

TAX FLASH NEWS

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The Bangalore ITAT decision on the applicability of TDS on year-end provisions

The Bangalore Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Biocon Ltd¹ (the taxpayer) held that the tax deducted at source (TDS) provisions are triggered for the amount credited to the 'provision for expenses account', in view of specific provisions available in all TDS sections. Accordingly, the taxpayer was liable to deduct tax at source from the year-end provision for expenses.

Further the Tribunal observed that the disallowance made under Section 40(a)(i)/(ia) will not absolve the taxpayer from the liability under Section 201/201(1A), when the taxpayer is deemed to be an assessee in default.

However, if the taxpayer is able to prove that the payees could not be identified in respect of particular expenses, then the mechanism provided under the TDS provisions would fail and hence the Assessing Officer (AO) would not be entitled to demand tax under Section 201(1) and interest under Section 201(1A) in respect of those expenses. It is the responsibility of the taxpayer to satisfy the AO by preparing a list of expenses, for which payees could not be identified at the time of making provision and the reasons for the same.

Facts of the case

The taxpayer is engaged in the business of manufacture and sale/licensing of active pharmaceutical ingredients and also trading in certain pharma formulations.

The AO noticed from the return of income filed for AY 2012-13 that the taxpayer had disallowed certain expenditure under Section 40(a)(i) and 40(a)(ia) for not deducting tax at source from those expenses.

Since there was failure on the part of the taxpayer to deduct tax at source, the AO initiated proceedings under Section 201(1) and 201(1A). The taxpayer filed a copy of tax audit report in Form 3CD and did not furnish any other details that were called for by the AO. Hence, the AO considered the taxpayer as an 'assessee in default' in terms of Section 190.

Before the Commissioner of Income-tax (Appeals) [CIT(A)], the taxpayer submitted that the provisions were made at the year-end at the time of finalisation of accounts. It was also submitted that there was uncertainty with regard to the identity of payees in some cases. Further, in most of the cases, the exact quantum of liability is not ascertainable. Accordingly, it was submitted that it was not possible to deduct tax without knowing identity of the payee. Further the taxpayer had voluntarily disallowed the expenses under Section 40(a)(i) and 40(a)(ia).

The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the order of the AO. Aggrieved, the taxpayer filed an appeal before the Tribunal.

Tribunal's decision

TDS on year-end provisions

Various TDS provisions include explanation that even if the sums are credited to any account, whether called 'Suspense Account' or by any other name, in the books of account of the payer, such crediting shall be deemed to be credit of such account to the account of the payee and the provisions of TDS shall apply accordingly.

¹ Biocon Ltd v. DCIT (ITA No.1248/Bang/2014) – Taxsutra.com

The question as to whether the above said clause available in various TDS provisions shall apply even to 'Provision for expenses' created at the year-end was examined by the Bangalore Tribunal in the case of IBM India Private Ltd². The Bangalore Tribunal observed that the statutory provisions that the liability to tax at source exists when the amount in question is credited to a 'suspense Account' or any other account by whatever name called, which will also include 'Provision' created in the books of accounts. Therefore, it is not possible for the taxpayer to argue that there was no accrual of expenditure in accordance with the mercantile system of account and therefore the TDS obligations do not get triggered. The Tribunal also referred the decision of Delhi Tribunal³.

Accordingly, it was held that the TDS provisions were triggered for the amount credited to 'Provision for expenses account', in view of specific provisions available in all TDS sections. Accordingly, the taxpayer was liable to deduct tax at source from the year-end provision for expenses.

Voluntary disallowance

The taxpayer relied on the decision of the Bangalore Tribunal in the case of Robert Bosch Engineering and Business Solutions P Ltd⁴ and contended that since the taxpayer had voluntarily disallowed the amount of year-end provision under Section 40(a)(i)/40(a)(ia), there was no requirement to raise any demand under Section 201(1)/201(1A).

The Tribunal observed that the Cochin Tribunal in the case of Agreenco Fibre Foam (P) Ltd⁵ held that the provisions of Section 40(a)(ia) provide only for deferment of the allowance and it does not provide for absolute disallowance. The objective of Section 40(a)(ia) appears to be to compel the taxpayer to deduct tax at source in order to claim the relevant expenditure as deduction.

In the case of Agreenco Fibre Foam (P) Ltd and also in the case of IBM India P Ltd, expressed the view that the disallowance under Section 40(a)(i) and 40(a)(ia) and the demand raised under Section 201 are two different consequences.

