No TDS on reimbursements to directors and on traded goods supplied to client

The ITAT, Mumbai in the matter of ***Techknowledgy Interactive Partners P. Ltd. v. ITO [ITA No. 350/MUM/2009 dated January 9, 2023]*** has held that no tax is required to be deducted at source on amount reimbursed to the director of the company. Further, when tax has been deducted at source by the assessee while receiving software consultancy services, disallowance cannot be done by the Revenue Department. Further, directed the Revenue Department to verify whether the assessee was merely a trader of a software and held that, if the purchases of software is traded goods and supplied to another client and not for the use of the assessee, no tax is required to be deducted at source.

Facts:

Techknowledgy Interactive Partners P. Ltd. ("**the Appellant**") is engaged in the business of trading in software and software products.

The Appellant had filed its return of income on October 31, 2005, declaring a total income of INR 3,64,579/-. The Revenue Department ("**the Respondent**") after scrutiny assessment under Section 143(3) of the Income Tax Act, 1961 ("**the IT Act**"), passed a final assessment order dated December 20, 2007, assessing a total income of INR 19,16,750/-.

The Respondent made disallowances under Section 40(a)(ia) on account of non-deduction of tax at source on payment car hire charges which was reimbursed to the directors of the company; software consultancy charges paid to one M/s Orbit Software and software consultancy charges paid to one M/s Springfield Organics. The Appellant preferred an appeal, however, the Appellate Authority also confirmed the order of the Respondent vide order dated September 29, 2008 ("**the Impugned Order**").

Being aggrieved, this appeal has been filed.

Flat no. 34B, Ground Floor, Pocket -1, Mayur Vihar, Phase –I, Delhi - 110091
Email: bimaljain@a2ztaxcorp.com; Web: www.a2ztaxcorp.com; Tel: +91 11 4242 7056

The Appellant contended that it had made tax deduction at source on the payment made to M/s Orbit Software and despite that, the Respondent disallowed the deduction holding that tax deduction was not made at source. Further, payment to M/s Springfield Organics was made for purchasing a software, which the appellant further supplied to one of its clients and softwares developed specifically for a client is held to be goods and sales tax was to be levied and hence, no tax was required to be deducted at source. Further, the provision of Section 40(a)(ia) of the IT Act is not applicable on reimbursement the payments made by the directors of the company as car hire charges.

Issue:

Whether the Respondent was right in passing the Impugned Order disallowing deductions as sought by the Appellant?

Held:

The ITAT, Mumbai in ***ITA No. 350/MUM/2009*** held as under:

- Held that, tax is not required to the deducted at source from payments made in the nature of reimbursements to the directors of the company towards car hire charges and therefore the addition was required to be deleted.
- Observed that, the Appellant had already deducted tax at source on the sum paid to M/s Orbit Software and it was also recorded in the Impugned Order.
- Held that, as tax was already deducted at source by the Appellant, there was no reason for the Respondent to disallow the deduction.
- Further held that, if the software purchased by the Appellant from M/s Springfield Organics was a traded good, to be further supplied to one of its clients and not to be used by the Appellant, it was not subject to tax deduction at source.
- Directed the Respondent to verify if the software purchased by the Appellant from M/s Springfield Organics were traded goods.

Relevant Provisions:

Section 143(3) of the Income Tax Act, 1961:

"On the day specified in the notice issued under sub-section (2), or as soon afterwards as may be, after hearing such evidence as the assessee may produce and such other evidence as the Assessing Officer may require on specified points, and after taking into account all relevant material which he has gathered, the Assessing Officer shall, by an order in writing, make an assessment of the total income or loss of the assessee, and determine the sum payable by him or refund of any amount due to him on the basis of such assessment:"

Section 40(a)(ia) of the IT Act:

"40. Amounts not deductible.–

Notwithstanding anything to the contrary in sections 30 to 38, the following amounts shall not be deducted in computing the income chargeable under the head "Profits and gains of business or profession",-

(a) in the case of any assessee-

…

(ia) thirty percent. of any sum payable to a resident, on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction, has not been paid on or before the due date specified in sub-section (1) of section 139,-

Provided that where in respect of any such sum, tax has been deducted in any subsequent year, or has been deducted during the previous year but paid after the due date specified in subsection (1) of section 139, thirty per cent. of such

sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.

Provided further that where an assessee fails to deduct the whole or any part of the tax in accordance with the provisions of Chapter XVII-B on any such sum but is not deemed to be an assessee in default under the first proviso to sub-section (1) of section 201, then, for the purpose of this sub-clause, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the payee referred to in the said proviso.

Explanation.-For the purposes of this sub-clause,-

(i) "commission or brokerage" shall have the same meaning as in clause (i) of the Explanation to section 194H;

(ii) "fees for technical services" shall have the same meaning as in Explanation2 to clause (vii) of sub-section (1) of section 9;

(iii) "professional services" shall have the same meaning as in clause (a) of the Explanation to section 194J;

(iv) "work" shall have the same meaning as in Explanation III to section 194C;

(v) "rent" shall have the same meaning as in clause (i) to the Explanation to section 194-I;

(vi) "royalty" shall have the same meaning as in Explanation 2 to clause (vi) of sub-section (1) of section 9;"

(Author can be reached at info@a2ztaxcorp.com)

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