B-COM-APP/2017/ 2-13162
GOVERNMENT OF SINDH
SINDH REVENUE BOARD
Karachi, dated 13th March, 2017

BEFORE THE COMMISSIONER (APPEALS) SINDH REVENUE BOARD

APPEAL NO. 195/2014

ORDER-IN-APPEAL NO. 31/2017

M/s Pakistan Beverages Limited, **Appellant**
D-113, Mangopir Road, S.I.T.E,
Karachi.

Versus

Mr. Sania Anwar, **Respondent**
Assistant Commissioner, Unit-10, Sindh Revenue Board,
9th Floor, Shaheen Complex, Karachi.

Representative(s): M/s Masood Associates, ARs for the Appellant

Ms. Anum Shaikh Assistant Commissioner, presently incharge of the Sector for Respondent.

Date filing of Appeals: **23-12-2014**
Final Date of Hearing: **08-03-2017**
Date of Order: **13-03-2017**

ORDER

Zamir A. Khalid, Commissioner (Appeals) SRB,- By this Order, I intend to dispose of the above titled/numbered Appeal filed against the Order in Original, bearing No. 706/2014 dated 28th November, 2014 (hereinafter referred as "OIO") passed by Mr. KALIMULLAH Siddiqui, Assistant Commissioner, Unit-16, Sindh Revenue Board, against the Appellant.

1. Brief facts of the case are the allegedly the Appellant is providing the franchise services, classified under tariff heading 9823.0000 of the Second

Schedule of the Sindh Sales Tax on Services Act, 2011 (hereinafter referred as the "Act, 2011"). The Respondent taken the price of concentrate amounting to Rs: 476,619,712/- purchased during the month of October, 2014 and multiplied the figures of one month with 12 in order to ascertain the value of concentrate for the period from July, 2011 to June, 2012 which equaled to Rs: 5,719,436,544/-. Instead of calculating the tax on value of consideration (10% of concentrate) as required under Rule 36 of the Sindh Sales Tax on Services Rules, 2011 the Respondent calculated the tax being the 10% of the value of concentrate, which equaled to Rs: 571,943,655/-. This amount was imposed, held to be recoverable along-with the default surcharge to be calculated at the time of payment and the penalties of Rs: 10,000/-, Rs: 120,000/-, Rs: 200,000/- Rs: 25,000/- Rs: 910,000/- and Rs: 100,000/- against Offences No. 1, 2, 3, 6(d), 13 and 15 of table section 43 of the Act, 2011. Later, the Respondent issued a Corrigendum dated 3rd December, 2014 under which the correction in the calculation was made and accordingly the amount of tax was calculated as Rs: 57,943,655/- (Rs: 5,719,436,366/- x 10% as per Rule 36(ii) of the Act, 2011). The Appellant felt aggrieved and filed this Appellant before me on factual as well as legal grounds as under:-

I. That the Appellant is bottler only and there is no consideration being paid to the foreign franchiser. That the royalty at 2% is being paid by M/s PEPSICO Lahore and not the Appellant.

II. That the then Rule 36(ii) when it fixed the rate of tax as 10% of value of concentrate is ultra vires the Act, 2011.

III. That without prejudice to the above legal grounds, the value taken by the Respondent after the reconciliation includes all the taxes paid, and per the Appellant the value had to exclude the other taxes.

IV. That without prejudice to the above grounds taken the value of the concentrate was hypothetical as the value of concentrate for the month of October, 2014 was multiplied with 12 to ascertain the value of July, 2011 to June, 2012 which is not sustainable in the eyes of law.

