Direct Tax Vista

Your weekly Direct Tax recap

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1. Supreme Court Checkmates Businesses who will not be allowed deduction w.r.t. employees contribution even incase there is a single day of delay

The Hon'ble Apex Court checkmated the business houses which deduct provident fund and ESIC contribution from the salary of employees and then deposit to the authorities. It held in the case of CHECKMATE SERVICES P. LTD Vs COMMISSIONER OF INCOME TAX-1 that any amount which the employers deduct and delay in payment to the Government would not be allowable as a deduction to the employers. The court held that deduction of provident fund and ESIC contribution from the salary of the employees are amounts which are held in trust by the employer. Income Tax has to be paid by the employers incase of any delay in payment of the said amounts to the Authorities for the benefit of employees.

This judgement comes just as we await the Implementation of The Labour Codes and it would mean that the employers have to be very careful in the Labour Law related compliances. It is a landmark judgement for the welfare of the employees and would be seen as a measure to curb the malpractice of some employers to use the employees' funds for the benefit of the business. Employees rights would stand further protected with the implementation of this judgement.

Before the amendment of Finance Act 2021 came, there has already been huge number of intimations u/s 143(1) of 1961 Act (summary proceedings) where adjustments were made on issue of employee contribution towards ESI/PF etc leading to mass appeals at first appeal (which were mainly dismissed on basis that Finance 2021 amendment is retrospective in nature) and further second appeals at ITAT (where large number of cases are hitherto decided by the ITATs across the country taking a view beneficial to assessee). Finance Act 2021 made amendments

in sec 36(l)(va) vide expl 2 and sec 43B (explanation 5). In this context the seminal issue of retrospective vs prospective nature of the stated amendment by Finance Act 2021 came up for extensive consideration before Hon'ble Delhi high court in case of PCIT vs TV Today Network Ltd (ITA 227/2022) order dated 27.07.2022 where high court took the view that stated amendment are prospective in nature.

Though in Hon'ble SC latest order there is no discussion on retrospective vs prospective scope of amendment by Finance Act 2021, but Hon'ble SC in the present order has considered entire conspectus of the matter (related to of sec 2(24)(x); sec 36(1)(va) (employee contribution) versus (employer contribution) vide sec 36(1) (iv) / sec 43B (b) / second proviso etc) with specific reference to explanatory CBDT circulars Circular No. 372 dated 08-12-1983. & Circular No. 495 dated 22.09.1987 etc). Applying the rule of strict interpretation that taxing statutes are to be construed strictly, and that there is no room for equitable considerations and difference in character of EMPLOYER & EMPLOYEE contribution - the employer's liability is to be paid out of its income whereas the second is deemed an income, by definition, since it is the deduction from the employees' income and held in trust by the employer.

The question is whether all the doors of the assesses are closed in the similar matters. Well, one might consider that where matter is already pending before first appeal (at CIT-A or /second appeal at ITAT and original disallowance was made in intimation u/s 143(1) of 1961 Act, one may still argue on jurisdictional ground of validity of the adjustment made in summary proceedings u/s 143(1) of 1961 Act are given restricted and limited scope of proceedings u/s 143(1).

2. Denial of exemption to trusts for participation in fairs 'outside India' – Is it application of income outside India

The subject matter is a ground of litigation in many cases. The same was also dealt with somewhat in the case of SPORTS GOOD EXPORT PROMOTION COUNCIL [2022-VIL-1274-ITAT-DEL]. We present our legal submission in this case as follows -

Section 11 of the Income Tax Act, 1961 is about Income from property held for charitable or religious purposes. The relevant extract of Sec. 11 is represented below:

(1) Subject to the provisions of sections 60 to 63, the following income shall not be included in the total income of the previous year of the person in receipt of the income-

(a) income derived from property held under trust wholly for charitable or religious purposes, to the extent to which such income is applied to such purposes in India; and, where any such income is accumulated or set apart for application to such purposes in India, to the extent to which the income so accumulated or set apart is not in excess of fifteen per cent of the income from such property;

(b) income derived from property held under trust in part only for such purposes, the trust having been created before the commencement of this Act, to the extent to which such income is applied to such purposes in India; and, where any such income is finally set apart for application to such purposes in India, to the extent to which the income so set apart is not in excess of fifteen percent of the income from such property;

(c) income derived from property held under trust-

(i) created on or after the 1st day of April, 1952, for a charitable purpose which tends to promote international welfare in which India is interested, to the extent to which such income is applied to such purposes outside India, and

