAKISTAN
REVENUE DIVISION
FEDERAL BOARD OF REVENUE

C.No. 4(49)IT-Budget/2017

Islamabad, the 6th September, 2017

Circular No.4 of 2017
(Income Tax)

SUBJECT: FINANCE ACT, 2017 – EXPLANATION OF IMPORTANT AMENDMENTS MADE IN THE INCOME TAX ORDINANCE, 2001.

Finance Act 2017 has brought certain amendments in the Income Tax Ordinance 2001. Some important amendments are explained hereunder:

8. Tax on undistributed profits [Section 5A]

A tax on undistributed reserves was introduced vide the Finance Act 2015 ...

... The basis of levy of such tax, is therefore solely dependent upon the extent to which a public company distributes / disburses its after tax profits...

(Underline added for emphasis.)

8. Finally, this purpose, for inserting 5A in the Ordinance, is also borne from the budget speech of the Finance Minister, Budget 2017-2018, delineating the *raison d'être* of 5A, wherefrom it was manifest that the provision was always intended to ensure that shareholders get their return on investment by *encouraging* companies to distribute dividends. Reliance upon the relevant budget documents is a judicially recognized means of assessment of statutory provisions, as demonstrated by the honorable Supreme Court in *Durrani Ceramics*⁹ and followed by this Division Bench in *MSC Switzerland Geneva*¹⁰.

The aforementioned narration demonstrates that the fundamental question to address would be *whether the Constitution permits admitted*

⁹ *Federation of Pakistan & Another vs. Durrani Ceramics & Others* reported as 2014 SCMR 1630.

¹⁰ *CIR vs. MSC Switzerland Geneva (ITRA 13 of 2018)*.

regulation of matters falling within the manifest remit of the Companies Act 2017 by recourse through a money bill.

9. The petitioners had *inter alia* contended that 5A amounted to impermissible double taxation on the same income. The learned Deputy Attorney General concurred to the extent that the levy being on the same income; however, articulated that it was permissible on the analogy of super tax. The departmental counsel¹¹ disagreed with the petitioners' counsel and the learned Deputy Attorney General and submitted that 5A did not amount to double taxation, as it envisaged a levy independent of income tax.

10. The august Supreme Court has illumined that courts ought to abstain from deciding larger questions, if a case could be decided on narrower grounds and that it was preferred for the courts to confine determinations to questions pivotal for the determination of a case¹². It is our considered view that a determination herein could be clinched by answering the fundamental question framed supra, therefore, we deem it prudent to eschew deliberation upon the question of double taxation and leave the matter for future consideration in an appropriate case¹³.

Money Bills - Article 73

11. Article 73 of the Constitution deals with money bills and elucidates that recourse thereto may be had for taxation and certain pertinent matters, delineated therein. The law defines tax as a compulsory exaction of monies by public authorities for utilization for public purposes. The august Supreme Court has maintained in the *WWF case*¹⁴ that the distinguishing feature of tax is that it imposes a common burden for raising revenues for a general, as opposed to specific, purpose.

12. It has been successfully demonstrated before us that the intent for inserting 5A in the Ordinance was specifically to supplement the provisions of the Act in so far as distribution of dividends by certain public companies was concerned; hence, admittedly not for raising revenues for a general purpose. In such context, no case has been made out before us to consider 5A amenable for promulgation vide a money bill.

¹¹ Mr. Ameer Bux Maitlo, Advocate.

¹² Per Saqib Nisar J (as he then was) in *LDA & Others vs. Imrana Tiwana & Others* reported as 2015 SCMR 1739.

¹³ Per Munib Akhtar J in *Shahid Gul & Partners vs. DCIT Peshawar* reported as 2021 SCMR 27.

¹⁴ Per Mian Saqib Nisar J (as he then was) in *Workers Welfare Funds & Others vs. East Pakistan Chrome Tannery (Pvt.) Ltd.* reported as PLD 2017 Supreme Court 28.

