Sec.194R – Rationalization or Vexation?

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The purpose of tax deduction at source has always been to widen the tax net. However, the recently introduced TDS provisions for the past couple of years may have definitely helped the legislature to widen the tax net but at a high compliance cost on part of the deductor. One wonders how would such provisions encourage one to venture into new businesses which is otherwise so popularly promoted by the Government in India. Can any MSME afford such type of compliances? In irony, one may say the legislature gives an opportunity to increase the employment rate in our country. Finance Act 2022 introduced a new section – 194R for the purpose of tax deduction at source from any benefit or perquisite provided to a resident arising from business or the exercise of a profession. With the insertion of section 194R coupled with the guidelines for the implementation of the same issued by the CBDT vide Circular No. 12 of 2022, dated 16th June 2022, now it seems as if almost the entire debit side of one's profit and loss account is exigible to TDS provisions. The intention of this write up is not to interpret word by word the applicability of section 194R, but to bring to notice certain vexed issues that erupt on the insertion of the same on the statute. Let us trail through the several documents that mention about the introduction of this new provision and the carrying forward of the same up till now. This begins with the budget speech and ends with the recently released CBDT Circular 12 of 2022 –

Relevant portion of the Budget Speech –

"Rationalizing TDS Provisions

137. It has been noticed that as a business promotion strategy, there is a tendency on businesses to pass on benefits to their agents. Such benefits are taxable in the hands of the agents. In order to track such transactions, I propose to provide for tax deduction by the person giving benefits, if the aggregate value of such benefits exceeds ` 20,000 during the financial year."

Relevant portion of the Memorandum to the Finance Bill 2022 –

"TDS on benefit or perquisite of a business or profession

As per clause (iv) of section 28 of the Act, the value of any benefit or perquisite, whether convertible into money or not, arising from business or exercise of profession is to be charged as business income in the hands of the recipient of such benefit or perquisite. However, in many cases, such recipient does not

report the receipt of benefits in their return of income, leading to furnishing of incorrect particulars of income.

2. Accordingly, in order to widen and deepen the tax base, it is proposed to insert a new section 194R to the Act to provide that the person responsible for providing to a resident, any benefit or perquisite, whether convertible into money or not, arising from carrying out of a business or exercising of a profession by such resident, shall, before providing such benefit or perquisite, as the case may be, to such resident, ensure that tax has been deducted in respect of such benefit or perquisite at the rate of ten per cent of the value or aggregate of value of such benefit or perquisite. For the purpose of this section, the expression 'person responsible for providing' has been proposed to mean a person providing such benefit or perquisite or in case of a company, the company itself including the principal officer thereof.

2.1 Further, in a case where the benefit or perquisite, as the case may be, is wholly in kind or partly in cash and partly in kind but such part in cash is not sufficient to meet the liability of deduction of tax in respect of whole of such benefit or perquisite, the person responsible for providing such benefit of perquisite shall, before releasing the benefit or perquisite, ensure that tax has been paid in respect of the benefit or perquisite.

2.2 No tax is to be deducted if the value or aggregate value of the benefit or perquisite paid or likely to be paid to a resident does not exceed twenty thousand rupees during the financial year.

2.3 Further, the provisions of the said section shall not apply to an individual or a Hindu undivided family, whose total sales, gross receipts or turnover does not exceed one crore rupees in case of business or fifty lakh rupees in case of profession during the financial year immediately preceding the financial year in which such benefit or perquisite, as the case may be, is provided.

3. This amendment will take effect from 1st July, 2022.

Relevant portion of section 194R as per Finance Act 2022 –

"*194R. (1) Any person responsible for providing to a resident, any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession, by such resident,* shall, **before providing such benefit or perquisite**, as the case may be, to such resident, ensure that tax has been deducted in respect of such benefit or perquisite at the rate of ten per cent. of the value or aggregate of value of such benefit or perquisite*:*

Provided that in a case where the benefit or perquisite, as the case may be, is wholly in kind or partly in cash and partly in kind but such part in cash is not sufficient to meet the liability of deduction of tax in respect of whole of such benefit or perquisite, the person responsible for providing such benefit or perquisite shall, before releasing the benefit or perquisite, ensure that tax required to be deducted has been paid in respect of the benefit or perquisite:

Provided further that the provisions of this section shall not apply in case of a resident where the value or aggregate of value of the benefit or perquisite provided or likely to be provided to such resident during the financial year does not exceed twenty thousand rupees:

……"

The CBDT Circular No. 12 of 2022, the title of which claims to remove the difficulty under sub-section (2) of section 194R shall be dealt with hereunder as and when required.

Lack of correlation

To begin with, the section and the memorandum itself are so worded that there is no corelation with the budget speech. The budget speech very clearly mentions to cover within the ambit the benefits passed on to the agents whereas the section and the memorandum are drafted wide enough to cover any benefit or perquisite, arising from business or the exercise of a profession, provided by any person to a resident. Be that as it may, the CBDT Circular goes in a complete new direction.

