

**IN THE SUPREME COURT OF PAKISTAN**  
(Appellate Jurisdiction)

**Present**

Mr. Justice Qazi Faez Isa  
Mr. Justice Yahya Afridi  
Mr. Justice Jamal Khan Mandokhail

**Civil Appeals No. 632 and 633/2019**

*(Against the order dated 23.11.2017 of the High Court of Sindh, Karachi passed in ITCs No. 228 & 229/2003)*

*The Commissioner Inland Revenue* ... *Appellant*

**Versus**

*M/s Habib Insurance Company Ltd* ... *Respondent*

For the Petitioner: Syed Mohsin Imam, ASC

For the Respondent: Mr. Anwar Kashif Mumtaz, ASC

Date of Hearing: 03.11.2022

**ORDER**

**Qazi Faez Isa, J.** These two appeals have been filed by the Commissioner Inland Revenue, Zone-III, Large Tax Payer Unit, Karachi assailing the common order whereby two income tax cases were decided, respectively pertaining to the tax years 1999-2000 and 2000-2001. The impugned order the learned Judges of a division bench of the High Court of Sindh at Karachi set aside the order passed by the Income Tax Appellate Tribunal (**the Tribunal**).

2. The question in both the cases is regarding the accounts to be maintained by the respondent, an insurance company, and in particular the amount that may be spent on the expenses of management. At the relevant time, the governing law was the Income Tax Ordinance, 1979 (**the Ordinance**). Section 26(a) of the Ordinance provided a special procedure with regard to certain types of businesses, including that of the business of insurance and provided that the *'tax payable thereon [insurance business] shall be computed in accordance with the rules contained in the*

*Fourth Schedule*'. And, the applicable rule was rule 5 of the Fourth Schedule, which is reproduced hereunder:

'5. **General insurance.**- The profits and gains of any business of insurance other than life insurance shall be taken to be the balance of the profits disclosed by the annual accounts required under the Insurance Act, 1938 (IV of 1938) to be furnished to the Controller of Insurance, subject to the following adjustments, namely:

(a) any expenditure or allowance or any reserve or provision for any expenditure, or the amount of any tax deducted at source from any dividends or interest received which is not deductible in computing the income chargeable under the head "Income from business or profession" shall be excluded;

(b) any amount either written off or taken to reserve to meet depreciation or loss on the realisation, of investments shall be allowed as a deduction, and any sums taken credit for in the accounts on account of appreciation, or gains on the realisation, of investments shall be treated as part of the profits and gains:

Provided that the Deputy Commissioner is satisfied about the reasonableness of the amount written off or taken to reserve in the accounts to meet depreciation, or loss on the realisation, of investments, as the case may be.

(c) Nothing contained in this rule shall be construed to authorise deduction of any expenditure or allowance or reserve or provision in excess of the limits laid down in the Insurance Act, 1938 (IV of 1938).'

The above mentioned clause (c) was inserted by Finance Act, 1999.

3. The learned counsel for the appellant submits that the aforesaid special mechanism was provided with regard to insurance businesses and that the said rule 5 of the said Fourth Schedule refers to the Insurance Act, 1938 ('**the Insurance Act**') which stipulates that the profits and gains of any business of insurance and the balance of the profit disclosed in the annual account shall be approved by the Controller of Insurance. However, section 40-C(1) of the Insurance Act, reproduced below, prescribes certain limits on expenses of management which, admittedly the respondent had exceeded:

'40-C. **Limitation of expenses of management in general insurance business.** (1) No insurer shall, in

respect of any class of general insurance business transacted by him in Pakistan, spend in any calendar year as expenses of management, including commission or remuneration for procuring business, an amount in excess of the prescribed limits and in prescribing any such limits regard shall be had to the size and age of the insurer.'

4. On the other hand, the learned counsel for the respondent relies upon the proviso to Section 40-C(1) of the Insurance Act which is reproduced hereunder:

'Provided that the Controller of Insurance may, on an application made to him in this behalf, condone the contravention of this sub-section by an insurer who has, on reasonable grounds, spent as such expenses an amount in excess of such limits.'

The learned counsel states that though the stipulated limit with regard to the expenses of management had been exceeded however, on an application of the respondent, the Controller of Insurance had condoned the said contravention. He further submits that the learned Judges of the High Court had correctly decided the cases by relying upon the decision in the case of *Commissioner of Income Tax v Messers ALPHA Insurance Co. Ltd.* (PLD 1981 Supreme Court 293).

5. We have heard the learned counsel, read the impugned order and that of the Tribunal, examined the cited legal provisions and considered the decision of this Court in the case of *ALPHA Insurance*.

6. A special procedure was prescribed in section 26(a) and rule 5 of the Fourth Schedule to the Ordinance with regard to insurance business. Admittedly the respondent had exceeded the prescribed limit of the *expenses of management*. Therefore, it needs examination whether the Controller of Insurance had pursuant to the proviso to section 40-C(1) condoned the excess amount said to have been spent on the expenses of management. However, before doing so it would be appropriate to reproduce section 40-C(2) of the Insurance Act:

'(2) Every insurer as aforesaid shall incorporate in the revenues account a certificate signed by the chairman, two directors and the principal officer of the insurer

and an auditor's certificate, certifying that all expenses of management wherever incurred, whether directly or indirectly, in respect of the business referred to in this section, have been fully debited in the revenue account as expenses.'