Provisions related to dividends per Companies Act 2017

13. Learned Deputy Attorney General had submitted that the sections 240 and 243 of the Act *mandated* distribution of dividends and 5A was a supplemental provision thereto. A perusal of the referenced provisions demonstrates to the contrary as section 240¹⁵ places restrictions upon distribution of dividends and section 243¹⁶ requires that *directors* may not withhold a dividend once it is declared. Respondents' learned counsel remained unable, despite repeated queries by us, to assist us with any provision of the Act whereby companies could be mandated to declare dividends.

14. It is manifest that the Act itself neither contains any mandatory requirement for declaring dividends nor any prejudicial consequences for the same. While the Parliament may have the right to vary the law in such regard, the exercise of any such right does not appear to be merited *vide* recourse through a money bill.

Ambit of a money bill

15. The august Supreme Court has consistently maintained that bypass of the regular legislative process, by unmerited recourse to money bills, could not be appreciated. *Mian Saqib Nisar J (as he then was)* illumined upon the ambit of Article 73 of the Constitution in the *WWF case*¹⁷ and observed as follows:

“not everything that pertains to finance would necessarily be related to tax. Therefore, merely inserting amendments, albeit relating to finance but which have no nexus to tax, in a Finance Act does not mean that such Act is a Money Bill as defined in Article 73(2) of the Constitution. The tendency to tag all matters pertaining to finance with tax matters (in the true sense of the word) in Finance Acts must be discouraged, for it allows the legislature to pass laws as Money Bills by bypassing the

¹⁵ 240. Certain restrictions on declaration of dividend. (1) The company in general meeting may declare dividends; but no dividend shall exceed the amount recommended by the board. (2) No dividend shall be declared or paid by a company for any financial year out of the profits of the company made from the sale or disposal of any immovable property or assets of a capital nature comprised in the undertaking or any of the undertaking of the company, unless the business of the company consists, whether wholly or partly, of selling and purchasing any such property or assets, except after such profits are set off or adjusted against losses arising from the sale of any such immovable property or assets of a capital nature: Provided that no dividend shall be declared or paid out of unrealized gain on investment property credited to profit and loss account.

¹⁶ 243. Directors not to withhold declared dividend. (1) When a dividend has been declared, it shall not be lawful for the directors of the company to withhold or defer its payment and the chief executive of the company shall be responsible to make the payment in the manner provided in section 242...

¹⁷ Per *Mian Saqib Nisar J (as he then was)* in *Workers Welfare Funds & Others vs. East Pakistan Chrome Tannery (Pvt.) Ltd.* reported as *PLD 2017 Supreme Court 28*.

regular legislative procedure under Article 70 of the Constitution by resorting to Article 73 thereof which must only be done in exceptional circumstances as and when permitted by the Constitution. The special legislative procedure is an exception and should be construed strictly and its operation restricted.”

16. It is settled law that while a legislature may make laws within its legislative competence; however, the legislative field may be circumscribed, limited and / or qualified¹⁸. If a legislature has overstepped the limits of its power and if such transgression is indirect, covert or disguised then such legislation may fall within the pale of colorable legislation¹⁹. *H M Serva*²⁰ expounded on colorable legislation and stated that while pretending to be a law in the exercise of undoubted power, it is in fact a law on a prohibited field²¹.

In consideration of the foregoing, we are constrained to observe that respondents' learned counsel have remained unable to provide any justification for legislation pertaining to governance of dividend related behavior, of certain public companies, having been enacted through a money bill.

Entries in the Federal Legislative List

17. The august Supreme Court has recognized in *Durrani Ceramics*²² that for an imposition to qualify as a tax, under the Federal Legislative List, it may be covered within entries 43 to 53 therein.

18. The Constitution empowers the Parliament to *regulate* corporations, per entry 31 of the Federal Legislative List. The power to regulate the declaration and distribution of dividends by corporations appears to fall within the domain of the said entry and no cavil in such regard has been articulated before us.

19. There is another entry in the Federal Legislative list, being entry 48; in respect of taxes on corporations. This entry empowers the Parliament to levy *taxes* on corporations. By definition, a tax is required to be a common burden for raising revenues for a general purpose. It is our deliberated view that 5A is not covered by entry 48²³; as 5A does not manifest itself to be a common burden

¹⁸ *KC Gajapati Natayan Deo vs. Orissa* reported as AIR 1953 SC 375; *G Nageswara Rao vs. Andhra Pradesh State Road Transport* reported as AIR 1959 SC 308.

