





1. Brief note on the short order issued by the Honorable High Court of Sindh in the constitutional petition challenging the constitutionality of section 65B of the Income Tax Ordinance 2001, as amended through Finance Act 2019.

1. PREAMBLE

Section 65B of the Income Tax Ordinance 2001 ("ITO") was introduced /enacted vide Finance Act 2010. At that time, section 65B read as under:

QUOTE

65B. TAX CREDIT FOR INVESTMENT:

- 1) Where a taxpayer being a company invests any amount in the purchase of plant and machinery, for the purposes of balancing, modernization, and replacement of the plant and machinery already installed therein, in an industrial undertaking setup in Pakistan and owned by it, credit equal to ten percent of the amount so invested shall be allowed against the tax payable by it in the manner hereinafter provided.
- 2) The provision of subsection (1) shall apply if the plant and machinery is purchased and installed at any time between the first day of July, 2010, and the 30th day of June, 2015.
- 3) The amount of credit admissible under this section shall be deducted from the tax payable by the taxpayer in respect of the tax year in which plant and machinery in the purchase of which the amount referred to in subsection (1) is invested and installed.
- Where no tax is payable by the taxpayer in respect of the tax year in which such plant and machinery is installed, or where the tax payable is less than the amount of credit, the amount of the credit or so much of it as is in excess thereof, as the case may be, shall be carried forward and deducted from the tax payable by the taxpayer in respect of the following tax year, and so on, but no such amount shall be carried forward for more than two years, however, the deductions made under subsection (2) and this subsection shall not exceed in aggregate the limit specified in subsection (1).
- 5) Where any credit is allowed under this section and subsequently it is discovered by the commissioner inland Revenue that any one or more of the conditions specified in this section was, or were, not fulfilled, as the case may

be, the credit originally allowed shall be deemed to have been wrongly allowed and the Commissioner Inland Revenue may, notwithstanding anything contained in this ordinance, re-compute the tax payable by the taxpayer for the relevant year and the provisions of this ordinance shall, so far as may be, apply accordingly.

UNQUOTE

The aforesaid section was amended, and the timeframe extended, through subsequent amendments introduced through later finance acts.

Through amendments introduced vide Finance Act 2018, the benefit of section 65B was supposed to remain till 30th June 2021 with a 10% tax credit available to the qualified companies. However, an amendment through Finance Act 2019 ("**FA 19**") was made, by virtue of which the tax credit was reduced to 5% for Tax Year 2019 and timeframe for the investment was also reduced to 30th June 2019.

AFTER THE AFORESAID AMENDMENT, SECTION 65B READ AS UNDER:

QUOTE

65B. TAX CREDIT FOR INVESTMENT:

- 1) Where a tax payer being a company invests any amount in the purchase of plant and machinery, for the of extension, expansion, balancing, purposes modernization, and replacement of the plant and machinery already installed therein, in an industrial undertaking setup in Pakistan and owned by it, credit equal to ten percent of the amount so invested shall be allowed against the tax payable, including on account of minimum tax and final taxes payable under any of the provisions of this ordinance, by it in the manner hereinafter provided. Provided that for the tax year 2019 the rate of credit shall be equal to five percent of the amount so invested. Provided further that the provision of subsection (5) relating to carry forward of the credit to be deducted from tax payable, for the following tax years, as specified in the said subsection, shall continue to apply after tax year 2019, and
- 2) The provision of subsection (1) shall apply if the plant and machinery is purchased and installed at any time between the first day of July, 2010, and the 30th day of June, 2019.



- 3) The amount of credit admissible under this section shall be deducted from the tax payable by the taxpayer in respect of the tax year in which plant and machinery in the purchase of which the amount referred to in subsection (1) is invested and installed.
- The provision of this section shall mutatis mutandis applies to a company setup in Pakistan before the first day of July, 2011, which makes investment through hundred percent new equity, during first day of July, 2011 and 30th day of June, 2016, for the purpose of balancing, modernization and replacement of the plant and machinery already installed in an industrial undertaking owned by the company. However, credit equal to twenty percent of the amount so invested shall be allowed against the tax payable, including an account of minimum tax and final tax payable under any of the provisions of this ordinance. The credit shall be allowed in the year in which the plant and machinery in the purchase of which the investment as aforesaid is made, is installed therein.

"Explanation---For the purposes of this section the term "new equity" shall, have the same meaning as defined in subsection (7) of section 65E.

