UNDERSTANDING TDS DEDUCTION AND ITS RESOLUTION

Introduction

Tax Deducted at Source (TDS) is a mechanism introduced by the Income Tax Department of India to collect tax at the source of income generation. It ensures timely tax collection and reduces the chances of tax evasion.

What is TDS?

TDS is applicable on various payments such as salaries, rent, interest, professional fees, and commission. The deductor (payer) is responsible for deducting the applicable percentage of tax before making the payment to the deductee (payee). The deducted tax is then deposited with the government within the specified timelines. TDS is deducted either PAN based and/or TAN based depending upon the nature of income. For eg., TDS on purchase of property and/or payment of rent for personal use is PAN based while TDS on professional fees, contractors, commission, etc is TAN based and applicable only on fulfillment of certain criteria(s).

Consequences of Non-Deduction of TDS

TDS not deducted or deposited incorrectly may lead to non-compliance. Failure to deduct or deposit TDS can result in severe penalties and interest charges. The deductor may be treated as an 'assessee in default' and subjected to the following consequences:

- Interest at the rate of **1% per month** for non-deduction
- Interest at **1.5% per month** for non-payment after deduction
- Disallowance of the expense under Section 40(a)(ia) of the Income Tax Act

Communications issued by department for short/non-deduction of TDS on rent paid to landlord

The tax department has initiated an extensive e-campaign via the Insight portal, issuing communicatins in cases of short or non-deduction of TDS on rent payments. This campaign primarily targets the detection of fraudulent house rent allowance (HRA) claims by salaried employees.

Under **Section 194IB** of the Income Tax Act, individuals or Hindu Undivided Families (HUFs) paying rent on property used for personal use exceeding **Rs. 50,000 per month** are obligated to deduct TDS at a rate of **2%** (previously **5%**). Non-compliance with this requirement often results in the issuance of such notices.

In cases where TDS has not been deducted, the department may treat the payer as an **assessee-in-default**, potentially leading to litigation.

Resolutions:

Probable resolutions for PAN-based TDS deductions (rent, purchase of property) include:

1. **Filing the Relevant Form**: The payer can file the applicable form, pay the necessary interest, and settle any late fees.
2. **Relying on Judicial Precedent**: The payer may invoke the ruling of the **Supreme Court** in the case of *Hindustan Coca Cola Beverages P. Ltd. v. CIT* [2007] 163 Taxman 355. The Court held that if the deductor fails to deduct TDS but the deductee has already paid tax on the income, the department cannot recover the tax again from the deductor by treating them as an assessee-in-default. However, the interest liability shall still stand payable.

<u>It is important to note that pursuing a litigative resolution can be a prolonged process, potentially taking years for final resolution. Therefore, timely compliance with TDS provisions remains the most effective way to avoid such complications.</u>

Probable resolutions for TAN-based TDS deductions (contractor, salary, commission, professional fees, etc) include:

1. **Form 26A** – Based on the judgement of Hindustan Coca Cola Beverages P. Ltd. (supra) CBDT had introduced Form 26A. It provides a remedy for cases where TDS was not deducted, but the payee has duly paid the taxes on the corresponding income. It is a certificate issued by a Chartered Accountant (CA) under Section 201(1) of the Income Tax Act, ensuring that the tax liability has been discharged by the payee.

Steps to Resolve Through Form 26A:

1. **Verification of Tax Payment:** Ensure that the payee has reported the income and paid the applicable tax.
2. **Engagement of a Chartered Accountant:** Obtain a certificate from a CA confirming the tax payment using Form 26A.
3. **Filing Form 26A:** The deductor needs to file Form 26A electronically on the TRACES portal.
4. **Approval by the Assessing Officer:** The Assessing Officer reviews the submission and approves the request if satisfied.

Benefits of Using Form 26A

- Avoidance of penal consequences for non-deduction of TDS
- Relief from being considered as an 'assessee in default'
- Restoration of expense deduction under Section 40(a)(ia)
- Reduced liability of interest

Conclusion

While TDS compliance is a critical responsibility, non-deduction can be addressed effectively through Form 26A if the payee has paid taxes on the income. Although, Form 26A is presently not available for PAN based filings, we have raised the same with CBDT and await clarification in the matter. Timely resolution through this mechanism can safeguard an assessee from penalties and ensure smooth financial operations

For any clarification you may feel free to contact us at hsco@singhvica.com

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