2. The issued above needed reconciliation. The Appellant was asked to provide the details of concentrate purchased in the tax year 2011-12. It was further required from M/s Pepsico Lahore to apprise of the facts as to whether any royalty is being paid by the Appellant or is only being paid by the M/s Pepsico Lahore. Further it was required to provide the agreements between the Appellant and the M/s Pepsico Lahore and the Agreement between M/s Pepsico Lahore and the M/s Pepsico US. The Agreement and details were provided. There was no element of payment of royalty by the Appellant was found. The M/s Pepsico Lahore provided the details of concentrate sold to the Appellant during the period in question. The Appellant provided the data and also the invoices. The same were reconciled by the Appellant in a long phase of reconciliation. The number of units of concentrate as per the invoices appeared as 66519, whereas the number of units as per data provided by M/s Pepsico Lahore appeared as 67,107. For the difference of number of 588 units, the Appellant submitted that 02 of the invoices were booked in the year 2012-13, therefore the difference of 588 units appears. The Respondent perused the invoices and found the submission as correct. The parties agreed after the reconciliation and accordingly the report was filed by the Respondent. As per the report the value of concentrate appeared as Rs: 4,116,893,811/- (67107 units), but due to the above two invoices booked in the next year the units reduced to 66,519 and accordingly the value of concentrate was reduced to Rs: 4,116,89,3055/-. The Respondent submitted that 10% of the value of concentrate is to be taken as the consideration as per the then Rule 36(ii) and 10% of rate of tax is applicable on such consideration. In view whereof the tax, based on Rule 36(ii) was calculated and it appeared as Rs: 41,168,930/- (4,116,89,3055 x 10% x 10%).

3. The matter was finally heard on 08-03-2017 and was reserved for Judgment by surfacing the above issues a to d of para 1 needing decision. The decisions on the issues in accordance with the submissions of the parties will follow hereunder. Firstly the Issue a of para 1 will be discussed and decided hereunder:-

I. In order to determine the issue a of para 1 firstly the agreements are required to be studied and understood. The study whereof shall help determining as to whether the activity in question falls into description

contained in the definition contained at section 2(46) and also the description given against the tariff heading 9823.0000.

a1. Firstly I will go through the different provisions of the Agreement dated 15th June, 2005 (hereinafter referred to as the Sindh Agreement) entered into between Appellant and the Pepsico, Inc, the State of the North Carolina, ie. the Foreign Company (hereinafter referred to as Pepsico US) considered by the Respondent as franchiser. As per clause 1 the PEPSICO US has appointed the Appellant as the exclusive "Bottler" for bottling, canning, selling and distributing the Pepsi-Cola, Mountain Dew, Diet Pepsi-Cola, Mirinda (in its Orange flavor) and Team soft drink beverages. Thereunder at clause 1 the PEPSICO US has listed the cities of province of Sindh. The appointment is for 8 years as under clause 2. Under clause 3(a) the Appellant is duty bound to purchase all units of concentrate designated by the PEPSICO US at a price and terms and condition of the PEPSICO US. Under clause 3(b) the Appellant has to obtain all the licenses, permits for shipment of any imported machinery, equipment, units, or other materials required to the bottling, canning selling and distributing of the beverages. Under the clause 3(c) the Appellant has to follow instructions of the PEPSICO US in handling and processing of beverages, concentrates, and the preparing, bottling canning selling and distribution of the beverages. Under clause (d) the Appellant is authorized to operate at thoroughly clean and sanitary bottling plants at some of the cities in Sindh. Under the clause (e) the PEPSICO US can inspect the plants. Under clause (g) the company is to sell the beverages only in the size, type and design of packages authorized by the company. Under the clause (h) the Appellant has to make efforts to increase sales and gain market share by actively promoting and soliciting the sales of beverages. Further the Appellant is authorized and is obligated to use the strategies and materials approved by the PEPSICO US to advertise and promote the product. The Appellant further has to sell the beverages to retailers at prevailing competitive market price and keep deposits of the bottles and cases under clause (i) & (j). Under clause 8(c) the Appellant has to pay

damages in the event of breach of the certain obligations of the contract, rate of which is based on the units purchased by the Appellant.

a2. The other Agreement is tripartite in nature (hereinafter referred to as the Concentrate Agreement), entered into among PEPSICO US, the Concentrate Manufacturing Company of Ireland (CMCI) and the M/s Pepsi-Cola International (Pvt) Ltd (Pepsico Lahore). Under this Agreement Pepsico Lahore is authorized to manufacture and distribute in Pakistan, all components of Pepsi Concentrate, 7UP Concentrate, Teem Concentrate, Mountain Dew Concentrate, MIRINDA Concentrate and any other Concentrates for which PCI Pak is thereafter authorized to manufacture and distribute the concentrate and is licensed to utilize the Trademarks in connection with the manufacture of the Concentrate. The Pepsico Lahore is authorized to use the trade marks accordingly for the manufacturing and distribution of the trade marks. Under the Concentrate Agreement the Pepsico Lahore is bound to sell and distribute the concentrate solely and exclusively to the authorized producers of the beverages in the territory. Remaining authorities in the Concentrate Agreements are similar to that of the Sindh Agreement. The Appellant is not a party to the Concentrate Agreement.

