



## Global Business Tax Alert Sharp Insights

Interest applicable for non-deduction of tax at source from year-end provision for expenses, despite provision being disallowed.

**Issue no: GBTA/16/2015**

**In this issue:**

Synopsis

Facts

Issue before the Tribunal

Ruling of the Bangalore

Tribunal

Comments

Upcoming Dbriefs - Register

Contacts

# Synopsis

The Bangalore Tribunal in IBM India Private Limited, has held that interest under section 201(1A) is leviable in a case where the taxpayer had not deducted tax on the year-end provision for expenses, even if such expenses were disallowed under section 40(a)(i) / 40(a)(ia) of the Act, by the taxpayer in its return of income.

## Facts

- The taxpayer company, IBM India Private Ltd., is a wholly owned subsidiary of a U.S. based company.
- The taxpayer made provision for commission expenses, professional charges, contractor charges, foreign payments etc. following mercantile system of accounting.
- In respect of expenses for which invoices have been submitted or payments had become due, the same were accounted and tax was deducted at source thereon. However, in respect of expenses, for which only service / work had been provided / performed by the vendors, but for which invoices had not been furnished or in respect of which payments had not fallen due for payment to vendors, provision for expenses were made in the books of accounts, by recognizing liability incurred.
- Expenses were debited to profit and loss account and credited to provision account and not to the vendor account. The said expenses consisted of year-end accruals which were based on a reasonable estimate. In the return of income for respective years, the taxpayer had added back the aforesaid provision for expenses under section 40(a)(ia) / 40(a)(i) of the Act.
- In the subsequent financial years, these expenses were reversed and on receipt of invoices, the expenses were booked after deducting and depositing appropriate tax at source.
- In view of the clear admission on the part of the taxpayer that it was obliged to deduct tax at source on the various amounts, by making disallowance under sections 40(a)(i) & 40(a)(ia) of the Act of the amounts in the return of income filed, The Assessing officer (AO) initiated proceedings under section 201(1) of the Act.

- The AO also levied interest under section 201(1A) of the Act on taxes not paid.
- The Commissioner of Income-tax (Appeals) upheld the order of the Assessing officer.

## Issue before the Tribunal

Whether the assessee should be treated as 'assessee in default' under section 201(1) and provisions of section 201(1A) are attracted for not deducting tax at source on the year-end provision for expenses disallowed under section 40(a)(i) / 40(a)(ia) of the Act, by the assessee in its return of income

## Ruling of the Bangalore Tribunal

- The Tribunal held that though the provision for expenses were reversed in subsequent years and tax were deducted and deposited in those years, there was a failure to deduct tax at source in the year when the provision for expenses were made.
- The Tribunal held that since the taxpayer has deducted tax at source on these amounts in the subsequent year as and when the amount were paid by it, no demand shall be raised under section 201(1) of the Act. In view thereof, the Tribunal held that the taxpayer shall not constitute 'assessee in default' as per section 201(1).
- The Tribunal held that even though there is disallowance under section 40(a)(ia) / 40(a)(i), it is not possible to argue that provisions of section 201 were not attracted.
- The Tribunal observed that credit to suspense account is deemed to be credit to the payee / vendor's account and hence TDS provisions should be complied with.
- The Tribunal observed that the assessee did not account for expenditure on accrual basis but on receipt of invoice, which was not in tune with mercantile system of accounting. Further the Tribunal did not agree with the taxpayer's argument that there is no accrual of expenditure as per mercantile system of accounting since the payee is not identified.
- The Tribunal observed that statutory provisions envisage that collection of tax is separate from the charge under section 4(1) of the Act.

- The Tribunal disagreed with the taxpayer's submissions that TDS provision operate on income, by holding that provisions of section, 194C, 194J, 195, do not use the expression 'income'.
- The Tribunal observed that it was not a case of the taxpayer, that the payments were not chargeable to tax. The Tribunal observed that the very fact that the taxpayer deducts tax on such amounts, in subsequent years, substantiates that payment in instant case, were chargeable to tax.
- The Tribunal held that as a person responsible for making payment, it is the duty of the taxpayer to deduct tax at source.
- The Tribunal held that the CBDT circular no.3/2010 dated 2 March 2010 relied by the taxpayer to contend that no tax was deductible in the instant case, is a specific circular applicable to Banks and issued under a specific circumstance.
- The Tribunal distinguished the decisions<sup>1</sup> relied by the taxpayer and held that since the assessee did not deduct tax at source on the provision for expenses, the interest under section 201(1A) should be levied.

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<sup>1</sup> DCIT Vs. M/S.Telco Construction Equipment Co.Ltd., ITA No.478/Bang/2012 for AY 07-08 dated 7.3.2014.  
ITAT Pune Bench in the case of DCIT Vs.Yeota Merchants Co-op.Bank Ltd., ITA No.805/PN/2011 for AY 07-08 dated 31.8.2012  
ITAT Bangalore in the case of Bovis Lend Lease (I) Pvt.Ltd. Vs. ITO ITA Nos. 636/Bang/2008 for AY 2003-04 to 2005-06, dated 28.8.2009

# Comments

- The Bangalore Tribunal has not considered the Mumbai Tribunal decision in the case of Pfizer Ltd. v. ITO (2013) 55 SOT 277 (Mum.) (Trib.), wherein it has been held that there is no obligation to deduct TDS in case of general credit entry and even if TDS is applicable, since the taxpayer had disallowed such amount under section 40(a)(i) / 40(a)(ia) of the Act, the Assessing officer cannot consider the same amounts as covered by section 194C to 194J so as to raise a TDS demand again under section 201 and levy interest under section 201(1A).
- The Bangalore Tribunal decision does not deal with the taxpayer's difficulty of complying with TDS provisions in cases where the amounts are not due for payment and provision for expenses is created based on accrual system of accounting.
- Year-end provision for expenses and withholding of tax at source should now be evaluated based on the Income Computation and Disclosure Standards X.

**Source:** Bangalore Tribunal decision dated 14 May 2015, in the case of IBM Private Ltd. Vs. ITO (ITA No. 749 to 752/Bang/2012 and 1588 to 1591/Bang/2012) for the assessment years 2006-07 to 2009-10.

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