There are different types of consequences for the failure to deduct tax at source or failure to remit the tax so deducted either in full or in part, which are as follows:

- Disallowance of expenses under Section 40(a)(i)/40(a)(ia)
- The taxpayer shall be deemed to be an assessee in default and hence the demand under Section 201(1)/201(1A) could be raised upon the taxpayer.
- Penalty under Section 271C/271CA and
- Prosecution under Section 276B

It is pertinent to note that each of the consequences mentioned above are independent of each other. However, in the case of disallowance of expenses to be made under Section 40(a)(ia) and under Section 40(a)(i), the proviso inserted in those sections gives a relief, i.e., if the taxpayer is 'not deemed to be an assessee in default under Section 201', then there was no requirement of making any disallowance under Section 40(a)(i)/40(a)(ia). Thus, the proviso given under Section 40(a)(i)/40(a)(ia) itself makes it very clear that the liability under Section 201 is independent of the above disallowances.

The Tribunal observed that each of the consequences is independent of each other was also supported by the Explanation given under Section 191. As per the Explanation given under Section 191 of the Act, the provisions of Section 201 are triggered when the taxpayer is 'deemed to be an assessee in default'. Further, this Explanation makes it very clear that this liability is 'without prejudice to any other consequences'. The taxpayer can escape from the disallowance to be made under Section 40(a)(i)/40(a)(ia), if he is not treated as an 'assessee in default'.

The disallowance under Section 40(a)(i)/40(a)(ia) and penalty under Section 271C/271CA are the direct liabilities, i.e., liabilities which are directly imposed upon the taxpayer due to his failure. On the contrary, the demand raised under Section 201(1)/201(1A) is vicarious liability imposed upon the taxpayer.

Thus the contention of the taxpayer that the suo-moto disallowance was made under Section 40(a)(i)/40(a)(ia), and therefore it was not liable for proceedings under Section 201(1) and 201(1A) was not correct. The disallowance made under Section 40(a)(i)/40(a)(ia) will not absolve the taxpayer from the liability under Section 201, when the taxpayer was deemed to be an assessee in default.

Deduction of tax at the time of payment

Relying on the decision of IBM India Private Ltd, it was observed that the demand raised under Section 201(1) is liable to be cancelled, if the taxpayer had deducted tax at source at the time of accounting the invoices/bills or at the time of making payment in the succeeding year. It was further held that the taxpayer would be liable to pay interest under Section 201(1A), in view of the delay in deduction/remittance of TDS amount.

² IBM India Private Ltd v. ITO (TDS) [2015] 154 ITD 497 (Bang)

³ Interglobe Aviation Ltd v. ACIT [2020] 181 ITD 225 (Del)

⁴ Robert Bosch Engineering and Business Solutions P Ltd (ITA Nos.1689 & 1690/Bang/2017 dated 31 January 2022)

⁵ Agreenco Fire Foam (P.) Ltd v. ITO (TDS) [2015] 153 ITD 262 (Cochin)

Payees could not be identified

In various decisions, the taxpayer had established the fact that the payees were not identifiable. Hence, there should not be any dispute to the proposition that the TDS mechanism will fail, if the payees were not identifiable. Accordingly, if the taxpayer, in the present case, was able to prove that the payees could not be identified in respect of particular expenses, then the mechanism provided under Chapter XVII-B would fail and hence the AO would not be entitled to demand tax under Section 201(1) and interest under Section 201(1A) in respect of those expenses.

Year-end provisions made on estimated basis

The second practical difficulty expressed by the taxpayer was that the year-end provisions were made on estimated basis and hence there might be difference between the estimate so made and the actual payments finally made. Under these circumstances, the question that arises is how the provisions of Section 201 could be applied. The Tribunal observed that the taxpayer raised a valid point. Since the year-end provisions were made on estimated basis, following five scenarios may emerge at the time of making actual payments in the succeeding year:

