IN THE INCOME TAX APPELLATE TRIBUNAL
BENCH 'C' KOLKATA

ITA No.964 (Kol) of 2009
Assessment Year: 2006-2007

S K SAIFUDDIN
KOLKATA
PAN NO:AUHPS2758N

Vs

INCOME TAX OFFICER
WARD-32(2), KOLKATA

D K Tyagi, JM and C D Rao, AM

Dated: February 17, 2011

Appellant Rep by: Sri Indranil Banerjee
Respondent Rep by: Sri B B Mohanty, CIT

ORDER

Per: D K Tyagi:

This appeal by the assessee for assessment year 2006-07 is directed against the order dated 24.3.2009 of C.I.T.(A)-XIX, Kolkata. The assessee has raised several grounds which are all directed against the action of ld. C.I.T.(A) in confirming the disallowance of labour charges of Rs.2,70,42,450/- u/s. 40(a)(ia) of the Act.

2. The assessee is engaged in the business of performing designing and embroidery work on the dress material and clothes supplied by different shopkeepers mainly from Kolkata under his proprietorship concern M/s. Modern Enterprise. In Form 3CD of the Auditor's report, nature of business or profession of the assessee was not mentioned. For doing this job, the assessee engages large number of labourers who are controlled and supervised by number of teams headed by senior, efficient and trusted workers. These labourers work at their homes and are connected to the assessee through the leaders of the team. The assessee received payments from different saree shopskeepers after deduction of taxes at source u/s. 194C from the payments made to him. The basic material, clothes are supplied by the shopkeepers and the other accessories being stitching materials and articles are supplied by the assessee himself. During the year under appeal, the assessee debited an amount of Rs.2,70,42,450/- as labour charges in his account. However, no tax had been deducted at source from such payment of labour charges. The A.O. required the assessee to explain as to why TDS was not deducted from such labour charges. In response, the assessee submitted that the none of the labour parties was either contractor or sub-contractor. The assessee made payments of labour charges to the labourers and also the prices of the materials and since the labourers were not the contractors or sub-contractors of the assessee, there was no question of deducting any tax at source u/s. 194C of the Act from the said payments made by the

assessee. There was no contract between the assessee and the labourers or even with the leaders. The leaders also did not work for supplying labourers to the assessee. They only coordinated and supervised the work. Therefore, provisions of Sec. 194C were not attracted in the given circumstances and the assessee has rightly not deducted tax at source from the labour payments made to the labourers. The A.O. was not convinced with the said explanation of the assessee. He held that the nature of payments are of job charges or in a way payments to sub-contractors for executing the job works for the assessee, which attract the provisions of Sec. 194C. As the assessee did not deduct TDS from such payments of labour charges, provisions of Sec. 194C were clearly applicable to the case of the assessee. In that view of the matter, the A.O. made disallowance of the labour charges to the extent of Rs.2,70,42,450/- u/s. 40(a)(ia) of the Act and added the same to the assessee's total income.

3. On appeal, the C.I.T.(A) upheld the action of the A.O. in disallowing labour payment u/s. 40(a)(ia) with the following discussions/observations :-

"(4.2) I have considered the submission made by the appellant and have gone through the other details and documents filed before me. During the relevant previous year, the appellant has acted as a contractor and has taken the job work of embroidery and zari work etc. on the sarees supplied to him by the contractees. The appellant has received an amount of Rs.2,97,41,168/- on account of job work charges on which the tax was deducted at source by the respective contractees. The appellant himself has not completed the said contractual job work by employing his own labour and karigars at his factory/business premises. In order to execute the contract/job work received by the appellant, he has given the said work to various persons/karigars, having expertise in doing the embroidery etc. During the course of assessment proceedings it was observed by the A.O. that the appellant has paid amount of Rs.2,70,42,450/- to 77 persons for the purpose of completion of job received by him from the contractees. It was also observed by the A.O. that in all the 77 cases, the payment on account of labour charges was exceeding Rs.50,000/- to each person. However, while making the payment on account of labour charges, the appellant has not deducted the tax as per the provisions of section 194C(2) of Income Tax Act. Before the A.O. it was contended by the appellant that he is in the business of embroidery and stitching. He procured orders from different shops, famous for the business of zari sarees. He has got his own labour though temporary, but they are becoming part and parcel of his business. It was submitted that there is no contract of lump sum value and number. The workers are paid at differential piece rate as per design etc. Each and every worker directly linked with the assessee. The selection of supervisor worker is not only essential but also inevitable. Every saree requires meticulous observations witch are infested with huge knitting manifestation where supervisory plays most critical role in the industry. It was further reiterated by the appellant before the A.O. that he has no contractual term of supply and rate and he pays the wages only in piece rate, individually. During the course of appellate proceedings also, the appellant has made similar argument contending that there was never any formal contract between the appellant and such craftsman/artisans. It was argued by the AR that the AO has not considered the actual position judiciously but has proceeded on a biased view. He has made his opinion on the basis payment to a paicu1ar person without considering the amount received by particular craftsman/artisans although the basic requirement of tax deduction is the existence of a contract. The requirement of section 1 94C is "payment in pursuance of a contract", the A.O. has not bought into record about the

existence of any contract between the appellant and the recipient of the labour charges.