¹⁹ *Ashok Kumar Alias Golu vs. Union of India* reported as [(1991) 3 SCC 498].

²⁰ *Constitutional Law of India, A Critical Commentary (Third Edition)* by H.M.Servai.

²¹ Relied upon by a Seven member judgment of the honorable Supreme Court in *Federation of Pakistan vs. Shaukat Ali Mian* reported as PLD 1999 Supreme Court 1026.

²² *Federation of Pakistan vs. Durrani Ceramics* reported as 2014 SCMR 1630; page 1654.

²³ Or entry 47; on the same analogy.

for raising revenues for a general purpose at all and instead seeks to target an additional levy on certain public companies with the objective to encourage / incentivize dividends.

20. Since, no case has been made out to qualify the enactment of 5A within the legislative remit of entries 43 to 53 of the Federal Legislative List, therefore, it is observed that such legislation could not have been endeavored vide a money bill.

Conclusion

21. It has been established that section 5A of the Ordinance amounts to legislation, not contemplated in the Constitution to be undertaken vide a money bill. In such a scenario no rationale has been articulated before us to justify the regulation of companies' behavior, pertaining to dividends, to be effected vide a money bill, within the mandate of Article 73 of the Constitution, while abjuring the regular legislative process. Therefore, it is our deliberated view that section 5A of the Income Tax Ordinance 2001 cannot be sustained on the constitutional anvil; hence, could not be construed to have legal effect.

22. In view of the reasoning and rationale herein deliberated, these petitions are allowed in terms delineated herein below:

- i. It is hereby declared that insertion of section 5A in the Income Tax Ordinance 2001, including amendments thereto from time to time, does not fall within the parameters delineated per Article 73 of the Constitution of Pakistan, 1973, hence, the provision impugned is found to be *ultra vires* of the Constitution, and is hereby struck down.
- ii. As a consequence, any show cause / demand notices²⁴ or constituents²⁵ thereof, seeking enforcement of section 5A of the Income Tax Ordinance 2001, are hereby set aside.

JUDGE

JUDGE

²⁴ *Usmani Glass v. STO*, reported as PLD 1971 SC 205; *Dewan Cement v. Pakistan*, reported as 2010 PTD 1717; *Filters Pakistan v. FBR*, reported as 2010 PTD 2036; *Shahnawaz Ltd. V. Pakistan*, reported as 2011 PTD 1558; *Engro Vopak v. Pakistan*, reported as 2012 PTD 130; and *Association of Builders v. Sindh*, reported as 2018 PTD 1487.

²⁵ *Engro Vopak v. Pakistan*, reported as 2012 PTD 130; *Standard Chartered Bank v. Pakistan*, reported as 2017 PTD 1585; and *Asia Petroleum v. Pakistan*, Unreported (CP D 2559 of 2009 & Others).