(ii) for charitable or religious purposes, created before the 1st day of April, 1952, to the extent to which such income is applied to such purposes outside India:

Provided that the Board, by general or special order, has directed in either case that it shall not be included in the total income of the person in receipt of such income;

There is no such mandate in Section 11 to the effect that the income of the trust should be applied (spent) in India and that the only requirement is that the purposes should exist in India and if that is satisfied, the income can be applied (spent) for such purposes even outside India. It so long as the purposes are in India, it does not matter as to where the situs of the application (spending) is. For Example, where a charitable hospital purchases equipment from abroad for the purpose of use in the hospital, it cannot be said that the amount spent for purchase of machinery from abroad would not qualify for exemption under section 11(1). Hence, the expenditure incurred for purposes in India and, therefore, the benefit under section 11(1)(a) of the said expenditure can be claimed.

Incase the assessee will apply (spend) the income for charitable purposes in India, the mere fact that the expenditure will be incurred out of India, does not disqualify the Income from exemption under section 11(1) and does not disqualify the corresponding expenditure for the purpose of application of Income. The requirement under section 11 of the Act is for application of income for 'purposes' in India and it does not restrict the application of income for the purpose of persons within the territory of India. The application of income need not be in India, but the application should result and should be for charitable / religious/ objects of general public utility in India. Merely because the payments are made outside India, it cannot be said that the charitable activities were also conducted outside the country.

3. Proper Inquiry should be one by TPO to indicate that 'receivables' reflect in a benefit to the AE

It is seen that every time a receivable appears w.r.t. dealings with foreign AEs, TPOs automatically characterize it as an international transaction intended to benefit the associated enterprise. However, it should be considered that there may be a delay in collection of monies for supplies made, even beyond the agreed limit, due to a variety of factors and the same will have to be investigated on a case-to-case basis.

Hence, the assesses may argue on grounds like the impact the receivable would have on the working capital of the assessee. Analysing the statistics over a period of time to discern a pattern which would indicate that the receivables for the supplies made to an associated enterprise does not reflect an international transaction intended to benefit the associated enterprise. Focussing on varied assessment years and the figure of receivables in relation to those assessment years reflecting a pattern. Further Incase an assessee is a debt free company, it can be agrued that it is not justifiable to presume that, borrowed funds have been utilized to pass on the facility to its AE's. Further, incase it can be depicted that the assessee has already factored the impact of the receivables on the working capital and thereby on its pricing/profitability vis-a-vis that of its comparables, any further adjustment only on the basis of the outstanding receivables could be argued to distort the picture and be impermissible.

4. U/s 194R Discount is a 'Benefit' and u/s 194H discount is a 'commission'

Clarifications by the CBDT for Section 194R suggests that while discount is also a 'benefit' yet to remove hardship, TDS u/s 194R will not be applicable. However, the question is that whether the discount provided by the sellers to distributors on the MRP, to reach at the distributor's price will be termed as a 'commission'.

In this regard it has been held again in the case of UNITECH WIRELESS (TAMILNADU) PRIVATE LIMITED Vs DEPUTY COMMISSIONER OF INCOME TAX [2022-VIL-1292-ITAT-DEL] that one has to see whether as per the terms of the agreement whether the distributor has to comply with the conditions of an agent like in respect of invoicing and accounts, maintenance of brand image of the seller, providing monthly sale reports and other information relating to business; whether Minimum performance targets are set for distributors; whether the Ultimate agreement for sale of the product is entered into between consumers and the seller. If this be the case then a principal and agent legal relationship is created and the discount between the MRP and the distributors price can be termed as a 'commission' and liable to TDS u/s 194H.

The analogy may be used in taking decisions in similar cases.

5. Equalization Levy intention is to target audience in India

The intention of Equalization levy is related to the targeted audience and incase the party paying the online advertisement charges has no relation in India, EL is not attracted. Where the assessee is only acting as a conduit for channelizing the funds from the person wanting to advertise to the platform on which such advertisement is to be done i.e. Google, and the person running the advertisement, person displaying the advertisement and the person using that advertisement are all outside India, it cannot be argued that these specified services are provided to a resident in India

In the case of PRAKASH CHANDRA MISHRA [2022-VIL-1271-ITAT-JAI] it was held accordingly by the ITAT Jaipur that Equalization Levy will not be attracted if the person making the payment to non-resident for specified services out of the amount received by him from a non-resident with the target customers of the advertisement campaign located outside India.

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