Direct Tax Vista

Your weekly Direct Tax recap

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1. Should employees suffer incase the employer defaults in payment of TDS?

On 15.07.2014, Karnataka High Court in ITA 165/2012 directed the revenue authorities to recover TDS amounting to Rs.302 crores from the Kingfisher airlines. On 18.11.2016, the Kingfisher Airlines Limited was ordered to be wound up by the Karnataka High Court. Now, the question before the Court in the case of SHRI CHINTAN BINDRA Vs DEPUTY COMMISSIONER OF INCOME TAX & ORS [2024-VIL-03-DEL-DT] was whether any recovery towards the said outstanding TDS demand can be effected against the employees, in view of the admitted position that the tax payable on salary of the employee was being regularly deducted at source by Kingfisher Airlines Ltd. who did not deposit the deducted tax with the revenue.

Section 205 read with instruction dated 01.06.2015, clearly point in the direction that the deductee/assessee cannot be called upon to pay tax, which has been deducted at source from his income. Extract of Section 205 is as under -

> *"Section 205 Bar against direct demand on assessee. Where tax is deductible at the source under the foregoing provisions of this Chapter, the assessee shall not be called upon to pay the tax himself to the extent to which tax has been deducted from that income."*

Extract of instruction dated 01.06.2015 is as under –

> *"...2. As per Section 199 of the Act credit of Tax Deducted at Source is given to the person only if it is paid to the Central Government Account. However, as per Section 205 of the Act the assessee shall not be called upon to pay the*

tax to the extent tax has been deducted from his income where the tax is deductible at source under the provisions of Chapter XVII. Thus the Act puts a bar on direct demand against the assessee in such cases and the demand on account of tax credit mismatch cannot be enforced coercively…"

Read harmoniously, it was considered that neither can the demand qua the tax withheld by the deductor/employer be recovered from employee, nor can the same amount be adjusted against the future refund, if any, payable to him. Payment of the tax deducted at source to the Central Government as mentioned in Section 199 read with Section 205, has to be understood as the payment in accordance with law.

Thus, where the employer fails to perform his duty to deposit the deducted tax with the revenue, the employee cannot be penalized. It would always be open for revenue to proceed against employer for recovery of the deducted tax

This is one of the judgements which will go down as one which provide relief to the masses and those who do not generally knock the doors of the Court.

2. Non-filing of ITR can lead to prosecution

Taxpayers are now witnessing a new era where economic offenses are no more taken with an attitude of "Letting things be". Tax Professionals should also change accordingly and ensure that tax compliances are in order. We have heard many cases under GST and Customs where prosecution proceedings have been initiated for suspected evasion of tax/duty. Now the Income Tax Authorities have also got into the Act by invoking Section 276C of The Income Tax Act. Even when an assessee failed to file its Return in time and to pay the tax due before the due date of filing the return of income, prosecution u/s 276CC and 276C(1) of the Income Tax Act was launched.

Section 278E gives a presumption to lay prosecution in case of non-filing of Return within the time limit and suppression of income in the Return filed, is with malafide intention to evade Tax. Hence, the Court held that it cannot by exercising its power

under Section 482 of Cr.P.C., quash the proceedings presuming the contrary. Let's first understand Section 276CC, before moving further –

> ***Failure to furnish returns of income.***
> ***276CC.*** *If a person wilfully fails to furnish in due time the return of fringe benefits which he is required to furnish under sub-section (1) of section 115WD or by notice given under sub-section (2) of the said section or section 115WH or the return of income which he is required to furnish under sub-section (1) of section 139 or by notice given under clause (i) of sub-section (1) of section 142] or section 148 or section 153A, he shall be punishable,-*
>
> *(i) in a case where the amount of tax, which would have been evaded if the failure had not been discovered, exceeds twenty-five hundred thousand rupees, with rigorous imprisonment for a term which shall not be less than six months but which may extend to seven years and with fine;*
>
> *(ii) in any other case, with imprisonment for a term which shall not be less than three months but which may extend to two years and with fine:*
>
> ***Provided*** *that a person shall not be proceeded against under this section for failure to furnish in due time the return of fringe benefits under sub-section (1) of section 115WD or return of income under sub-section (1) of section 139-*
>
> *(i) for any assessment year commencing prior to the 1st day of April, 1975; or*
> *(ii) for any assessment year commencing on or after the 1st day of April 1975, if-*
> *(a) the return is furnished by him before the expiry of the assessment year or a return is furnished by him under sub-section (8A) of section 139 within the time provided in that sub-section; or*
> *(b) the tax payable by such person, not being a company, on the total income determined on regular assessment, as reduced by the advance tax or self-*

assessment tax, if any, paid before the expiry of the assessment year, and any tax deducted or collected at source, does not exceed ten thousand rupees.]