Point of time of TDS

The guidelines by way of the said circular do not guide as to when the tax may be deducted. Subsection (1) of section 194R mentions that the person responsible to pay the perquisite or benefit shall,**before providing such benefit or perquisite**, as the case may be, to such resident, ensure that tax has been deducted in respect of such benefit or perquisite at the rate of ten per cent. of the value or aggregate of value of such benefit or perquisite. It may be noted that, unlike other TDS provisions where the liability to deduct tax at source arises at the time of payment or credit, whichever is earlier, section 194R makes the person responsible to deduct the tax at source **before** providing such benefit or perquisite. This could be any time before providing the benefit or perquisite to the beneficiary. Hence, a view may be taken that the payer is not responsible to deduct tax at source at the time of credit of such sum to the account of the beneficiary or a provision in books of accounts if the perquisite of benefit is yet not paid. Cue may be taken from the provisions of section 194B wherein the responsibility of TDS arises at the time of payment of winnings from any lottery or crossword puzzle. Reference is made to judgment of the Gauhati High Court in the case of Director of State Lotteries v. Assistant Commissioner of Income-tax [TS-5104-HC-1999(GAUHATI)-O] (Civil Rule Nos. 405 AND 2786 OF 1994)

Type of income for the recipient

Referring to the guidelines provided under question 1 of the circular, the deductor is not required to check whether the amount of benefit or perquisite that he is providing would be taxable in the hands of the recipient under clause (iv) of section 28 of the Act. The amount could be taxable under any other section like section 41(1) etc. The circular further mentions that Section 194R of the Act casts an obligation on the person responsible for providing any benefit or perquisite to a resident, to deduct tax at source at the rate of 10%. There is no further requirement to check whether the amount is taxable in the hands of the recipient or under which section it is taxable. It is so obvious that this explanation is a complete antithesis to the wording of the section and the memorandum explaining the same. There are innumerable judicial pronouncements which have considered the Budget Speech and the Memorandum explaining the Finance Bill for the interpretation and to determine the intention behind any provisions on the statute. Whereas, in case of Section 194R there is simply no coordination at all between these documents.

Question 3 of the CBDT Circular clarifies that the benefits and perquisites even in the nature of a capital assets in the hands of the recipients are covered under this TDS provision and that the same is held by many courts. The irony is that even at this stage, the CBDT has explained the concept relying only on judicial precedents relating to section 28(iv) of the Income-tax Act.

Applicable to cash and kind, both

Moving ahead to the guidelines provided under Question No. 2 of the circular which goes to mention that the proviso clearly indicates the intent of legislature that there could also be situations where benefit or perquisite is in cash or the benefit or perquisite is in kind or partly in cash and partly in kind. Thus, section 194R of the Act clearly brings in its scope the situation where the benefit or perquisite is in cash or in kind or partly in cash or partly in kind. Lately, it has been an observation that the documents released by the CDDT are very similar to a legal opinion drafted by a tax consultant wherein various judicial pronouncements are referred for the interpretation of the statute. It is very obvious to mention at this stage that considering the Memorandum to the Finance Bill, only the incomes covered under section 28(iv) were envisaged to be covered and the Hon'ble Supreme Court in the Mahindra & Mahindra Case [TS-220-SC-2018] (Civil Appeal Nos. 6949-6950 OF 2004 & Others) has very clearly held *that on a plain reading of Section 28 (iv) of the IT Act, prima facie, it appears that for the applicability of the said provision, the income which can be taxed shall arise from the business or profession. Also, in order to invoke the provision of Section 28 (iv) of the IT Act, the benefit which is received has to be in some other form rather than in the shape of money*. At this juncture it may be noted that, these guidelines are not in tandem with the Memorandum and the Apex Court ruling. Moreover, the intention was to cover the benefits and perquisites provided in kind which went unnoticed and unreported. The cash paid is in any which way covered under one or the other provision of TDS. Moreover, it may also be noted that if the payer bears any part of the tax then the question arises whether grossing up provisions under section 195A may be complied with. According to the provisions of section 195A, where under an agreement or other arrangement, the tax chargeable on any income (covered under any other provisions of TDS) is to

be borne by the person by whom the income is payable, then, for the purposes of deduction of tax under those provisions such income shall be increased to such amount as would, after deduction of tax thereon at the rates in force for the financial year in which such income is payable, be equal to the net amount payable under such agreement or arrangement. The CBDT Circular explains to cover cash element as well and the tax borne by the deductor is a cash benefit so the same may be covered under section 194R.

Reimbursements

The CBDT in its guidelines pertaining to question 7 has dealt with the issue of reimbursement of out-of-pocket expenses with the help of an illustration. To summarise, if the invoice for the expense is in the name of the deductor, the same is not in the nature of benefit or perquisite but if the invoice is in the name of the service provider/consultant and if the expense is reimbursed by the deductor then the same is covered under section 194R for TDS. It is noteworthy at this stage that this issue of reimbursement was settled by the CBDT way back in the year 1995 in Circular No. 715. The relevant portion reads as under –

"Question 30 : Whether the deduction of tax at source under sections 194C and 194J has to be made out of the gross amount of the bill including reimbursements or excluding reimbursement for actual expenses ?

Answer : Sections 194C and 194J refer to any sum paid. Obviously, reimbursements cannot be deducted out of the bill amount for the purpose of tax deduction at source."

After the guidelines vide the CBDT Circular 12 of 2022, one would wonder whether the TDS on reimbursements should be done under section 194R or the already prevalent TDS sections like 194C, 194J, 194H, etc. Maybe we might soon get another set of guidelines to interpret these guidelines!!

Above listed are only a few anomalies that struck immediately on reading the above listed documents. The actual adversities that will be faced shall unfold in times to come. In India, the stories with morals from Panchtantra and various other mythologies have taught many a times that the benefit of one should not be at the cost of others' pain. Did those stories mention that the said morals are not applicable to the Exchequer?!!!