Direct Tax Vista

Your weekly Direct Tax recap

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1. TDS Deductor does not deposit the same – Recourse for the deductee?

Section 205 of the Act is very crystal clear in its intention and clarifies that where tax stands deducted at source the deductee shall not be called upon to pay the tax himself to the extent to which tax has been deducted from the income. Further incase the deduction of tax from the salary of deductee is not disputed and Government's claim of TDS stands satisfied under Insolvency and Bankruptcy Code, it cannot be said to be still outstanding so as to deny its credit to the deductee.

Even though the deductee is occupying the position of Head-Finance of the assessee in default company, there is no provision under law for creating such a liability upon any individual by attributing malice upon him for being party to the default in deposit of TDS. Head-Finance is also to be considered merely an employee who was being paid salary by the company which has a distinct and independent identity to its employees. The same was held in the case of SANJAY GUPTA Vs ITO, WARD-70(1), NEW DELHI [2022-VIL-1341-ITAT-DEL].

The CBDT has also issued Instruction dated 01-06-2015 and Instruction dated 11-03-2016 on this matter. The CBDT has clearly stated that in cases where TDS is deducted by the employer or deductor and the same has not been deposited with the Government, and the Assessing Officer cannot raise tax demands upon the payees.

The Gujarat High Court, in the case of Kartik Vijaysinh Sonavane [2021] 132 Taxmann.com 293 (Gujarat), has cancelled the demand raised upon an employee for the TDS amount not paid by his employer. Kartik was a pilot in Kingfisher Airlines.

The airline duly deducted tax from his salaried income but didn't deposit the same with the Government. The Assessing Officer issued a notice to him to pay the tax. The Gujarat High Court has ruled that TDS credit shall be given to the assessee despite the same was not paid by the airline.

The Karnataka High Court in the case of Anusuya Alva [2005] 147 Taxman 152 also held that if the tenant has deducted tax from the rent but has not paid it to the Government, the only course open to the revenue is to recover the amount from the tenant who has deducted the tax and not from the landlord.

If the taxpayer has found discrepancies in Form 26AS, he should contact the deductor for such a mismatch. There might be the following reasons for TDS credit mismatch:

(a) TDS is not deposited with Govt.
(b) TDS is deposited, but the TDS statement is not yet filed;
(c) The deductor has quoted the wrong PAN in the TDS statement; or
(d) An incorrect TDS amount has been mentioned in the TDS statement.

These mistakes can be corrected by the deductor only. Thus, the taxpayer should approach his deductor to correct the mistake at the earliest and make sure that same is corrected before filing of ITR. A taxpayer has no legal right to force the deductor to deposit TDS or make any corrections in TDS Statement. If the deductor refuses to entertain the taxpayer's request, he can submit TDS proof to Dept.

In response to the demand notice, the taxpayer can file a reply on the e-filing portal with supporting documents of TDS deducted from his income. The taxpayer can submit the salary slips and bank statement showing credit of net salary/other income after deduction of TDS. AO is bound to allow TDS credit to the taxpayer if the documents submitted are found correct. However, if he still doesn't allow the credit, the only option left is to file an appeal before CIT(A).

2. With Second landmark Decision on Charitable Trust, the litigation landscape in this sector may see fresh offshoots

In our Last Edition 29 of Direct Tax Vista, we discussed the impact of The decision of the Apex Court in the case of M/s NEW NOBLE EDUCATIONAL SOCIETY VERSUS THE CHIEF COMMISSIONER OF INCOME TAX AND ANR., [2022-VIL-23-SC-DT], wherein we discussed that the important points which come out of the judgement as follows, on the basis of which future cases u/s 2(15) may be decided –

1. It is not a bar for trusts to generate surpluses in a given year or set of years per se.
2. Incase the surplus is generated in the course of providing charitable activities, there is no case for denial of exemption.
3. However, if the surplus is generated by other than charitable activities, then the exemption of the trust may be denied.
4. This judgement would apply prospectively. However, it would also apply to already existing trusts.