a3. As is apparent from the above sub-paras a1 to a2 that there are two arrangements. In the first arrangement the authorities have been delegated through the Concentrate Agreement to the Pepsico Lahore. In that arrangement the CMCI is primarily the manufacturer of the concentrate, who, under the tripartite agreement (Concentrate Agreement) has authorized Pepsico Lahore to manufacture and obviously the CMCI has also provided certain technical assistance to the Pepsico Lahore as well. Under the Concentrate Agreement a quarterly royalty of 2% of the net sales of the concentrate is to be paid by the Pepsico Lahore to PEPSICO US. For the purpose of providing expertise of manufacturing the concentrate it is the CMCI who is the owner of concentrate expertise and has delegated the authority to Pepsico Lahore in agreement with the PEPSICO US, but however, the element as to how the CMCI has to be

benefitted is absent in the Concentrate Agreement. As a matter of fact the Pepsico Lahore has to pay the royalty @ 2% of the value of concentrate in a quarter of an year. The same cost will, and thus has to include in the total cost of a unit of the concentrate being sold to the Appellant or any other authorized person dealing in this behalf. The Appellant is absent in the Concentrate Agreement.

a4. In the 2nd arrangement in case of Sindh Agreement, there comes the Appellant. Factually, since the Pepsico Lahore has to pay the 2% royalty to PEPSICO US, and that cost is included in the value of concentrate, therefore the cost incurred by the Appellant to purchase the concentrate will also include the 2% amount of royalty. However, it is learned from both the agreements, the invoices raised by Pepsico Lahore and a Supplier Payment History Report that the Appellant is not directly paying the royalty to the PEPSICO US for the technical assistance it receives in preparation/production of the beverages.

a5. A question as to whether the Appellant is only a "bottler" is also required to be determined. As far as the authority delegated through the Sindh Agreement is concerned the Appellant is bound to purchase the concentrate from the Pepsico Lahore (being seller of the concentrate), but Pepsico Lahore is not part to the Sindh Agreement. By further reading the Sindh Agreement as described above in para a1 the Agreement is not merely a bottler agreement but is for bottling, selling and distributing as well. Further it is to be seen that under clause 3 (a) of Concentrate Agreement the Appellant has not been termed as "bottler" but is termed as "authorized producer". As a matter of fact the Appellant receives the mere concentrate and not readily drinks for bottling. Making a concentrate is the first step towards preparing a drink as such. And thereafter there are certain processes/steps which enable a drink to form a drinkable state. After receiving a concentrate prepared by the Pepsico Lahore the Appellant has to do the following and thereafter becomes the element of bottling the drinks:-

1. Mixing of water and sugar and to add caffeine (if required) to the concentrate by means of centrifuge machines or as the state of caffeine demands;

2. Then to pour the acid and flavoring mixture into the water/sugar mixture;

3. To mix the part concentrate with five parts of water in a certain quantity;

4. Then comes the bottling;

5. Hereafter the drinks form the state of drinking and are sold and distribute to the retailers in Sindh;

The display of facts will show that the Concentrate Agreement terms the Appellant as "authorized producer". And further it shows that the Appellant receives a concentrate and thereafter there are certain steps and processes to bring the concentrate in a drinkable form. In view whereof, the Appellant is to be termed as a producer and not merely as a bottler. The term "bottler" used in the Sindh Agreement is only for the identification of the Appellant and reference purposes and cannot be construed as such to mean a bottler only.

a6. In order to further see as to whether the activity of the Appellant is covered within the four corners of the term "franchise services" the description in the definition contained at section 2(46) of the Act, 2011 is required to be read and understood. The definition is given hereunder:-