(4.3) Thus, the main contention of the appellant is that there was no formal written contract between the appellant and the persons to execute the work. Another contention of the appellant is that though the payment has been made to the specified person termed as group leader, but the said payment was on account of a group of person working along with the said specified person. For the better understanding of the facts of the case and applicability of provision of section 194C, it is necessary to look into the provisions of section 194C(2) of the Act which read as under:

"Any person (being a contractor and not being an individual or a Hindu undivided family) responsible for paying any sum to any resident (hereafter in this section referred to as the sub-contractor) in pursuance of a contract with the subcontractor for carrying out, or for the supply of labour for carrying out, the whole or any part of the work undertaken by the contractor or for supplying whether wholly or partly any labour which the contractor has undertaken to supply shall, at the time of credit of such sum to the account of the subcontractor 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, deduct an amount equal to one per cent of such sum as income-tax on income comprised therein:

[Provided that an individual or a Hindu undivided family, whose total sales, gross receipts or turnover from the business or profession carried on by him exceed the monetary limits specified under clause (a) or clause (b) of section 44AB during the financial year immediately preceding the financial year in which such sum is credited or paid to the account of the sub-contractor, shall be liable to deduct income-tax under this sub-section."

(4.4) In the appellant's case, there is no doubt at all that he is a contractor who has taken the contract of job work of embroidery on the sarees supplied to him by the contractees. To execute the work awarded to him by the contractees he has engaged the labour through various persons to whom he has made the payment of labour charges. In terms of provisions of section 194C(2) of the Act such persons are to be treated as sub-contractors because the appellant has failed to prove that these persons were his employees. It is immaterial as to whether the appellant was having a formal written contract with them or not. An oral contract is also considered to be a contract falling within the purview of provisions of section 194C of Income-tax Act. Further in the case of appellant first proviso to section 194C(3) of the Act is applicable because in all the 77 cases of payment of labour charges, the appellant has made payment during the financial year, which exceeds Rs.50,000/-. Under the circumstances, the appellant was liable to deduct the tax u/s. 194C(2) of the Act.. It is immaterial that the payment to each person was made on behalf of various laborers working with the said sub-contractor. On perusal of ledger extract submitted by the appellant, it is observed that the payment on account of labour charges was made to 77 persons termed as group leader or supervisor and in turn they have paid the wages to various workers under them. In view of above, it is held that the provisions of section 194C(2) of the Act were applicable to the appellant and he was required to deduct the tax at source while making the payments of such labour charges. However the appellant has failed to do so.

(4.5) As per the provisions of section 40(a)(ia) of the Act, if an assessee has failed to deduct or after deduction as failed to pay the amount of tax on the amounts paid or payable to a contractor or sub-contractor, being recipient, for carrying out any work including supply of labour for carrying out any work, including supply of labour for carrying out any work, on which tax is deductible at source under chapter-XVII-B, shall not be allowed as deduction in computing income chargeable under the head "Profits and gains or business of profession". As mentioned above the appellant being a contractor has made payment of labour charges to his sub-contractors and hence he was liable to deduct the tax u/s. 1 94C(2) of the Income-tax Act. He cannot deny his responsibility of deducting the tax merely for the reason that he has made the payments to the Group leader/supervisor for the sake convenience. The appellant has failed to prove that each and every labourer/karigar/artisan were engaged by himself and they were not supplied by the so-c&jed Group leaders and supervisors. Since the appellant has failed to deduct the tax at source, the A.O. has rightly invoked the provisions of section 40(a)(ia) of the Act. In my opinion the A.O. has rightly disallowed the amount of Rs2,7O,42,45O/- u/s.40(a)(ia) of the Act. Under these circumstances, I am not inclined to interfere with the view taken by the A.O. The disallowance of Rs.2,70,42,450/- so made is confirmed."

Hence this appeal by the assessee.