This week there is another judgement on these lines. In the case of ASSISTANT COMMISSIONER OF INCOME TAX (EXEMPTIONS) Vs AHMEDABAD URBAN DEVELOPMENT AUTHORITY [2022-VIL-24-SC-DT] the question before The Court was whether local authorities can be treated as charitable institutions even though they are involved in the activity of profit where the entire revenue or income so generated was to be kept in a fund and its accounts were mandatorily audited by the State's Accountant General. Like last case, The revenue relied on the decisions in Lok Shikshana Trust, and Indian Chamber of Commerce, highlighting that the significance of the change brought about by Section 2(15) of the IT Act. It was argued that Parliament amended the definition due to rampant abuse of the law by businesses claiming to be driven by charitable purposes - contention of assessee organisations was that all three corporations i.e. Ahmedabad Urban Development Authority ("AUDA"); the Gujarat Industrial Development Corporation ("GIDC") and Gujarat Housing Board ("GHB") were established by or under statutes enacted by the Gujarat legislature treated as local authority under Section 10(20) of the IT Act, as it existed till 2003. Thereafter they were treated as charitable institutions

engaged in activities involved in the advancement of public utility till the amendment of 2008 and if surplus is generated in the activities of AUDA, GIDC, or GHB, those would not be handed to the State Government, which previously had control over them but rather kept in a separate fund to be utilised for further development, expansion and development activities by each of such corporations - These cannot be construed as carrying on any trade, business or commerce. It was held that The General test under Section 2(15) where an assessee takes the benefit of the limb “advancing general public utility”, it cannot engage itself in any trade, commerce or business, or provide service in relation thereto for any consideration (“cess, or fee, or any other consideration”). However, in the course of achieving the object of general public utility, the concerned trust, society, or other such organization, can carry on trade, commerce or business or provide services in relation thereto for consideration, provided that –

(i) the activities of trade, commerce or business are connected to the achievement of its objects of GPU; and
(ii) the receipt from such business or commercial activity or service in relation thereto, does not exceed the quantified limit, as amended over the years

Generally, the charging of any amount towards consideration for such an activity (advancing general public utility - GPU), which is on cost-basis or nominally above cost, cannot be considered to be “trade, commerce, or business” or any services in relation thereto. It is only when the charges are markedly or significantly above the cost incurred by the assessee in question, that they would fall within the mischief of “cess, or fee, or any other consideration” towards “trade, commerce or business”.

In this regard, the Court has clarified through illustrations what kind of services or goods provided on cost or nominal basis would normally be excluded from the mischief of trade, commerce, or business, in the body of the judgment. Section 11(4A) must be interpreted harmoniously with Section 2(15), with which there is no conflict. Carrying out activity in the nature of trade, commerce or business, or service in relation to such activities, should be conducted in the course of achieving the GPU object, and the income, profit or surplus or gains must, therefore, be

incidental. The requirement in Section 11(4A) of maintaining separate books of account is also in line with the necessity of demonstrating that the quantitative limit prescribed in the proviso to Section 2(15), has not been breached. Similarly, the insertion of Section 13(8), seventeenth proviso to Section 10(23C) and third proviso to Section 143(3), reaffirm this interpretation and bring uniformity across the statutory provisions. In this decision, the revenue's appeals against Ahmedabad Urban Development Authority (AUDA); the Gujarat Industrial Development Corporation (GIDC) and Gujarat Housing Board (GHB) were rejected.

Now with two elaborate judgements incase of 'objects' of Charitable trusts, both assessees as well as revenue have a lot to read, understand and implement!

3. Taxing *Angadias* - Principles for determining the income will remain the same even though the source of income is illegal in nature

The primary function of the Act is to bring the income of various kinds into the tax net. The income-tax authorities are not concerned about the manner or means of acquiring income. The income might have been earned illegally or by resorting to unlawful means. Illegality tainted with the earning has no bearing on its taxability. It is not possible for the income tax authorities to act like police to prevent the commission of unlawful acts, but it is possible for the tax. machinery to tax such income. During such process, strict rules of evidence are not applicable to the income-tax authorities. Those pieces of evidence, which are not sufficient in ordinary legal proceedings to prove a particular fact, would be sufficient for the tax officials to assess the income of an individual.

Further, If a business is illegal, neither the profits earned nor the losses incurred would be enforceable in law: but that does not take the profits out of the taxing statute. Similarly, the taint of illegality of the business cannot detract from the losses being taken into account for computation of the amounts which can subjected to tax under section 10(1). The tax collector cannot be heard to say that he will bring the gross receipts to tax, he can only tax profits of a trade or business. That cannot be done without deducting losses and the legitimate expenses of the business.

