

IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCH 'A', BANGALORE

BEFORE SHRI. N. V. VASUDEVAN, JUDICIAL MEMBER

AND

SHRI. ABRAHAM P. GEORGE, ACCOUNTANT MEMBER

I.T.A No.426/Bang/2014
(Assessment Year : 2005-06)

M/s. Ravi Spice Processors P. Ltd,
P. B. No.6919, No.74/1m 3rd Main Road,
New Tharagupet, Bangalore 560 002
PAN : AAACR8178B

..Appellant

v.

Asst. Commissioner of Income-tax,
Circle 12(4), Bangalore

..Respondent

Assessee by : Shri. V. Srinivasan, CA
Revenue by : Shri. T. N. Prakash, JCIT

Heard on : 29.09.2015
Pronounced on : .10.2015

ORDER

PER ABRAHAM P. GEORGE, ACCOUNTANT MEMBER :

In this appeal filed by the assessee it has altogether taken five grounds of which grounds 1 and 5 are general, ground 4 consequential in nature, needing no specific adjudication.

02. Effective grounds are grounds 2 and 3, which are reproduced hereunder :

“2. The learned CIT (A) is not justified in upholding the disallowance of a sum of Rs.10,23,138/- being freight on purchase u/s.40(a)(ia) without appreciating that the provisions of section 40(a)(ia) of the Act have no application at all under the facts and in the circumstances of the appellant’s case.

3. The learned CIT (A) is not justified in upholding the disallowance of Rs.36,16,957/- being freight forwarding expenses u/s.40(a)(ia) without appreciating that the provisions of section 40(a)(ia) of the Act have no application at all under the facts and in the circumstances of the appellant’s case.”

03. Facts apropos are that assessee, an exporter of spices and food items had filed its return of income for the impugned assessment year declaring income of Rs.1,25,16,914/-. During the course of assessment proceedings it was noted by the AO that assessee had effected payments for freight on purchases without effecting deduction of tax at source. As per the AO CBDT circular No.715 dt.08.08.1995, clearly mandated deduction of tax at source on payments to transporters, clearing and forwarding agents for carriage of goods. AO also noted that the circular stipulated such deductions to be made on gross amounts including reimbursements. Assessee had during the relevant previous year paid a sum of Rs.10,23,138/- as freight on purchases. Assessee had also paid a sum of Rs.36,16,957/- to clearing and forwarding agents during the course of its export business. When assessee was put on notice that it had not deducted tax at source as required under law, it replied that the lorries used for transportation of goods were engaged by the suppliers who supplied the commodities. As per the assessee, agencies like M/s. Kanakadurga Lorry Supply Office, engaged several private vehicles and payments to individual lorry drivers did not fall within the purview of Section 194C of the Act. As per the assessee, it was

under no obligation to deduct tax at source on the payments effected to the lorry drivers.

04. Vis-a-vis disallowance of freight forwarding expenses, argument of the assessee was that major part of the payments made to clearing agents were reimbursements. Assessee also took a plea that Hariharan Logistics which was a forwarding and clearing agent had already declared the whole of the amounts received from the assessee in its return as a part of its income. Thus as per assessee, Section 40(a)(ia) could not be applied either on freight paid for purchases nor on freight and forwarding charges paid to the clearing and forwarding agents. However, AO was not impressed by the above arguments. According to him, circular No.715 (supra) applied for both the above payments. He disallowed freight on purchases of Rs.10,23,138/- paid by the assessee and freight forwarding expenses of Rs.36,16,957/-, paid to the clearing and forwarding agents relying on section 40(a)(ia) of the Act.

05. Aggrieved assessee moved in appeal before the CIT (A). Argument of the assessee was that it was purchasing goods from various persons outside Bangalore. As per the assessee the sellers who were also the consigners of the goods consigned the goods through several lorry owners from their respective places and such lorry owners were engaged through transport agency offices. Though the lorry transport receipts were issued by the concerned transport agencies, they were acting as brokers only. Assessee also produced a copy of lorry receipt issued by M/s. Kanakadurga Lorry Supply Office as a typical and

illustrative example. As per the assessee, their contract was with consigners of the goods and it was for the consigners to find the transporters and send the goods to the assessee. Goods were to be delivered at Bangalore. As per the assessee it had never made any payment to the lorry transport office. Payments were effected to the vehicle drivers who were delivering the goods to the assessee. There was no entry made in the books regarding payments made by the assessee on the date of purchase with regard to freight. In other words as per the assessee, freight paid by the assessee was towards the cost of purchase. Thus according to assessee, Section 194C of the Act was not applicable.