4. The assessee's ld. A/R filed a written representation and also argued verbally. According to him, since the assessee merely made payments of wages (labour charges) to the labourers and also the prices of the materials and since the labourers are not contractors or sub-contractors of the assessee, there was no question of deducting any tax at source as required u/s. 194C of the Act from the said payments made by the assessee and, therefore, provisions of sec. 40(a)(ia) would not be attracted in the case of the assessee. He submitted that the A.O. himself has admitted the payments as labour charges when he wrote in the order that the assessee failed to discharge his duty to deduct and deposit on labour charges paid. He further submitted that provision of Sec. 194C(2) is not applicable to the case of the assessee, as alleged by the A.O., because as per this section, payment should be made to the sub-contractor in pursuance of a contract. In the case of the assessee neither there was any formal contract nor oral contract and the labour-heads were not sub-contractors of the assessee. The assessee engaged some labourers under supervision/leadership of senior, efficient and trusted workers for carrying out embroidery work under some arrangement. In spite of this position, the C.I.T.(A) presumed existence of alleged contract between the assessee and the labour heads from the bills charging per piece rate and the passing the work to the labour heads. In support of his submissions, the ld. A/R relied on the several decisions of High Courts and Tribunal, copies of which have also been placed in the paper book, and some of them are as below :-

a) *Mrinalini Biri Mfg. Co. Ltd. [105 CTR 327 (Cal)]*

b) *Jahangir Biri Factory Pvt. Ltd. [126 TTJ 567 (Cal)]*

c) *Samanwaya vs. ACIT [34 SOT 332 (Kol)]*

d) *Md. Hafizul Mallick [ITA No.1200/Kol/09, order dated 13.11.2009]*

The ld. A/R also pleaded that even if it is to be considered that there was some agreement and hence work contract between the assessee and the labourers and also the labour-heads regarding carrying on embroidery works etc., in any case, the labourers and the labour-heads were not the sub-contractors of the assessee and thus the provisions of Sec. 194C(2) were not at all attracted to the case of the assessee. According to him, since the assessee himself acts as a contractor of the shopkeepers, both the authorities below have been under the erroneous impression that anybody engaged by him to carry on some work on his behalf will be a sub-contractor.

5. The Ld. Departmental Representative, on the other hand, relied on the orders of the authorities below and reiterated the reasonings adopted by the ld. C.I.T.(A) in disallowing the labour payments u/s. 40(a)(ia) of the Act.

6. We have heard the parties and perused the material placed before us. According to the A.O., assessee's case falls within the purview of Sec. 194C(2) of the Act as the assessee was a contractor and if labour charges were paid by the contractor for carrying out any work including supply of labour to the sub-contractor, it required deduction of tax at source u/s. 194C(2). Facts have been given above. However, to reiterate, the assessee used to receive dress material and clothes from different shopkeepers for carrying on embroidery work etc. on these materials. The payments made by these shopkeepers to the assessee were subject to TDS. Therefore, the assessee acted as a contractor. The assessee engaged large number labourers under the supervision/control of teams headed by senioro and efficient workers and handed over those dress material and clothes to them for embroidery work and after completion of work the labour sardars/labaourers used to return back those finished materials duly embroidered to the assessee and raised bills for labour charges.

6.1. Now we look into the meaning of 'contractor' and 'sub-contractor'. From a perusal of section 194C of the Act, it is obvious that a 'contractor' for the purpose of the provisions of this section would be any person who enters into a contract with the Central or any State Government, any local authority and corporation established by or under a Central, State or Provincial Act, any company or any co-operative society for carrying out any work including the supply of labour for carrying out any work and a 'sub-contractor' would mean any person who enters into a contract with the contractor for carrying out, or for the supply of labour for carrying out, the whole or part of the work undertaken by the contractor under a contract with any of the authorities named above or for supply whether wholly or partly any labour which the contractor has undertaken to supply in terms of his contract with any of the aforesaid authorities. Hon'ble Himachal Pradesh High Court had the occasion to deal with the meaning of 'contractor' and 'sub-contractor' in terms of Sec. 194C in the case of *ITO v. Rama Nand & Co., [163 ITR 702, 704 (HP)]*. In that case, the respondent-firm purchased from the Government certain quantity of scents of timber. It was held that the respondent-firm was not a 'contractor' within the meaning of section 194C as it had not entered into any contract for carrying out any work or for supply of labour for carrying out any work with any Government, local authority, corporation, company or co-operative society. Therefore, the payments made by the respondent-firm to any person could not be treated as payments made by a 'contractor' to a 'sub-contractor' so as to attract the provision 194C(2). The relevant portion of the observation of their Lordships of Hon'ble Himachal Pradesh High Court at page 704 of the Report is, to quote, as under :-

