

No TDS on reimbursement of expenses if it had no income element: HC

Summary – The High Court of Karnataka in a recent case of Kalyani Steels Ltd., (the Assessee) held that If there is no income embedded in a payment, then TDS provisions would not apply as TDS is only an alternative method of collection of Taxes

Facts

- The assessee was engaged in the business of manufacture of steel. It had made payment to a company named 'HSL' towards managerial and technical services rendered by way of operating and maintaining an integrated steel plant.
- The Assessing Officer noted that HSL was a service company and managed an integrated steel plant for assessee, the required labour and staff for the services had been employed by HSL and HSL had used its assets and machineries for rendering the agreed services. Further, amounts received towards service charges had been accounted in the Profit & Loss account of HSL and the same was offered to tax. Hence, the Assessing Officer held that, the assessee was in default under section 201 for not deducting TDS under section 194J and, consequently, interest under section 201(1A) was computed.
- The Commissioner (Appeal) concluded that the payment made by the assessee to HSL was reimbursement of expenses and there was no liability to deduct TDS under section 194J and hence, section 201(1) and 201(1A) were not justifiable.
- The assessee contended that as per the terms of agreement between them, the assessee had reimbursed the expenses incurred by HSL in performance of its obligations. The said payment did not comprise of any income component in the hands of HSL. Thus, it was argued that there being no income in the hands of HSL, section 194J was not applicable.

Held

- A reading of section 194J discloses that, an amount equal to ten percent of such sum as income-tax has to be deducted on income comprised therein, by a person not being an individual or a HUF, who is responsible for paying a resident any sum towards fees for technical services; as per clause (b) of section 194J(1), the relevant factor is 'income comprised'. To attract this provision, there must be an income comprised therein. Section 2(24) defines the income. The reimbursement of expenses incurred by HSL, cannot be categorized as income under section 2(24).
- Section 190 provides for deduction at source and advance payment. This provision makes it clear that deduction at source shall be on such income not otherwise. The primary factor to attract section 194J is the ingredient of 'income comprised therein'. If no income was reflected in the balance sheet and Profit & Loss account of HSL towards the reimbursement charges paid on cost to cost basis by KSL it ceases to have the character of income. As such the assessee cannot, be treated

as the assessee in default in not deducting tax at source under section 194J. The arguments of the revenue that the fees paid by the assessee is towards technical services is imaginary one not established with substantial material.

- The Assessing Officer proceeded to pass the orders under sections 201 and 201(1A) on the footing that the assessee was required to deduct tax from the payments made to HSL irrespective of the fact that the said payments include element of income or not. This approach of the Assessing Officer is contrary to section 194J which in unequivocal terms describes deduction of income tax on income comprised therein.
- It is true that if there is no income embedded in a payment, then TDS provisions would not apply as TDS is only an alternative method of collection of Taxes.
- In view of the factual finding of the appellate authorities that the payment made by assessee to HSL for various expenses incurred would be a reimbursement and not a fee for technical services, section 194J is not attracted.
- The CBDT in Circular No. 715 dated 3-8-1995 has clarified that the reimbursement cannot be deducted out of the bill amount for the purpose of TDS. The Assessing Officer's view is against the intent of the said circular.
- Under the circumstances, the assessee falls outside the scope of section 194J read with section 200 during the relevant assessment years. Consequently, the provisions of sections 201 and 201(1A) are not attracted.