- of the tax year in which such plant or machinery is installed , or where the tax payable is less than the amount of credit as aforesaid, the amount of the credit or so much of it as is in excess thereof, as the case may be, shall be carried forward and deducted from the tox payable by the taxpayer in respect of the following tax year and so on, but no such amount shall be carried forward for more than two tax years in the case of investment referred to in subsection (1) and for more than five tax years in respect of investment referred to in subsection (4), however, the deduction made under this section shall not exceed in aggregate the limit specified in 51.013-Section (1) or subsection (4), as the case may be
- Where any credit is allowed under this section and subsequently it is discovered by the Commissioner Inland Revenue that any one or more of the conditions specified in this section was, or were, not fulfilled,, as the case may be, the credit originally allowed shall be deemed to have been wrongly allowed and the commissioner; notwithstanding anything contained in this Ordinance, shall re-compute the lax payable by the taxpayer for the relevant year and the provisions of this Ordinance shall, so for as may be, apply accordingly.

UNQUOTE

2. ARGUMENTS BY THE PETITIONERS' COUNSEL

The Petitioners through their counsels challenged the Constitutionality of Section 65B of the ITO (as amended by the FA 19) on, inter-alia, grounds that past and closed transactions cannot be reopened, vested rights created by a specific provision of law cannot be rescinded by an amendment of the same, that whilst construing a provision intending retrospective effect and dealing with vested rights, the words used in the provision cannot be stretched to include matters that do not fall within the plain language of the provision.

3. DECISION OF THE HONOURABLE SHC VIDE SHORT ORDER DATED 7th FEBRUARY 2023

THE HONORABLE SINDH HIGH COURT HAS DECIDED AS FOLLOWS:

- 1. The SHC has decided to remove the retrospective effect given through Section 65B(2) (as amended through FA 2019). The Honorable SHC has held that Section 65B(2) shall be read to reflect that Section 65B(1) of the ITO shall apply if the plant and machinery was purchased before 30th June 2019 and installed before 30th June 2021.
- 2. Moreover, the SHC has further held that Section 65B(3) shall be read as that the amount of credit admissible under Section 65B shall be deducted from the tax payable by the taxpayer in respect of the tax year in which the plant or machinery is installed. Meaning thereby, that the tax credit admissible will be deducted in the tax year in which the plant or machinery is installed.
- **3.** The department shall determine whether the said plant or machinery to which the tax credit pertains, was purchased before 30th June 2019 and installed before 30th June 2021.
- **4.** The following proviso introduced vide FA 19 has been struck down by the SHC:

QUOTE

Provided that for the tax year 2019 the rate of credit shall be **equal to five percent** of the amount so invested

UNQUOTE



4. OUR EXPLANATORY COMMENTS

The said decision of the SHC means that the tax credit relating to the plant and machinery purchased before 30th June 2019 that was mainly hit by the amendment of Finance Act 2019, has been allowed as admissible and will be deductible if the machinery was installed before 30th June 2021. The restriction of up to 30th June 2021 seems to emanate from the position prior to FA 19, i.e. Section 65B as amended through FA 2018.

Moreover, as per this decision, the tax credit shall be deductible against the tax payable by the taxpayer. Since the admissibility and deductibility of the tax credit has been restricted up to Normal Tax Year 2021, it is likely that the taxpayer shall revise its income tax returns from Tax Year 2019 to Tax Year 2021, whereafter the tax authorities shall first determine whether the plant and machinery was purchased before 30th June 2019 and installed before 30th June 2021, before allowing revision of such income tax returns.

Lastly, the proviso restricting the rate of credit to 5% in Tax Year 2019 of the amount invested, has been struck down by the SHC. This means that the rate of credit allowed shall be 10% of the amount invested in terms of Section 65(B)(1) of the ITO.

DISCLAIMER

The judgment discussed in this document was recently announced by the honorable Sindh High Court. These comments are based on our understanding of tax law and past practices. These comments are provided for general use of public and should not be used for any specific transaction. We do not guarantee that these comments/interpretations will be acceptable by the tax department. This document is not and shall not be construed to be a legal opinion, legal assistance, a legal advice, or a financial advice for, inter-alia, investing, managing taxes, incorporating any legal entities. Tola & Tola does not assume, nor does it bear any responsibility, financial or otherwise, that can or may arise out of the use of this document by any individual or entity. Moreover, the laws (including Rules, Regulations, Acts and Ordinances) covered in this document are subject to changes, hence, it is recommended that the reader must refer to the actual text of the law being referred to in this document, and the actual text of any supplementary legislation (including any rules, by-laws, regulations, crossreferenced Acts or Ordinances) thereto which may not have been mentioned in the document. Tola & Tola also bears no responsibility to update this document for events and circumstances occurring on or after the date of this document.

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