Incase of an *Angadia* (money transfer agent) There is continuous cash deposit and withdrawal on daily basis from these accounts. The A.O. cannot make an addition of total cash deposits in these bank accounts by considering only the credit side of the bank account and ignoring the debit side altogether. It is legally settled principle that the evidence should be relied upon in total and not in piece-meal manner. Hence only the commission of Angadias (money transfer agent) will be liable to tax as was held in ANIRUDH J. SOLANKI Vs THE ASSISTANT COMMISSIONER OF INCOME TAX, CENTRAL CIRCLE-1, RAJKOT [2022-VIL-1348-ITAT-RKT].

4. Income Tax and GST conundrum on Warranties

Now a days, most manufacturing and project companies provide warranties related to the repairing, maintenance and replacement of goods sold which contractually bind the company to provide free supplies/replacements of spares and hence the liability in respect of warranty for instruments sold/placed should be provided in the year in which the instruments are sold/placed. Such expenses are contingent upon the receipt of claims in future.

In Income Tax it is important that the calculation of provisions is scientific and the assessee should be able to correlate the provisions of warranty with the claims made by the customers for defective goods in proportionate manner in this particular year. It was held in the case of SIEMENS HEALTHCARE DIAGNOSTICS LTD. Vs THE A.C.I.T. [2022-VIL-638-ITAT-AHM] that merely giving overall amount will not prove the case of the assessee that it is properly arrived at the particular amount for provisions for warranty in the present assessment year without giving any details of the method used by the assessee.

The Apex Court's judgement in the case of Rotork Controls India Pvt. Ltd., Vs. Commissioner of Income- Tax, Chennai. [(2009)314 ITR 62 (SC) is the landmark judgement on warranties which holds that a provision is a liability, which can be measured only by using a substantial degree of estimation and it is recognized when:

(a) an enterprise has a present obligation as result of past event;

(b) it is probable and an outflow of resources will be required to settle the obligation; and

(c) a reliable estimate can be made of the amount of obligation.

In the case of TTK PRESTIGE LTD Vs THE DEPUTY COMMISSIONER OF INCOME-TAX, BENGALURU [2022-VIL-234-KAR-DT] again, The Court held that based on its past experience if assessee has made provision of 1% of sales value towards warranty and replacement expenses and when warranty costs are integral part of sale price, the assessee has to provide for such warranty costs in its account for relevant year and it has to be considered as an eligible deduction.

In GST too the reversal of ITC on warranty costs are sometimes contested by field formations invoking '*Section 17(5)(h) - goods lost, stolen, destroyed, written off or disposed of by way of gift or free samples*'; In this regard, CBIC FAQ on IT/ITES states as follows -

'Question 20: What would be the tax liability on replacement of parts (no consideration is charged from a customer) under a warranty and whether the supplier is required to reverse the input tax credit?
Answer: As parts are provided to the customer without a consideration under warranty, no GST is chargeable on such replacement. The value of supply made earlier includes the charges to be incurred during the warranty period. Therefore, the supplier who has undertaken the warranty replacement is not required to reverse the input tax credit on the parts/components replaced.'

It is however important to depict from the Cost Sheet / BOM that warranty was actually included in the price of actual sold goods.

5. Receipt of termination of Trust is Capital Receipt

The nature of receipt in the hands of beneficiary takes the same colour as that of the trust. Thus, in a case where what is distributed by the trust is the income earned by the trust during the year, it is income in the hands of the beneficiary. But on the other hand, if the trust is distributing its capital/corpus, then what is the beneficiary

is getting cannot be held to be his/her income – it has to take the same colour as in the hence of the trust. This Ratio was laid down In the Case of CIT versus managing trustees Nagore Durga 57 ITR 321 (SC) and CIT versus Kamalini Khatau 209 ITR 101 (SC), by the Apex Court.

Further it was also held in the case of THE ASSISTANT COMMISSIONER OF INCOME TAX Vs SRIMATI ANJANA LAXMIDAS VORA [2022-VIL-1342-ITAT-MUM], that Incase a trustee can clearly demonstrate with evidence that what that the trustee has received this year is not income of the trust, much less income earned during the relevant previous year and it is corpus remittance, it will not be taxable. Further incase the identity and creditworthiness of the trust as well as the genuineness of the transaction can be proved the provisions of Section 68 of the act could not be applied.

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