"It is obvious from the above extracted provisions that a "contractor" for the purpose of these provisions would be any person who enters into a contract with the Central or any State Government, any local authority, any corporation established by or under a Central, State or Provincial Act, any company or any co-operative society for carrying out any work including the supply of labour for carrying out any work and a "sub-contractor" would mean any person who enters into a contract with the contractor carrying out, or for the supply of labour for carrying out, the whole or part of the work undertaken by the contractor under a contract with any of the authorities named above or for supply whether wholly or partly any labout which the contractor has undertaken to supply in terms of his contract with any of the aforesaid authorities. Now, in the instant cases, admittedly, the respondent firm had not entered into any contract for carrying out any work or for supply of labour for carrying out any work with any Government, local authority, corporation, company or co-operative society. The respondent thus not being a contractor, the payments made by this firm to any person cannot be treated as payments made by a contractor to a sub-contractor so as to attract the provisions of section 194C(2) of the Act."

[Emphasis supplied]

It is pertinent to mention here that the Department filed S.L.P. before the Hon'ble Supreme Court in the above case and their Lordships of Hon'ble Supreme Court upheld the decision of Hon'ble Himachal Pradesh High Court and thus dismissed the *S.L.P. [157 ITR (ST) 31]*. From the above, it is thus clear that there should be a relation as contractor and sub-contractor to carry out any work or for supply of labour for carrying out any work.

6.2. The C.I.T.(A) pointed out that there is no necessity for the existence of a written contract and an oral contract is equally valid. However, there is no direct evidence on record to conclusively hold that there was any written contract or even oral contract agreement between the parties. Further, it is not clear from the evidence on record whether the assessee used to get his work done through the same labour sardars in earlier or subsequent years so as to ponder over actual nature of job, whether there was any permanent arrangement or it is mere temporary arrangement between the assessee and the labour-heads. If there is existence of permanent contract between assessee and labour heads on principal to principal basis, then how the provisions of section 194C(2) are attracted.

6.3. The learned A/R has disputed the stand of the Revenue that engagement of labour-heads/sardars for embroidery work was work contract between the assessee and such labour-heads and there was a verbal/oral agreement for the contractual job as per bill raised by the assessee piece-wise. In our considered opinion, when the assessee claims that there was no existence of any contract with labourers/labour-heads for such embroidery work etc. and materials were supplied by the assessee, onus shifts upon the department to prove otherwise, more so when the Revenue claims that there was existence of contract or at least oral agreement. According to Sec. 110 of the Evidence Act, 1872 dealing with burden of proof as to ownership, when the question is whether any person is owner of anything of which he has shown to be in possession, the burden of proving that he is not the owner is on the person who affirms that he is not the owner.

6.4. Sec. 40(a)(ia) requires that unless tax is deducted according to section 194C on payment to contractors or sub-contractors, which includes supplier of labourers for carrying out any work, it will attract disallowance of expenditure. The Hon'ble Supreme Court in *Birla Cement Works v, CBDT [2001] 248 ITR 216* has laid down the conditions precedent for attracting the provisions of section 194C, namely,(i) there must be a contract between the person responsible for making payment to contractor, (ii) the contract must be for carrying out of any work, (iii) the work is to be carried through the contractor, (iv) the consideration for the contract should exceed Rs.10,000/-, i.e., the amount fixed by section 194C and (v) that the payment is made to the contractor for the work carried out by him. Therefore, section 40(a)(ia) cannot be read in isolation or to the exclusion of section 194C, In the instant case, the controversy was regarding the payments made for disbursement of labour charges to labour-heads. The assessee had specifically stated before the lower authorities that there was no contract between the assessee and the labour-heads. Whereas it is the case of the Revenue that the assessee's case falls u/s. 194C(2) of the Act. Thus, revenue claims that there was existence of sub-contract and these labour heads are sub-contractors. It is also not clear from the records whether there is any contract existed on principal-to-principal basis between assessee and labour heads. Keeping in view the totality of the facts and circumstances of the case and the submissions of the parties, we deem it proper to restore the issue of determination of existence of any contract between the assessee and the labour-heads to the file of A.O. in the light of guidelines enunciated by the Hon'ble Supreme Court in the case of Birla Cement Works (supra) as discussed above and the facts of the case. We, therefore, set aside the orders of the authorities below and restore the matter back to the file of the A.O. for the above purpose. Needless to mention, the A.O. shall provide adequate opportunity of being heard to the assessee while readjudicating the issue.

7. In the result, the appeal by the assessee is allowed for statistical purposes.

(This order is pronounced in the open Court on 17.2.2011.)