

Second proviso to section 40(a)(ia) has retrospective effect

Summary – The High Court of Delhi in a recent case of Ansal Land Mark Township (P.) Ltd., (the Assessee) held that Second proviso to section 40(a)(ia) which states that TDS shall be deemed to be deducted and paid by a deductor if resident recipient has disclosed the amount in his return of income and paid tax thereon, is retrospective in nature

The issue that arose before the High Court was -

- Whether the second proviso to Section 40(a)(ia) (inserted by the Finance Act, 2012), which states that TDS shall be deemed to be deducted and paid by a deductor if resident recipient has disclosed the amount in his return of income and paid tax thereon, is retrospective in nature or not ?

The High Court held as under-

- Section 40(a)(ia) was introduced by the Finance (No. 2) Act, 2004 to ensure that an expenditure should not be allowed as deduction in the hands of an assessee in a situation where income embedded in such expenditure has remained untaxed due to tax withholding lapses by the assessee.
- Hence, section 40(a)(ia) is not a penalty provision for tax withholding lapse but it is a provision introduced to compensate any loss to the revenue in cases where deductor hasn't deducted TDS on amount paid to deductee and, in turn, deductee also hasn't offered to tax income embedded in such amount.
- The penalty for tax withholding lapse per se is separately provided under section 271C. and, therefore, section 40(a)(ia) isn't attracted to the same. Hence, an assessee could not be penalized under section 40(a)(ia) when there was no loss to revenue.
- The Agra Tribunal in the case of *Rajiv Kumar Agarwal v. ACIT [2014] 45 taxmann.com 555 (Agra - Trib.)* had held that the second proviso to Section 40(a)(ia) is declaratory and curative in nature and has 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, even though the Finance Act, 2012 had not specifically stated that proviso is retrospective in nature
- The High Court affirmed the ratio laid down by The Agra Tribunal and held that said proviso is declaratory and curative in nature and has retrospective effect from 1st April 2005.