06. In so far as the payments effected to Hariharin Logistics was concerned, argument of the assessee was that they had to incur expenditure like documentation charges, Customs charges, transportation charges, fumigation charges taxi charges etc., These were reimbursed to the forwarding agents. Actual charges levied by such forwarding agents was specifically mentioned in the bills raised. One copy of the bill of Hariharan Logistics was also placed before the CIT (A). As per the assessee, payments for services rendered by such forwarding agents never exceeded a sum of Rs.twenty thousand at a given instance.

07. However, C IT (A) was not appreciative of the above contentions. According to him, supplier of goods was only a facilitator for transportation arrangement. Transport agency had issued received the lorry receipts and the concerned supplier had issued debit notes for the above paid as advance on

behalf of the assessee to the concerned transport agency. As per the CIT (A) just because the payments were effected to the truck driver at the end of unloading there would be no change in the complexion of the transaction. CIT (A) was of the opinion that assessee was making contradictory submissions. In one place it was telling that the freight charges paid formed a part of the cost of goods. However in a later submission assessee stated that the supplier was identifying the transport agency and was delivering the goods to them. As per the CIT (A), no evidence was adduced by the assessee to show that the supplier of the goods had agreed to arrange for the transportation of the goods and to deliver the goods at the assessee's premises. Thus according to him assessee was bound to deduct tax on the amount of freight expenditure.

08. In so far as non-deduction of tax at source on freight and forwarding expenditure was concerned, CIT (A) noted that what was claimed by the assessee as reimbursements were not actually reimbursements. Forwarding agent was only a single point for providing multiple service to the assessee and it was under a contractual obligation to do so. As per the CIT (A) assessee should have deducted tax on the payments made to Forwarding agents. He thus applied section 40(a)(ia) of the Act to both the payments, namely freight expenditure and freight and forwarding charges paid to carrying and forwarding agents.

09. Now before us, Ld. AR strongly assailing the order of lower authorities submitted that the bill raised by Kanakadurga Lorry Office clearly indicated the

consigner as Shree Gajanan Industries who was the supplier of goods. As per the Ld. AR, assessee had not entered into any contract with Kanakadurga Lorry Office at any point of time. Relying on a bill no.1049, dt.17.04.2004 of Kanakadurga Lorry Office, Ld. AR submitted that lorry owners name was mentioned as S. K. Khajanayab Rasul P, and lorry driver's name was B. Purnachandra Rao. As per the Ld. AR, lorry by which the goods were to be transported was decided by the seller and the assessee had no role in this. Placing reliance on a letter dt.17.04.2004 of Shree Gajanan Industries, Ld. AR submitted that goods were despatched by them with a direction to the assessee to pay the balance of the lorry rent. Thus according to him the contract was between the transporter and the consigner and not between the assessee and the lorry owner. Assessee had no choice. In any case, as per the Ld. AR, payment to each of the driver engaged by the consigner was less than Rs.20,000/- and therefore Section 194C of the Act was not at all attracted.

10. In so far as the second issue of non-deduction of tax at source on payments effected to freight and forwarding agent was concerned, Ld. AR submitted that the concerned clearing and forwarding agents, namely Hariharan Logistics had accounted the whole of the money received by them from the assessee as a part of its income and paid taxes due thereon. Relying on the decision of coordinate bench in the case of DCIT v. Ananda Marakala [ITA No.1584/Bang/2012, dt.13.09.2013], Ld. AR submitted that once the recipient

had accounted the income, liability for non-deduction of tax at source on the payer could not be fastened.

11. Per contra, Ld. DR strongly supported the orders of lower authorities.

12. We have perused the orders and heard the rival contentions. In so far as the first issue, via., payment for freight charges on goods received by the assessee is concerned, no doubt the receipt of Kanakadurga Lorry Office stated the consigner as Gajanana Industries who was the supplier. Lorry owner's name and lorry driver's name are also mentioned therein. It is clear from the bill dt.17.04.2004 available on record that Kanakadurga Lorry Office was not the owner of the lorry. For application of Section 194C of the Act, it is essential that there is a contract between the assessee and the person who is transporting the goods. Question before us is whether Shree Gajanan Industries who was the supplier to goods the assessee had engaged the lorry owner through Kanakadurga Lorry Office at the behest of the assessee or on its own. If it was on the direction of the assessee that the lorry was engaged by the supplier, then we can construe the contract as one between the assessee and the lorry office. It might be true that the assessee paid to the lorry owner the balance of the amount due for the transportation. However, existence of agreement for transportation, whether oral or written, if any, between the assessee and Shree Gajanan Industries, as to how the supplies were to be made, viz., whether it was the responsibility of the seller to find the transporter and transport it to the assessee's premises, or it was under direction of the latter the former was doing

so, was never verified by the lower authorities. We are of the opinion that this issue requires a fresh look by the AO for verifying all aspects of the payment of freight charges.