Generally, taxpayers who have been charged under Section 276CC may defend themselves by proving that they had a reasonable cause for the failure to disclose income or furnish accurate particulars of income, or that the failure was due to a bona fide mistake or inadvertent error. Further, the authority has to prove that it is a “willful” non-compliance. In addition, if the taxpayer voluntarily and completely discloses the income before any notice is issued under Section 142(1)/ 153A of the Income Tax Act, they may be able to avoid penalty and prosecution. Atleast after the notice is received, the subsequent return filing will relax the rigours of the law to some extent.

However, incase there is a failure to file the return of income even after receipt of notice under Section 153A of the Act within period of 30 days from date of receipt of notice under Section 153A of the Act, then the department cannot be faulted in launching prosecution as was held in the case of P. ARULMUDI Vs THE ASSISTANT COMMISSIONER OF INCOME TAX, CHENNAI [2024-VIL-07-MAD-DT].

3. Capital subsidies also taxable...Balance Sheets maybe recalibrated

Whenever, there is a challenge to constitutional validity of a tax statute, the approach of the Court is two-fold –

i. To inspect the existence of enacting power
ii. To ascertain whether the enacted provision impinges upon any fundamental right.

Hence, in this backdrop the Hon’ble Bombay High Court tested The Constitutional validity of taxing ‘capital subsidies’, which were earlier exempt in the case of SERUM INSTITUTE OF INDIA PRIVATE LIMITED Vs UNION OF INDIA [2024-VIL-08-BOM-DT]. To lay down the context, The ‘real income theory’ in Income Tax means that only revenue receipts will be taxable. However, Section 2(24)(xviii) Inserted

vide THE FINANCE ACT, 2015 w.e.f. 1st April, 2016 is a tax on “revenue receipt as well as capital receipt” and reads as follows -

> *2(24) (xviii) assistance in the form of a subsidy or grant or cash incentive or duty drawback or waiver or concession or reimbursement (by whatever name called) by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee 93[other than,-*
> *(a) the subsidy or grant or reimbursement which is taken into account for determination of the actual cost of the asset in accordance with the provisions of Explanation 10 to clause (1) of section 43; or*
> *(b) the subsidy or grant by the Central Government for the purpose of the corpus of a trust or institution established by the Central Government or a State Government, as the case may be;];*

The amendment does not create any distinction between taxability of a capital subsidy or revenue subsidy. Post this amendment the refund of sales tax, i.e., SGST, be liable to tax as income; even the electricity duty exemption and the 50% exemption from payment of stamp duty are also to be treated as income. When the Central Government taxes these incentives and benefits as income of recipient, it is an indirect mechanism to tax the revenue of the State.

In the present case, the legislative power of the Parliament to enact sub-clause in the light of Article 245 of the Constitution was not doubted at all. Further, Imposition of tax on subsidies under amended provision was not considered to constitute “taking away” of a benefit, but rather construed as representing a recalibration of fiscal advantages in line with broader economic and policy considerations.

Trade & Industry thus need to also recalibrate their balance sheets accordingly.

4. Write back u/s 41(1) is to be taxed incase nexus of original amount with Capital expenditure cannot be demonstrated

Simple Income Tax provisions need simple back up workings and supporting documentary evidences. If those are not available, then there is no point in going

to Courts. To Section 41(1) of The Income Tax Act, it is a sine qua non that there should be an allowance or deduction claimed by the taxpayer in the earlier AY w.r.t. the expenditure, loss or trading liability. The objective is that the taxpayer should not get double deduction – once by claiming an expenditure and then by not being taxed on the write back benefit. However, to treat a write back u/s 41(1) of The Income Tax Act, as a 'capital write back', the taxpayer has to demonstrate that amount of written back represents capital receipt by establishing the nexus between relevant funds borrowed from specific creditors which as claimed by it were used to create assets which were accounted as Fixed assets in Balance sheet. In absence of the same, the same has to be brought to tax as was held in the case of M/s MERCANTILE VENTURES LTD Vs THE DY. COMMISSIONER OF INCOME TAX, CHENNAI [2024-VIL-40-ITAT-CHE].