"(46) ***"franchise"*** *means an authority given by a franchiser, including an associate of the franchiser, under which the franchisee is contractually or otherwise granted any right to produce, manufacture, distribute sell or trade or otherwise deal in or do any other business activity in respect of goods or to provide services or to undertake any process identified with the franchiser against a consideration or fee, including technical fee, management fee, or royalty or such other fee or charges, irrespective of the fact whether*

or not a trademark, service mark, trade name, logo, brand name or any such representation or symbol, as the case may be, is involved;"

a7. As a matter of fact and record the authority has been delegated by way of Sindh Agreement, whereby the Appellant has to purchase the concentrate from the Pepsico Lahore and then after producing the brands as per the specifications provided the Appellant has to sell and distribute the drinks at market price to retailors. The PEPSICO US is obligated to provide all the technical assistance required in producing the bottling of the drinks. The Appellant has no own recognition in the course of producing, selling and distributing the drinks, but the trade-marks and the intellectual property recognitions of the PEPSICO US is on the face. In such a situation the activity is well covered under the terminology franchise as is described in the above definition. Even otherwise if the term franchise is seen in common parlance of ordinary dictionary meaning it will be seen that the arrangement as such sufficiently falls in the category of franchise. And there is no room for any other interpretation and also there is no legal and factual cavil to understand as such. Therefore, in view of the above I have formed my opinion that the arrangement squarely falls into the category of franchise services when read with the definition as well as under the ordinary meaning of franchise as such.

a8. However, what has been disturbing me was that what is and where is the consideration in the Sindh Arrangement. In this regard I have studied the both the Agreements in juxta position. From reading the same it will be seen that the Appellant is not the party to the Concentrate Agreement and equally the Pepsico Lahore is not party to the Sindh Agreement. But there are some common obligations for both in the either agreements. The Pepsico Lahore is bound to sell the concentrate to authorized producers/the Appellant and the equally the Appellant is bound to purchase the concentrate from the Pepsico Lahore. Therefore, these agreements cannot be taken as separate and distinct and for the purpose of

ascertaining the factual position the interpretation has to be based on both the agreements. As matter of fact the technical assistance is being provided by the PEPSICO US to the Appellant and sufficiently the authority has also been delegated to be used in the name of PEPSICO US. Against such use of authority and provision of technical assistance to both the Pepsico Lahore and the Appellant the consideration is definitely being received by the PEPSICO US. And that is the royalty at 2% from on value of concentrate sold by the the Pepsico Lahore. And the burden of which is already being borne by both of the Appellant as well. So therefore there exists the element of consideration in both the cases of the Appellant as well as in the case of the Pepsico Lahore. The sale of the Pepsico Lahore is nation-wide and at the total sale of the concentrate a @ 2% is required to be paid as a royalty. In such a situation the value of consideration/services was not determinable in ordinary course.

a9. The Board has the powers conferred under section 5 of the Act, 2011 to fix any other value of a service or class of services if the value is not determinable in an ordinary course of valuation. The section 5(d) is a non-abstente clause which says that *"where the Board deems necessary it may, by notification in the official Gazette, fix the value of any service or class of services and for that purpose fix different value for different classes of description of the same or similar types of services"*. Accordingly, the Board fixed the value of services under the then Rule 36(ii) (now Rule 36(4)) as 10% of the value of concentrate purchased by the beverage companies.

II. In view of the findings accorded in para 9a above the ground b of para 1 is also replied in negative. The Board has sufficient powers to fix another value of services/consideration as under section 5(d) and thus it has not gone *ultra vires* the Act, 2011 when framing and publishing the then Rule 36(ii) (presently Rule 36(4)) and proviso thereon.

III. As far ground c of para 1 is concerned, it will be seen that section 5 provides for the valuation of services. It says that the *"(1) The value of taxable services is:-- (a) the consideration in money including all Federal and*

Provincial duties and taxes, if any, which the person providing a service receives from the recipients of service but excludes the amount of sales tax." The Appellant is a recipient of services in fact and under section 24(3) read with subsection (2) of section 3 all the provisions applicable on the service provider are also applicable on the Appellant. The Board has fixed a rate of tax @10% to be applied on 10% of value of concentrate purchased by taking the same as the value of concentrate. The Board has not given any exception to duties and taxes from the valuation of services other than the tax on sale of services to which the statute has granted exception. Therefore, in my humble opinion the construction shall be on the clause a. of subsection (1) of section 5, and the value of services shall be the 10 % of the value of concentrate and nothing shall be excluded to reduce the value.

IV. As far as the ground d above, it will be seen that the Respondent could not take the value received in any of the month to calculate value of another month or periods. Rather it had to be on factual basis for which the Appellant was required to provide the documents and evidence. Accordingly, the matter was put to reconciliation, as a result of which the correct value as per Rule 36 read with section 5 was ascertained and in this regard the Appellant as well as the Pepsico Lahore provided the record and documents. The Appellant agreed with the calculations made and accepted the same, without prejudice to the basic contentions discussed and decided above. Thus, having decided the above legal issues there also remains no factual dispute as well.