13. In so far as the payments effected to Hariharan Logistics for freight and forwarding of goods exported by the assessee are concerned, claim of the assessee is that Hariharan Logistics had accounted the whole of the payments received by the assessee as its income and paid due taxes thereon. Coordinate bench in the case of Adanda Marakala (supra), had held as under at para 14 to 26 of its order dt.13.09.2013 :

14. In order to find answer to this question, it would be relevant to note down the legislative history of the provision. Section 40 has certain clauses providing for the amounts which are not deductible. Sub-clause (ia) of clause (a) of section 40 was inserted by the Finance (No.2) Act, 2004 with effect from 1st April, 2005 reading as under:-

“40. Notwithstanding anything to the contrary in sections 30 to 38, the following amounts shall not be deducted in computed the income chargeable under the head ‘Profits and gains of business or profession’—

.....

(ia) any interest, commission or brokerage, fees for professional services or fees for technical services payable to a resident, or amounts payable to a contractor or sub-contractor, being resident, for carrying out any work (including supply of labour for carrying out any work), on or, after deduction, has not been paid during the previous year, or in the subsequent year before the expiry of the time prescribed under sub-section (1) of section 200 :

Provided that where in respect of any such sum, tax has been deducted in any subsequent year or, has been deducted in the previous year but paid in any subsequent year after the expiry of the time prescribed under sub-section (1) of section 200, such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.

Explanation. – For the purposes of this sub-clause, -

- (i) “commission or brokerage” shall have the same meaning as in clause (i) of the Explanation to section 194H;
- (ii) “fees for technical services” shall have the same meaning as in Explanation 2 to clause (vii) of sub-section (1) of section 9;
- (iii) “professional services” shall have the same meaning as in clause (a) of the Explanation to section 194J;
- (iv) “work” shall have the same meaning as in Explanation III to section 194C; ”

The Memorandum explaining the provisions in the Finance Bill explained the rationale of the insertion of the new provision in following words :-

“With a view to **augment compliance of TDS provisions**, it is proposed to extend the provisions of section 40(a)(i) to payments of interest, commission or brokerage, fees for professional services or fees for technical services to residents, and payments to a resident contractor or sub-contractor for carrying out any work (including supply of labour for carrying out any work), on which tax has not been deducted or after deduction, has not been paid before the expiry of the time prescribed under sub-section (1) of section 200 and in accordance with the other provisions of Chapter XVII-B. It is also proposed to provide that where in respect of payment of any sum, tax has been deducted under Chapter XVII-B or paid in any subsequent year, the sum of payment shall be allowed in computing the income of the previous year in which such tax has been paid.

The proposed amendment will take effect from 1st day of April, 2005 and will, accordingly, apply in relation to the assessment year 2005-2006 and subsequent years. [Clause 11]”

Thereafter the Finance Act, 2008 made amendment to clause (a) in sub-clause (ia) in section 40 with retrospective effect from 1st April, 2005. The section as amended by the Finance Act, 2008 read as under:-

“(ia) any interest, commission or brokerage, rent, royalty, fees for professional services or fees for technical services payable to a resident, or amounts payable to a contractor or sub-contractor, being resident, for carrying out any work (including supply of labour for carrying out any work), on which tax is deductible at source under Chapter XVII-B and such tax has not been paid,-

(A) in a case where the tax was deductible and was so deducted during the last month of the previous year, on or before the due date specified in sub-section (1) of section 139 ; or

(B) in any other case, on or before the last day of the previous year.

Provided that where in respect of any such sum, tax has been deducted in any subsequent year, or has been deducted-

(A) during the last month of the previous year but paid after the said due date ; or

(B) during any other month of the previous year but paid after the end of the said previous year, such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.” ;

15. The Finance Act, 2008 brought out amendment to section 40(a)(ia) w.r.e.f. 1.4.2005 by relaxing earlier position to some extent. It made two categories of defaults causing disallowance on the basis of the period of the previous year in which tax was deductible. The first category of disallowances included the cases in which tax was deductible and was so deducted during the last month of the previous year but there was failure to pay such tax on or before the due date specified in sub-section (1) of section 139 of the Act. In other words, if any amount on which tax was deductible during last month of the previous year, that is March 2005, but was paid before 31st October, 2005, being the due date u/s 139(1), the deductibility of the amount was kept intact. The second category included cases other than those given in category first. To put it simply, if tax was deductible and was so deducted during the first eleven months of the previous year, that is, up to February, 2005, the disallowance was to be made if the assessee failed to pay it before 31st March, 2005.