5. For the purpose of section 153A/143(3) of the Act, the assessment can be said to be "made" only when the DIN is quoted

The well-established dicta for The Income Tax Dept. is that circulars issued by the CBDT are binding on them. Although, they cannot dictate the manner in which assessment has to be carried out in a particular case, yet a Circular cannot be side-stepped causing prejudice to the assessee by bringing to naught the object for which it is issued. Circular no. 19/2019 mandates that if the 'communication' is issued under three exceptions, the 'communication' shall state the fact that the 'communication' is issued manually without a DIN and the date of obtaining of the written approval of the Chief Commissioner / Director General of Income-Tax for issue of manual communication.

The generation of DIN is condition precedent for making an assessment manually or otherwise on the ITBA and then before it is uploaded on ITBA, first it should have DIN bearing on its face and then only it should be signed. Thus, for the purpose of section 153A/143(3) of the Act, the assessment can be said to be 'made' only when the DIN is quoted on the order before it is signed. If without first generating the DIN and before it is quoted on the order, the order is signed, the order is non-est.

It was held in the case of HARJEET SINGH Vs ACIT, CENTRAL CIRCLE 31, NEW DELHI [2024-VIL-30-ITAT-DEL], that even the generation of DIN subsequently and generation of intimation to be sent to assessee are of no consequence for the purpose of assessment and raising the demand.

6. Interest expense incurred on loans taken out to invest in a company in the same line of business as the taxpayer, would be an allowable expense

Interest expense incurred on loans taken out to acquire a controlling interest in a company in the same line of business as the taxpayer would be an allowable expense under section 36(1)(iii) as was held again in the case of TECH MAHINDRA LIMITED Vs DY. CIT, RANGE 2(2) MUMBAI [2024-VIL-27-ITAT-MUM]. It has to be demonstrated that the funds are borrowed to expand the business activities geographically, by up-streaming, by down-streaming or by any other way. The expansion of activities in a foreign territory required the acquisition of a company via a purchase of shares in that company.

7. Bombay High Court dissects taxability on 'accrual' concept, when a dispute is under judicial purview

Mesne profits, which are yet to be determined, do not come within the purview of an accrued income for the purposes of Section 4 and 5 of the Income Tax Act till the judgment in regard to civil dispute was rendered in this regard.

Consider that rent of a property is Rs.20,000 per month but the landlord files a suit demanding Rs.50,000/- per month alongwith damages. This Rs.50,000/- becomes a demand for "mesne profits". Section 2 (12) of CPC, 1908 defines and states that, "mesne profits" of property means those profits which the person in wrongful possession of such property actually received or might with ordinary diligence have received therefrom, together with interest on such profits, but shall not include profits due to improvements made by the person in wrongful possession.

The Supreme Court, in the case of P. Mariappa Gounder vs. CIT [(1998) 3 SCC 552] held that it is only when the trial court determined the amount of mesne profit, the

right to receive the same is accrued in the landlord's favour and the liability became ascertained only on the date of the trial court determining mesne profit.

For determining the point of time of accrual, two factors are relevant. The first is a qualitative factor and second is a quantitative factor. The qualitative factor is relatable to the terms of the agreement or conduct of the parties for determining when the legal right to receive income emerges. The quantitative factor is relatable to the exact sum in respect of which the qualitative factor of legal right to receive is applied. When both converge, there is a legal right to receive a certain sum of money as income. In order that income may be said to have accrued at a particular point of time, it must have ripened into a debt at that time, that is to say, the Assessee, should have acquired a right to receive payment at that moment, though the receipt itself may take place later.

Thus it was again held in the case of T.V. PATEL PVT LTD Vs THE DY. COMMISSIONER OF INCOME TAX SPECIAL RANGE-14, MUMBAI [2024-VIL-05-BOM-DT] that if the matter is pending before the judicial forum, till the case is decided finally by the judicial forum, it cannot be said that the Assessee has acquired a right to receive the income for the purposes of Section 5 of the Income Tax Act, 1961.

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