4. I have also gone through the Judgment of the Judgment of the Honorable Appellant Tribunal Inland Revenue (Pakistan) Karachi Bench, Karachi, dated 09-06-2014 which is mainly relied upon by the Appellant. In this Judgment the Honorable Tribunal dismissed the departmental appeal for imposition of Federal Excise Duty on M/s Sukkhur Beverages Ltd. The Judgment of the Tribunal was based on the Judgment of Honorable Peshawar High Court delivered in the Reference Application No. 6/2013 in the case of CIR Peshawar versus Nothern Bottleing Company (Pvt) Ltd and a subsequent decision of the Honorable Supreme Court dated 26-11-2014 in Civil Petitions No. 1742 & 1743/2014. In this Judgment the Honorable Tribunal held that the agreement in the case of M/s

Sukkur Beverages Ltd was "bottler" agreement thus the Federal Excise Duty could not be imposed. I have gone through the provisions of the Federal Excise Act, 2005. Under Section 10 read with clause (b) the value of services has to be the value, retail price, tariff value and the rate of duty in force--, in case of services, on the date on which the services are provided or rendered the rate is to be applicable. But further study of the section 10(b) and other provisions of the Federal Excise Act, 2005 will show that there is no machinery provisions in the Federal Excise Act, 2005. Whereas in section 5(d) is available in the case of the Act, 2011 being the machinery provision. Section 5(d) allows the Board to fix a value of services if it could not be determined in the ordinary course of valuation. As a matter of fact there has to be an impact of royalty being paid by the Pepsico Lahore onto the cost of concentrate. The Appellant is being benefitted by way of receipt of technical assistance and the sale of produced beverages, whereas the PEPSICTO US is being benefited by the royalty being paid indirectly by the Pepsico Lahore instead of the Appellant. Further it is to be seen that Agreements or their provisions, in that case or the provisions of the Act, 2011 have not been under the perusal and study of the Honorable Supreme Court but instead it was the Federal Excise Duty imposed under the Federal Excise Act, 2005. The case of imposition of Federal Excise Duty is obviously a distinguishable case when read with the provisions of the Act, 2011 and the Agreements in question. In my humble opinion the case of the Appellant is amply covered under the Act, 2011 based on which, in the facts and circumstances of the case, the Rule 36(ii)/36(4) was made to determine value of services.

5. As far as the penalties are concerned, it will be seen that there involved a thorough interpretation of the statute, the agreements and the rules. Therefore a lenient view is inevitable.

6. In view of the above findings, the OIO is upheld in principle and it is held that the Appellant is a franchisee of the PEPSICO US and is liable to pay the Sindh sales tax on services at the applicable rate. However, the OIO is altered as in the case of value of services taken on actual basis after the reconciliation provided by the Appellant and the Pepsico Lahore. The Appellant is directed to

comply with the law and to pay the amount of tax determined above in para 1 forthwith and also to pay the default surcharge to be calculated at the time of payment. However, the Appellant shall only be required to pay the penalties imposed in the event of failure to pay the tax and default surcharge within a period of 15 days of receipt of this Order.

7. The Appeal was filed on 23-12-2014. So far 166 days (excluding time taken through adjournments) have passed. In the meantime the time of 120 statutory days was to reach in the proceedings the time was accordingly extended under section 59(5) of the Act, 2011 for 60 days on 2-05-2016. Since the reconciliation was ongoing in detail to determine the value, therefore, the extension was inevitable. Today is 166th days, therefore the Order is within the extended time.

8. This Order comprises **(12)** pages and each page bears my official seal and signature.

(Zamir A. Khalid)
Commissioner (Appeals)
Sindh Revenue Board, Karachi

(Zameer A. Khalid
Commissioner (Appeals)
SINDH REVENUE BOARD

Via Courier Services/Registered Post to:

M/s Pakistan Beverages Limited,
D-113, Mangopir Road, S.I.T.E,
Karachi.

Copy for Information and necessary action to:

1) The Chairman, Sindh Revenue Board, Karachi.
2) The Commissioner-III, Sindh Revenue Board, Karachi.
3) Deputy Commissioner (Legal Wing), Sindh Revenue Board, Karachi.
4) The Assistant Commissioner (Unit-30), SRB, Karachi.
5) Guard File.
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