16. Then came the amendment to section 40(a)(ia) by the Finance Act, 2010 with retrospective effect from 1st April, 2010. The provision so amended, now reads as under :-

“(ia) any interest, commission or brokerage, rent, royalty, fees for professional services or fees for technical services payable to a resident, or amounts payable to a contractor or sub-contractor, being resident, for carrying out any work (including supply of labour for carrying out any work), on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or; after deduction, has not been paid on or before the due date specified in sub-section (1) of section 139

Provided that where in respect of any such sum, tax has been deducted in any subsequent year, or has been deducted during the previous year but paid after the due date specified in sub-section (1) of section 139, such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.”

17. From the above provision as amended by the Finance Act, 2010 with retrospective effect from 1st April, 2010 it can be seen that the only difference which this amendment has made is dispensing with the earlier two categories of defaults as per the Finance Act, 2008, as discussed in the earlier para, causing disallowance on the basis of the period of the previous year during which tax was deductible. The first category of disallowances included the cases in which tax was deductible and was so deducted during the last month of the previous year but there was failure to pay such tax on or before the due date specified in sub-section (1) of section 139. The Finance Act, 2010 has not tinkered with this position. The second category of the Finance Act, 2008 which required the deposit of tax before the close of the previous year in case of deduction during the first eleven months, as a pre-condition for the grant of deduction in the year of incurring expenditure, has been altered. The hitherto requirement of the assessee deducting tax at source during the first eleven months of the previous year and paying it before the close of the previous year up to 31st March of the previous year as a requirement for grant of deduction in the year of incurring such expenditure, has been eased to extend such time for payment of tax up to due date u/s 139(1) of the Act. As per the new amendment, the disallowance will be made if after deducting tax at source, the assessee fails to pay the amount of tax on or before the due date specified in subsection (1) of section 139 of the Act. The effect of this amendment is that now the assessee deducting tax either in the last month of the previous year or first eleven months of the previous year shall be entitled to deduction of the expenditure in the year of incurring it, if the tax so deducted at source is paid on or before the due date u/s 139(1). This is the only difference which has been made by the Finance Act, 2010.
18. The question as to whether the Amendment by the Finance Act, 2010 as aforesaid is prospective or retrospective from 1.4.2005 came up for consideration before the Mumbai Special Bench ITAT in the case of *Bharati Shipyard Ltd.* Before the Special Bench, it was argued that the amendment was made with a view to remove the unnecessary hardship caused to the assessee by the earlier provision. The Special Bench by its *order dated 9.9.2011*, however, held that the amendment carried out by the Finance Act, 2010 with retrospective effect from assessment year

2010-2011 cannot be held to be retrospective from assessment year 2005-2006. The Special Bench held that the amendment brought out by the Finance Act, 2010 to section 40(a)(ia) w.e.f. 01.04.2010, is not remedial and curative in nature.

19. Prior to the decision of the Special Bench, identical issue had come up for consideration before the ITAT Kolkata Bench in the case of *Virgin Creations Vs. ITO, Ward 32(4), Kolkata ITA No. 267/Kol/2009 for AY 05-06*. The issue that arose for consideration was disallowance of expenses u/s.40(a)(ia) claimed as deduction while computing income from business being embroidery charges, dyeing charges, interest on loan and freight charges without deducting tax at source. The Embroidery charges were paid between 22nd may, 2004 to 30.11.2004. Tax had been deducted at source but were paid to the Government only on 28.10.2005 and not within the time contemplated by Section 200(1) of the Act. The dyeing charges were paid between 5.4.2004 to 20.8.2004. Tax was deducted at source but was paid to the Government only on 28.10.2005. Freight outward charges were paid without deduction of tax at source. Interest on loans were credited to the creditors account on 31.3.2005 to the extent they were paid after the due date for filing return of income u/s.139(1) of the Act, the disallowance was made u/s.40(a)(ia) of the Act. Before the Tribunal, the Assessee contented that the amendment by the Finance Act, 2010 with retrospective effect from 1st April, 2010 whereby amount of tax deducted at the time of making payment in respect of expenditure referred to in Sec.40(a)(ia) of the Act, if paid to the Government on or before the due date for filing the return of income due date u/s 139(1) of the Act should be allowed as a deduction. In other words it was argued that the amendment by the Finance Act, 2010 to the provisions of Sec.40(a)(ia) has to be held to be retrospective w.e.f. 1-4-2005. The ITAT Kolkata Bench by its order dated 15.12.2010, held as follows:

“8. After hearing the rival submissions and on careful perusal of the materials available on record, keeping in view of the fact that though the Ld.D.R. submitted that the decisions of the Coordinate Benches are not binding and the Kolkata benches may take a different view, since Mumbai Bench after analyzing the provisions of Sec.40(a)9ia since its inception and various amendments made to the same including the suggestion made by the Industry in the form of representation in their pre-budget memorandum to the Hon’ble Finance Minister and by applying the decision of the Hon’ble Apex Court in the case of Alom Extrusions Ltd., has observed that “The provisions of Section 40(a)(ia) as stood prior to the amendments made by the Finance Act 2010 thus were resulting into unintended consequences and causing grave and genuine hardships to the assesses who had substantially complied with the relevant TDS

provisions by deducting the tax at source and by paying the same to the credit of the Government before the due date of filing of their returns u/s.139(1). In order to remedy this position and to remove the hardships which was being caused to the assessee belonging to such category, amendments have been made in the provisions of Section 40(a)(ia) by the Finance Act, 2010. The said amendments, in our opinion, thus are clearly remedial/curative in nature as held by the Hon'ble Supreme Court in the case of Allied Motors Pvt. Ltd. (supra) and Mom Extrusions Ltd. (supra) and the same therefore would apply retrospectively w.e.f. 1st April, 2005. In the case of R.B.Jodha Mal Kuthiala 82 ITR 570, it was held by the Hon'ble Supreme Court that a proviso which is inserted to remedy unintended consequences and to make the provision workable, requires to be treated as retrospective in operation so that a reasonable interpretation can be given to the section as a whole. In the present case, the amount of tax deducted at source from the freight charges during the period 01/04/2005 to 28/02/2006 was paid by the Assessee in the month of July and August 2006 i.e., well before the due date of filing of its return of income for the year under consideration. This being the undisputed position, we hold that the disallowance made by the A.O. and confirmed by the learned CIT(A) on account of freight charges by invoking the provisions of Section 40(a)(ia) is not sustainable as per the amendments made in the said provisions by the Finance Act, 2010 which, being remedial/curative in nature, have retrospective application", we find no reason to deviate from the decisions of the ITAT's Mumbai Bench and Ahmedabad Bench, in the absence of a contrary view, except the other benches decisions or any other High Court. Therefore, respectfully following the decision of the Coordinate Benches (supra), we allow the ground nos. I to 3 of the assessee's appeal."

20. As against the aforesaid decision, the Revenue preferred appeal before the Hon'ble Calcutta High Court. The Hon'ble Calcutta High Court in *ITA No. 302 of 2011, GA 3200/2011 decided on 23.11.2011*, held as follows:

"We have heard Mr. Nizamuddin and gone through the impugned judgment and order. We have also examined the point formulated for which the present appeal is sought to be admitted. It is argued by Mr. Nizamuddin that this court needs to take decision as to whether section 40(A)(ia) is having retrospective operation or not.

The learned Tribunal on fact found that the assessee had deducted tax at source from the paid charges between the period April 1, 2005 and

April 28, 2006 and the same were paid by the assessee in July and August 2006, i.e. well before the due date of filing of the return of income for the year under consideration. This factual position was undisputed. Moreover, the Supreme Court, as has been recorded by the learned Tribunal, in the case of Allied Motors Pvt. Ltd. and also in the case of Alom Extrusions Ltd., has already decided that the aforesaid provision has retrospective application. Again, in the case reported in 82 ITR 570, the Supreme Court held that the provision, which has inserted the remedy to make the provision workable, requires to be treated with retrospective operation so that reasonable deduction can be given to the section as well. In view of the authoritative pronouncement of the Supreme Court, this court cannot decide otherwise. Hence we dismiss the appeal without any order as to costs.”

21. Further liberalization of provisions of Section 40(a)(ia) was made through amendment brought by the Finance Act 2012. With a view to liberalize provisions of Section 40(a)(ia) of the Act Finance Act 2012 brought amendment w.e.f 01.04.2013 as under. The following second proviso shall be inserted in sub-clause (ia) of clause (a) of Section 40 by the Finance Act, 2012, w.e.f. 1-4-2013 :

“Provided further that where an assessee fails to deduct the whole or any part of the tax in accordance with the provisions of Chapter XVII-B on any such sum but is not deemed to be an assessee in default under the first proviso to sub-section (1) of Section 201, then, for the purpose of this sub-clause, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the resident payee referred to in the said proviso.”