7. Though said certificate has not been produced by the respondent nonetheless we proceeded to consider whether the respondent had produced the requisite letter/certificate/order of the Controller of Insurance. The only documents which were relied upon by the respondent on the basis of which it alleged that the Controller of Insurance had condoned the additional expenses are two undated letters written by the Assistant Controller of Insurance, which are reproduced hereunder:

The first letter:

'Dear Sir,

I am directed to refer M/s Habib Insurance Company Limited letter dated 23.02.2000, on the above subject and to state that the competent authority has condoned the excess expenses of management for the year 1998 in accordance with the proviso of Section 40-C (1) of Insurance Act, 1938.

02. This issues with approval of the Controller of Insurance.'

The second letter:

'Dear Sir,

Reference M/s. Habib Insurance Company Limited's letter dated 24<sup>th</sup> August 2002 on the subject.

2. It is to inform you that the then Controller of Insurance, in exercise of the powers conferred under the proviso to Section 40-C(1) of the Insurance Act 1938 had condoned the entire management expenses exceeding the prescribed limit of the Company for the year 1998 as reflected by the audited accounts for the said year.'

8. We asked the learned Mr. Anwar Kashif Mumtaz to refer to the respondent's application(s) submitted to the Controller of Insurance calling upon him to exercise powers pursuant to the proviso to section 40-C(1) and the letter/certificate/order issued thereon by the Controller of Insurance condoning the excessive expenditure. The learned counsel states that the same have not

been filed. Since these are appeals the entire record of the case is available with this Court which we examined but the said documents are not part of the record. The Tribunal had noted that the requisite documents were not produced, nor any other document to show the '*specific amount of Excess Management Expenses condoned by the Controller*'. Once the respondent had admitted that the prescribed maximum limit of expenses had been exceeded it was incumbent upon it to show that the excess in the *expenses of management* had been condoned by the Controller of Insurance, and to what extent. However, documents in this regard which the respondent should have possessed were not produced, despite the noting of the stated discrepancy by the Tribunal. If, for whatever reason, the requisite documents were not produced before the Tribunal the same should have been produced before the High Court, but this too was also not done, nor were the same produced before this Court.

9. The above quoted letters of the Assistant Controller while referring to the excess in the expenses of management states that the same had been condoned but does not refer to the number and/or date of the letter/certificate/order of the Controller of Insurance which had condoned it. The burden to establish that the Controller of Insurance had condoned the *excess management expenses* lay upon the respondent but the respondent had failed to produce any document to establish this fact. Therefore, the High Court had incorrectly set aside the Tribunal's decision and had done so without any basis. The requisite document(s) regarding the Controller of Insurance condoning the excess in the expenses of management were also not produced before the High Court, nor even before us.

10. In the *ALPHA Insurance* case the scope of section 40-C(1) of the Insurance Act and its proviso were explained, as under:

'9. What clearly emerges from section 40-C is that there is a prohibition against exceeding the management expenses. The prohibition is not, however, absolute, irremediable, or punitive in all cases. On the contrary, it appears from the language of the proviso itself that it is a regulatory supervisory and corrective power exerciseable by the Controller of Insurance. The other feature of this provision of law is that it is a mandatory

requirement that "all expenses of management wherever incurred, whether directly or indirectly" must be "fully debited in the revenue account as expenses." Thus the annual statement of account, the balance-sheet and the profit and loss account must reflect fully and correctly, uncontrolled by any limitations prescribed under the Insurance Act all the expenses of management including there exceeding the ceiling. They have to be treated as a part of the account and the balance-sheet for all purposes and in fact form the jurisdictional basis for the Controller of Insurance for either condoning it or penalizing it. The certificate of the Chairman two directors and the principal officer of the insurer and an auditor's certificate "certifying" that all expenses of management wherever incurred, whether directly or indirectly" in respect of general insurance "have been fully debited in the revenue account as expenses" is to be incorporated in the revenue account.

10. The jurisdiction of the Income-tax Officer under rule 6 of First Schedule to the Income-tax Act is confined to the taking of the profits and gains of any business of insurance other than life insurance "to be the balance of the profits disclosed by the annual accounts, copies of which are required under the Insurance Act, 1938 to be furnished to the Controller of Insurance." This presents the Assessing Authority with a fate accompli, over which he exercises no control. If the law requires such excess to be excluded from the balance-sheet the Assessing Authority cannot reintroduce it. If the law, as in these cases requires such expenses to be included in the balance-sheet, the Assessing Authority cannot exclude it on any principle not made a part of the First Schedule to the Income-tax. This brings us back to the starting point, namely, that the Income Tax Officer has no power to do anything not contained in the First Schedule to the Income-tax Act.'

11. We are in complete agreement with the aforesaid but in the present cases there is no proof of the Controller of Insurance condoning the excess in the expenses of management. In the present cases the letter/certificate/order of the Controller of Insurance, issued pursuant to exercising powers under the said proviso, was not produced. The cited decision in the *ALPHA Insurance* case did not hold that an insurance company could expend on *expenses of management* more than the prescribed limit or that without providing the requisite proof of the Controller of Insurance condoning the excess in expenses it could be assumed the Controller had done so. In our opinion, the order of the division bench of the Tribunal to the extent as noted above accorded with the facts and the law and did not call for any interference by the

High Court. Therefore, the impugned order dated 23 November 2017 of the High Court is set aside and resultantly the orders of the Tribunal dated 13 November 2002 and 13 May 2003 are restored.

12. For the aforesaid reasons, both the appeals are allowed in the foregoing terms but with no order as to costs as we have reversed the decision of the High Court.

Judge

Judge

Judge

*Islamabad,*  
*03.11.2022*  
*Rizwan*

**'Approved for Reporting'**