

No additions on basis of TDS claimed if corresponding income not taxable due to cash system of accounting

Summary – The Delhi ITAT in a recent case of Dhruv Sachdeva., (the Assessee) held that In terms of Rule 37BA, revenue could not, merely because credit for tax deducted at source was erroneously claimed by assessee, bring corresponding professional receipts to tax, if such receipts were otherwise not assessable as income in accordance with law

Facts

- The assessee was following cash system of account. He received certain amount as professional receipts after payer deducted tax at source under section 194J.
- The assessee claimed credit for prepaid taxes on account of TDS, even in respect of those professional receipts appearing in Form 26AS which were not shown by the assessee as professional receipt in the return of income for relevant year.
- In course of assessment, revenue authorities made addition which had resulted because of mismatch between gross professional receipts as per Form 26AS and the receipts shown by the assessee in the return of income.
- On second appeal:

Held

- In the case of the assessee *i.e.* the Payee, deductors have deducted tax at source under section 194J and under section 194A. Under these provisions, the deductor is required to deduct tax at source at the time of credit of the specified sum or income (as the case may be) to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier. Thus, the deductor is required to deduct tax at source at the time when the sum or income (as the case may be) is credited to the account of the payee, even if actual payment is made later. At times, a situation may arise, as has happened in the case of the assessee, that actual payment of certain sum(s) or income (as the case may be) may be made to the payee (here, the Assessee) in a subsequent year although tax has been deducted at source by the deductor in an earlier year, because the sum or income (as the case may be) was credited by the deductor to the account of the payee, in such earlier year.
- In such situations, if the payee follows cash system of accounting instead of mercantile system, even though the sum or income (as the case may be) has been credited to the account of the payee and the corresponding amount has accrued as income of the payee in the earlier year, the payee does not recognize it as income of the earlier year, and offers it as income of the subsequent year (the year in which actual payment was received) in accordance with cash system of accounting. This is what has happened in the present case: though certain sums/income appear in Form 26AS for this

year (because tax was deducted at source in this year) the assessee has not offered it as income in the return of income because actual payment was not received by the assessee in this year; and these amounts have been disclosed by the assessee as income in a subsequent year, in the year in which it was actually received, in accordance with cash system of accounting.

- The Commissioner (Appeals) confirmed the aforesaid addition made by the Assessing Officer by taking note of Rule 37BA of Income Tax Rules, 1962("I.T. Rules", for short) and upheld this addition on the ground that the assessee had taken credit of the corresponding tax deducted at source. However, the Commissioner (Appeals) has not interpreted the provisions of law correctly. As per Rule 37BA, credit for tax deducted at source and paid to the Central Government is to be given for the Assessment Year for which such income is assessable. However, provisions under Rule 37BA of 1962. Rules do not authorize Revenue to bring such amounts to tax which are not assessable during the year on the basis of regular method of accounting followed by the assessee. Section 145(1) makes it abundantly clear that income chargeable under the head of "Profit and Gain of business or profession" shall be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee. If the assessee has erroneously taken credit for prepaid taxes on account of tax deducted at source; then having regard to Rule 37BA of 1962 Rules, Revenue will be justified in denying credit for such amount of prepaid taxes on account of tax deducted at source. However, Revenue cannot, merely because credit for tax deducted at source has been erroneously claimed by the assessee, bring corresponding professional receipts to tax, if such receipts are otherwise not assessable as income in accordance with law. In this case both sides, Revenue as well as assessee, are in error of law. On one hand, the assessee has erroneously claimed credit for prepaid taxes on account of tax deducted at source even in respect of such amounts which are not assessable to tax in this year as per method of accounting regularly followed by the assessee.
- On the other hand, revenue has added certain amounts as income of this year, even though these amounts were not actually received in this year and were not, under cash system of accounting regularly followed by the assessee, chargeable as income of this year, in view of unambiguous provisions prescribed under section 145(1). The assessee distorted the law by wrongly claiming credit for prepaid taxes on account of tax deducted at source; even though corresponding amounts are not offered as income, and thus the approach of the assessee was to distort law.
- On the other side, the approach of revenue was to wrongly invert the law by erroneously charging such amounts to tax which are not assessable as assessee's income of this year under cash system of accounting regularly followed by the assessee, merely because assessee has claimed credit for tax deducted at source on corresponding amounts; instead of following the correct approach where under revenue should have allowed credit for tax deducted as source in respect of such amounts only which are assessable as income of this year in accordance with cash system of accounting regularly followed by assessee. The approaches of both assessee and revenue are wrong.
- It is not permitted for anyone to either distort or to invert law. Therefore, the orders of Commissioner (Appeals) and the Assessing Officer are set aside and this matter is restored to the file

of the Assessing Officer to re-compute the income of the assessee in accordance with cash system of accounting, which is the system of accounting regularly employed by the assessee; and to give credit for prepaid taxes on account of tax deducted at source, as per law, having regard to section 199, read with rule 37BA of Income Tax Rules.