22. Since provisions of Section 40(a)(ia) as amended by Finance Act, 2012 is linked to Section 201 of the Act, in which a proviso was inserted, it is necessary to look into those provisions which read thus:

“Sec.201: (1) Where any person, including the principal officer of a company –

(a) who is required to deduct any sum in accordance with the provisions of this Act; or

(b) referred to in sub-section (1A) of Section 192, being an employer, does not deduct, or does not pay, or after so deducting fails to pay, the whole or any part of the tax, as required by or under this Act, then, such person, shall, without prejudice to any other

consequences which he may incur, be deemed to be an assessee in default in respect of such tax:

Provided that any person, including the principal officer of a company, who fails to deduct the whole or any part of the tax in accordance with the provisions of this Chapter on the sum paid to a resident or on the sum credited to the account of a resident shall not be deemed to be an assessee in default in respect of such tax if such resident –

(i) has furnished his return of income under Section 139;

(ii) has taken into account such sum for computing income in such return of income; and

(iii) has paid the tax due on the income declared by him in such return of income, and the person furnishes a certificate to this effect from an accountant in such form as may be prescribed:

23. Memorandum explaining the provisions while introducing Finance Bill, 2012 provides the justification of the amendment to section 40(a)(ia) in the following words:-

“In order to rationalise the provisions of disallowance on account of non-deduction of tax from the payments made to a resident payee, it is proposed to amend section 40(a)(ia) to provide that where an assessee makes payment of the nature specified in the said section to a resident payee without deduction of tax and is not deemed to be an assessee in default under section 201(1) on account of payment of taxes by the payee, then, for the purpose of allowing deduction of such sum, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the resident payee.”

24. The provisions of Sec.40(a)(ia) of the Act are meant to ensure that the Assessee's perform their obligation to deduct tax at source in accordance with the provisions of the Act. Such compliance will ensure revenue collection without much hassle. When the object sought to be achieved by those provisions are found to be achieved, it would be unjust to disallowance legitimate business expenses of an Assessee. Despite due collection of taxes due, if disallowance of genuine business expenses are made than that would be unjust enrichment on the part of the Government as the payee would have also paid the taxes on such income. In order to remove this anomaly, this amendment has been introduced. In case of payment to non resident, the government does not have any other

mechanism to recover the due taxes. Hence, no amendment was made in section 40(a)(i). The legislature has not given blanket deduction under section 40(a)(ia). The deduction as per amended section will be allowed only if the -

- (i) payee has furnished his return of income under section 139;
- (ii) payee has taken into account such sum for computing income in such return of income; and
- (iii) payee has paid the tax due on the income declared by him in such return of income,

and the payer furnishes a certificate to this effect from an accountant in such form as may be prescribed.

25. The question is as to whether the amendment made as above is prospective or retrospective w.e.f. 1.4.2005 when the provisions of Sec.40(a)(ia) were introduced. Keeping in view the purpose behind the proviso inserted by the Finance Act, 2012 in section 40(a)(ia) of the Act, it can be said to be declaratory and curative in nature and therefore, should be given retrospective effect from 1st April, 2005, being the date from which sub-clause (ia) of section 40(a) was inserted by the Finance (No. 2) Act, 2004. In *CIT Vs. Alom Extrusions Ltd.* 319 ITR 306 (SC), the Hon'ble Supreme Court had to deal with the question, whether omission (deletion) of the second proviso to s. 43B of the IT Act, 1961, by the Finance Act, 2003, operated w.e.f. 1st April, 2004, or whether it operated retrospectively w.e.f. 1st April, 1988? Prior to Finance Act, 2003, the second proviso to s. 43B of the IT Act, 1961 (for short, "the Act") restricted the deduction in respect of any sum payable by an employer by way of contribution to provident fund/superannuation fund or any other fund for the welfare of employees, unless it stood paid within the specified due date. According to the second proviso, the payment made by the employer towards contribution to provident fund or any other welfare fund was allowable as deduction, if paid before the date for filing the return of income and necessary evidence of such payment was enclosed with the return of income. In other words, if contribution stood paid after the date for filing of the return, it stood disallowed. This resulted in great hardship to the employers. They represented to the Government about their hardship and, consequently, pursuant to the report of the Kelkar Committee, the Government introduced Finance Act, 2003, by which the second proviso stood deleted w.e.f. 1st April, 2004, and certain changes were also made in the first proviso by which uniformity was brought about between payment of fees, taxes, cess, etc., on one hand and contribution made to Employees' Provident Fund, etc., on the other. According to the Department, the omission of the second proviso giving relief to the assessee(s)