Scenario	Interest
1. The actual payment made in the succeeding year is more than the provision amount.	TDS was deducted at the time of credit or at the time of making actual payment. Since year-end provision was made on 31 March 2012 in this case, the date on which TDS was deductible shall be 31 March 2012. The taxpayer shall be liable to pay interest from 31 March 2012 to the date of actual deduction/payment as per the provisions of Section 201(1A) on the amount of ' Provision ' created as on 31 March 2012.
2. The actual payment made in the succeeding year is less than the provision amount	The TDS was deducted at the time of credit or at the time of making actual payment. Since year-end provision was made on 31 March 2012 in this case, the date on which TDS was deductible shall be 31 March 2012. The taxpayer shall be liable to pay interest from 31 March 2012 to the date of actual deduction/payment as per the provisions of Section 201(1A) on the amount of ' actual payment ' made.
3. No payment is required to be made in succeeding year, since it was ascertained that there is no liability to pay the Amount. Accordingly, entire amount of provision is reversed in the succeeding year.	There will no liability to deduct tax at source from the amount of provision created as on 31 March 2012, as it was found that the said amount was not payable at all to anyone. The provisions of Section 201 will not be applicable.
4. Payment has not yet been made in the succeeding year, even though the liability to pay was acknowledged. However, the tax was deducted and paid in the succeeding year.	Interest under Section 201(1A) shall be payable as discussed in scenario 1 .
5. Payment has not yet been made in the succeeding year, even though the liability was acknowledged. However, tax was not deducted in the succeeding year.	The taxpayer would be liable to pay demand under Section 201(1) equivalent to the TDS amount deductible on the entire amount of provision. The taxpayer shall also be liable to pay interest under Section 201(1A) till the date of deduction/payment, which may cross the succeeding year.

The taxpayer had claimed to have deducted tax at source at the time of accounting of invoices/payments. Accordingly, the year-end provisions may fall under any one of the categories discussed above. Consequently, the issue was restored to the file of AO in order to enable him to recompute the liability, if any, under Section 201(1) and interest under Section 201(1A).

The Tribunal observed that the year-end provisions made by the taxpayer also included 'Commission payable to non-residents', which was liable for deduction of tax at source under Section 195. The provisions of Section 195 are triggered only if that payment is chargeable under the provisions of the Act. It was observed that the taxpayer had not furnished any detail to the AO/CIT(A) with regard to the applicability or otherwise of provisions of Section 195 to the above said payment. Hence, the issue was restored to the file of the AO for examining it afresh in accordance with law.

Our comments

The issue with respect to the applicability of TDS on the year-end provisions has been a subject matter of debate before the Courts/Tribunal.

Some of the Courts/Tribunal⁶ have held that mere passing of book entries, which have subsequently been reversed, would not give rise to an obligation to deduct tax at source. No income had accrued, arisen or deemed to have accrued or arisen, which is chargeable to tax in the hands of a payee. Similarly, there are few cases⁷ where it was held that the taxpayer had no liability to deduct tax in respect of provision made in the books of accounts since the payees were not identifiable at the time of making of the provision, thus no statutory obligation was cast upon the taxpayer to deduct tax at source. Further, the Gujarat High Court⁸ held that the year-end provisions for expenses were not to be disallowed under Section 40(a)(ia) on account of non-deduction of tax at source since such provisions were contingent in nature.

However, the Chennai Tribunal in the case of Dishnet Wireless Limited⁹ held that wherever the payee was identified, and quantum was also ascertainable on the last day of the financial year, the taxpayer has to deduct tax at source. Similarly, in various cases¹⁰ it was held that the taxpayer was liable to deduct tax on the provision for expenditure created in the books of accounts.

The Tribunal in the present case has dealt with various aspects of the applicability of TDS provisions on year-end provisions and held TDS provisions are triggered for the amount credited to the 'provision for expenses account', in view of specific provisions available in all TDS sections. Further the disallowance made under Section 40(a)(i)/(ia) will not absolve the taxpayer from the liability under Section 201/201(1A), when the taxpayer is deemed to be an assessee in default. However, if the taxpayer is able to prove that the payees could not be identified in respect of particular expenses, then the mechanism provided under the TDS provisions would fail and thus Section 201(1) and interest under Section 201(1A) would not apply.

⁶ DIT v. Ericsson Communications Ltd. [2015] 61 taxmann.com 117 (Del), Karnataka Power Transmission Corporation Limited v. DCIT [2016] 383 ITR 59 (Kar)

⁷ Alliance Media & Entertainment Ltd. v. ITO [2017] 79 taxmann.com 114 (Mum), Industrial Development Bank of India v. ITO [2007] 107 ITD 45 (Mum)

⁸ PCIT v. Sanghi Infrastructure Ltd [2018] 257 Taxman 371 (Guj)

⁹ Dishnet Wireless Ltd. v. DCIT [2016] 45 ITR(T) 430 (Chennai)

¹⁰ IBM India Private Ltd v. ITO (TDS) [2015] 154 ITD 497 (Bang), Inter Globe Aviation Ltd. v. ACIT (ITA No. 5347/Del/2012)

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