Schedule

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| CP D 4727 of 2017; Sameer Arif vs. Federation of Pakistan & Others | CP D 4971 of 2017; Javedan Corp. Ltd. vs. Federation of Pakistan & Others |
| CP D 4972 of 2017; TPL Direct Insurance Ltd. vs. Pakistan & Others | CP D 4973 of 2017; Aisha Steel Mills Ltd. vs. Pakistan & Others |
| CP D 4974 of 2017; Sapphire Fibre Ltd. vs. Pakistan & Others | CP D 4975 of 2017; Dawood Hercules Corp. Ltd. vs. Pakistan & Others |
| CP D 4976 of 2017; Lucky Cement Ltd. vs. Pakistan & Others | CP D 4977 of 2017; Thal Ltd. vs. Pakistan & Others |
| CP D 5080 of 2017; Reliance Cotton Spinning Mills Ltd. vs. Pak. & Others | CP D 5083 of 2017; Engro Polymer and Chemical Ltd. vs. Pakistan & Others |
| CP D 5084 of 2017; Dawood Lawrencepur Ltd. vs. Pakistan & Others | CP D 5086 of 2017; Engro Corp. Ltd. vs. Pakistan & Others |
| CP D 5431 of 2017; J.S. Global vs. Federation of Pakistan & Others | CP D 5432 of 2017; Jahangir Siddiqui & Co. Ltd. vs. Pakistan & Others |
| CP D 5466 of 2017; Otsuka Pakistan Ltd. vs. Federation of Pak & Others | CP D 5529 of 2017; Attock Cement Pakistan Ltd. vs. Pakistan & Others |
| CP D 5561 of 2017; J.S. Investment Ltd. vs. Federation of Pak & Others | CP D 5897 of 2017; Pakistan Refinery Ltd. vs. Federation of Pak & Others |
| CP D 5898 of 2017; Mirpurkhas Sugar Mills vs. Federation of Pak & Others | CP D 6143 of 2017; Ismail Industries Ltd. vs. Federation of Pak & Others |
| CP D 6213 of 2017; Tata Textile Mills Ltd. vs. Federation of Pak & Others | CP D 6242 of 2017; Glaxo Smith Kline vs. Federation of Pakistan & Others |
| CP D 6403 of 2017; Lotte Chemical Pakistan vs. Pakistan & Others | CP D 6404 of 2017; TPL Properties Ltd. vs. Federation of Pakistan & Others |
| CP D 6444 of 2017; Sitara Chemical Industries Ltd. vs. Pakistan & Others | CP D 6450 of 2017; Fecto Cement Ltd. vs. Federation of Pakistan & Others |
| CP D 6451 of 2017; Hum TV Network Ltd. vs. Federation of Pak & Others | CP D 6463 of 2017; Power Cement Ltd. vs. The Commissioner I.R & Others |
| CP D 6541 of 2017; Buxly Paints Limited vs. Federation of Pak & Others | CP D 6558 of 2017; Pak Suzuki Moto Co. vs. Pakistan & Others |
| CP D 6598 of 2017; BIPL Securities Ltd. vs. Federation of Pakistan & Others | CP D 6619 of 2017; Towellers Ltd. vs. Federation of Pakistan & Others |
| CP D 7202 of 2017; Faran Sugar Mills Ltd. vs. Pakistan & Others | CP D 7258 of 2017; Exide Pakistan Limited vs. Pakistan & Others |
| CP D 7317 of 2017; Sanofi Aventis Pakistan Ltd. vs. Pakistan & Others | CP D 7621 of 2017; Deewan Cement Ltd. vs. Federation of Pak & Others |
| CP D 7734 of 2017; Engro Foods Ltd. vs. Pakistan & Others | CP D 8029 of 2017; Byco Petroleum Pakistan Ltd. vs. Pakistan & Others |
| CP D 8409 of 2017; Crescent Fibres Ltd. vs. Federation of Pak & Others | CP D 8898 of 2017; Saarim Enterprises vs. Federation of Pakistan & Others |
| CP D 8925 of 2017; Idrees Textile Mills Ltd. vs. Federation of Pak & Others | CP D 1039 of 2018; Singer Pakistan Ltd. vs. Federation of Pak & Others |
| CP D 2784 of 2018; Arabian Sea Enterprises vs. Federation of Pak & Others | CP D 5768 of 2018; Indus Dyeing & Manufacturing Co. vs. Fed. of Pak & Others |
| CP D 6505 of 2018; Sunrays Textile Mills Ltd vs. Federation of Pak & Others | CP D 6802 of 2018; Hum Network Ltd. vs. Sindh & Others |
| CP D 8670 of 2018; JS Global Capital (Ltd) vs. Pakistan & Others | CP D 8671 of 2018; JS Investment Ltd. vs. Pakistan & Others |
| CP D 8672 of 2018; Jahangir Siddiqui & Co. Ltd. vs. Pakistan & Others | CP D 3966 of 2019; Fecto Cement Ltd. vs. Federation of Pakistan & Others |
| CP D 5996 of 2019; Thatta Cement Co. Ltd. vs. The Commissioner IR & Others | |