[employer(s)] operated only w.e.f. 1st April, 2004, whereas, according to the assessee(s)-employer(s), the said Finance Act, 2003, to the extent indicated above, operated w.e.f. 1st April, 1988 (retrospectively). The Hon'ble Supreme Court held that the deletion of the second proviso was retrospective w.e.f.1.4.2004. The Court considered the scheme of the Act and the historical background and the object of introduction of the provisions of S. 43B. The Court also referred to the earlier amendments made in 1988 with introduction of the first and second provisos. The Court also noted further amendment made in 1989 in the second proviso dealing with the items covered in S. 43B(b) (*i.e.*, contribution to employees welfare funds). After considering the same, the Court was of the view that it was clear that prior to the amendment of 2003, the employer was entitled to deduction only if the contribution stands credited on or before the due date given in the Provident Fund Act on account of second proviso to S. 43B. The situation created further difficulties and as a result of representations made by the industry, the amendment of 2003 was carried out which deleted the second proviso and also made first proviso applicable to contribution to employees welfare funds referred to in S. 43B(b).

“15. We find no merit in these civil appeals filed by the Department for the following reasons : firstly, as stated above, s. 43B (main section), which stood inserted by Finance Act, 1983, w.e.f. 1st April, 1984, expressly commences with a non obstante clause, the underlying object being to disallow deductions claimed merely by making a book entry based on mercantile system of accounting. At the same time, s. 43B (main section) made it mandatory for the Department to grant deduction in computing the income under s. 28 in the year in which tax, duty, cess, etc., is actually paid. However, Parliament took cognizance of the fact that accounting year of a company did not always tally with the due dates under the Provident Fund Act, Municipal Corporation Act (octroi) and other tax laws. Therefore, by way of first proviso, an incentive/relaxation was sought to be given in respect of tax, duty, cess or fee by explicitly stating that if such tax, duty, cess or fee is paid before the date of filing of the return under the IT Act (due date), the assessee(s) then would be entitled to deduction. However, this relaxation/incentive was restricted only to tax, duty, cess and fee. It did not apply to contributions to labour welfare funds. The reason appears to be that the employer(s) should not sit on the collected contributions and deprive the workmen of the rightful benefits under social welfare legislations by delaying payment of contributions to the welfare funds. However, as stated above, the second proviso resulted in implementation problems, which have been mentioned hereinabove, and which resulted in the enactment of Finance Act, 2003, deleting the second proviso and bringing about uniformity in the first proviso by equating tax, duty, cess and fee with contributions to welfare

funds. Once this uniformity is brought about in the first proviso, then, in our view, the Finance Act, 2003, which is made applicable by the Parliament only w.e.f. 1st April, 2004, would become curative in nature, hence, it would apply retrospectively w.e.f. 1st April, 1988. Secondly, it may be noted that, in the case of Allied Motors (P) Ltd. Etc. vs. CIT (1997) 139 CTR (SC) 364 : (1997) 224 ITR 677 (SC), the scheme of s. 43B of the Act came to be examined. In that case, the question which arose for determination was, whether sales-tax collected by the assessee and paid after the end of the relevant previous year but within the time allowed under the relevant sales-tax law should be disallowed under s. 43B of the Act while computing the business income of the previous year ? That was a case which related to asst. yr. 1984-85. The relevant accounting period ended on 30th June, 1983. The ITO disallowed the deduction claimed by the assessee which was on account of sales-tax collected by the assessee for the last quarter of the relevant accounting year. The deduction was disallowed under s. 43B which, as stated above, was inserted w.e.f. 1st April, 1984. It is also relevant to note that the first proviso which came into force w.e.f. 1st April, 1988 was not on the statute book when the assessments were made in the case of Allied Motors (P) Ltd. Etc. (supra). However, the assessee contended that even though the first proviso came to be inserted w.e.f. 1st April, 1988, it was entitled to the benefit of that proviso because it operated retrospectively from 1st April, 1984, when s. 43B stood inserted. This is how the question of retrospectivity arose in Allied Motors (P) Ltd. Etc. (supra). This Court, in Allied Motors (P) Ltd. Etc. (supra) held that when a proviso is inserted to remedy unintended consequences and to make the section workable, a proviso which supplies an obvious omission in the section and which proviso is required to be read into the section to give the section a reasonable interpretation, it could be read retrospective in operation, particularly to give effect to the section as a whole. Accordingly, this Court, in Allied Motors (P) Ltd. Etc. (supra), held that the first proviso was curative in nature, hence, retrospective in operation w.e.f. 1st April, 1988. It is important to note once again that, by Finance Act, 2003, not only the second proviso is deleted but even the first proviso is sought to be amended by bringing about an uniformity in tax, duty, cess and fee on the one hand vis-a-vis contributions to welfare funds of employee(s) on the other. This is one more reason why we hold that the Finance Act, 2003, is retrospective in operation. Moreover, the judgment in Allied Motors (P) Ltd. Etc. (supra) is delivered by a Bench of three learned Judges, which is binding on us. Accordingly, we hold that Finance Act, 2003, will operate retrospectively w.e.f. 1st April, 1988 (when the first proviso stood inserted). Lastly, we may point out the hardship and the invidious discrimination which would be caused to the assessee(s) if the contention of the Department is to be accepted that Finance Act, 2003, to the above extent, operated prospectively. Take an

example—in the present case, the respondents have deposited the contributions with the R.P.F.C. after 31st March (end of accounting year) but before filing of the Returns under the IT Act and the date of payment falls after the due date under the Employees' Provident Fund Act, they will be denied deduction for all times. In view of the second proviso, which stood on the statute book at the relevant time, each of such assessee(s) would not be entitled to deduction under s. 43B of the Act for all times. They would lose the benefit of deduction even in the year of account in which they pay the contributions to the welfare funds, whereas a defaulter, who fails to pay the contribution to the welfare fund right upto 1st April, 2004, and who pays the contribution after 1st April, 2004, would get the benefit of deduction under s. 43B of the Act. In our view, therefore, Finance Act, 2003, to the extent indicated above, should be read as retrospective. It would, therefore, operate from 1st April, 1988, when the first proviso was introduced. It is true that the Parliament has explicitly stated that Finance Act, 2003, will operate w.e.f. 1st April, 2004. However, the matter before us involves the principle of construction to be placed on the provisions of Finance Act, 2003.

16. Before concluding, we extract hereinbelow the relevant observations of this Court in the case of CIT vs. J.H. Gotla (1985) 48 CTR (SC) 363 : (1985) 156 ITR 323 (SC), which reads as under :

"We should find out the intention from the language used by the legislature and if strict literal construction leads to an absurd result, i.e., a result not intended to be subserved by the object of the legislation found in the manner indicated before, then if another construction is possible apart from strict literal construction, then that construction should be preferred to the strict literal construction. Though equity and taxation are often strangers, attempts should be made that these do not remain always so and if a construction results in equity rather than in injustice, then such construction should be preferred to the literal construction."

17. For the aforesaid reasons, we hold that Finance Act, 2003, to the extent indicated above, is curative in nature, hence, it is retrospective and it would operate w.e.f. 1st April, 1988 (when the first proviso came to be inserted). For the above reasons, we find no merit in this batch of civil appeals filed by the Department which are hereby dismissed with no order as to costs."

26. We are of the view that the reasoning of the Hon'ble Supreme Court in the case of Alom Extrusions Ltd(supra) will equally to the amendment to Sec.40(a)(ia) of the Act whereby a second proviso was inserted in sub-clause (ia) of clause (a) of Section 40 by the Finance Act,

2012, w.e.f. 1-4-2013. The provisions are intended to remove hardship. It was argued on behalf of the revenue that the existing provisions allow deduction in the year of payment and to that extent there is no hardship. We are of the view that the hardship in such an event would be taxing an Assessee on a higher income in one year and taxing him on lower income in a subsequent year. To the extent the Assessee is made to pay tax on a higher income in one year, there would still be hardship.”

14. In view of the decision of the coordinate bench, assessee can always plead that recipient of the amounts had accounted the income and filed returns and hence the rigors of Section 40(a)(ia) of the Act could not be applied to it. However, question whether the recipients of payments had indeed accounted the amounts and returned the income therefrom in their return of income requires to be verified. We are of the opinion therefore that this issue also requires a fresh look by the AO.

15. In the result, we set aside the orders of lower authorities and remit both the issues under section 40(a)(ia) of the Act, back to the AO for verification afresh in accordance with law.

16. Appeal of the assessee is allowed for statistical purpose.

Order pronounced in the open court on 1st day of October, 2015.

Sd/-

(N. V. VASUDEVAN)
JUDICIAL MEMBER

Sd/-

(ABRAHAM P GEORGE)
ACCOUNTANT MEMBER

MCN

Copy to:

1. The assessee
2. The Assessing Officer
3. The Commissioner of Income-tax
4. Commissioner of Income-tax(A)
5. DR
6. GF, ITAT, Bangalore

By Order
Assistant Registrar