

Higher rate of TDS on payments made to Non – filers of Income Tax Returns

Introduction

The concept of tax deductible at source (TDS) was introduced with an aim to collect taxes at the time of generation of income. A person (deductor) who is liable to make payment of specified nature to any other person (deductee) shall deduct tax at source and remit the same into the account of the Central Government as per the prescribed rates of tax. The deductee would be entitled to claim the credit of the tax so deducted by the deductor on the basis of TDS certificate issued by the deductor.

In order to encourage people to file their income tax returns, a new provision under section 206AB of the Income Tax Act, 1961 is made applicable with effect from 01/07/2021, based on which deductors may have to deduct TDS at higher rate in case the deductee has not filed the Income Tax returns for 2 years and subject to other conditions.

Overview of section 206AB

A. Applicability of provisions of section 206AB:

Sections where applicability of section 206AB is **Not Required**

- Section 192: TDS on Salary
- Section 192A: TDS on withdrawal from EPF
- Section 194B: TDS on winning from lotteries, crossword puzzles, etc
- Section 194BB: TDS on winning from racehorses
- Section 194LBC: TDS on income in respect of investment in Securitization Trust
- Section 194N: TDS on cash withdrawal

Sections where applicability of section 206AB is **Required**

- Section 193: Interest on securities
- Section 194: Dividend Income
- Section 194A: Interest other than interest on securities
- Section 194C: Payment to contractors
- Section 194H: Commission or brokerage
- Section 194I : Rent
- All other TDS sections i.e 194DA, 194EE, 194F, 194G, 194J, 194K, 194M, 194O, 194Q, 194P, 194IA, 194IB, 194IC, etc.

B. Applicable on payments to be made to specified persons:

“A person who has not filed the returns of income for both of the two assessment years relevant to the two previous years immediately prior to the previous year in which tax is required to be deducted, for which the time limit of filing return of income under sub-section (1) of section 139 has expired; and the aggregate of tax deducted at source and tax collected at source in his case is rupees fifty thousand or more in each of these two previous years:

Provided that the specified person shall not include a non-resident who does not have a permanent establishment in India.”

Therefore, all the following conditions must be satisfied in order to term the deductee as a specified person:

- a. Deductee has not filed the return of income for both of the two assessment years relevant to the previous years immediately before the previous year in which tax is required to be deducted;

AND

- b. The due date to file such return of income, as prescribed under Section 139(1), has expired;

AND

- c. The aggregate amount of tax deducted and collected at source is Rs.50,000/- or more in his case in each of these two previous years.

C. Rate of TDS if payment is made to specified person:

In cases where section 206AB is applicable and payment is to be made to a specified person, then TDS needs to be deducted at a higher of the following rate:

- a. Twice the rate specified in the relevant provision
- b. Twice the rate or rates in force
- c. At rate of 5%

- D. In case where the specified person has not provided his PAN to the deductor, then TDS shall be deducted at a rate higher of the following:
- a. Rates provided in this section, or
 - b. At the rate of 20%.

Ambiguity in the term “in his case” for specified person

The third condition of specified person provides that the aggregate TDS and TCS in his case has to be greater than Rs.50,000/- in each of the two previous years. The moot question here is the meaning of the term “in his case” because there are two views possible as under;

1) Aggregate amount of Tax deducted and Tax collected at source by the deductor himself against payment to the payee

AND

2) Aggregate amount of Tax deducted and Tax collected at source by all the parties against payments to the payee

View 1 seems more logical as it is not possible for the deductor to check the total amount of Tax Deducted and Tax Collected by all the parties against the payee for both the years. Form 26AS of the payee must contain the details of aggregate TDS and TCS, however it being a confidential data, the deductor cannot enforce the payee to provide the copies of Form 26AS.

Does person not liable to file ITR fall in the category of specified persons

The term Specified person is defined as a “person who has not filed return of income for both the assessment years.....” The intent of the new provisions is that high rate of TDS should be applicable on payments made to the non-filers of Income-tax return as evident from the memorandum as well as the nomenclature of the section. However, from the plain reading of the section, even a person not liable to file return of income may fall under the meaning of specified person and thus even if the deductee was not required to file the return of income for the 2 assessment years, the deductor may end up deducting TDS at a higher rate if other conditions are satisfied.

Practical challenges

The first condition which the deductors have to check is whether the deductee has filed income tax return for the previous two assessment years. Thus, in order to ensure that the deductee has filed the income tax returns, deductor will need an ITR acknowledgement of the deductee. What if the deductee refuses to share the ITR acknowledgement on the basis of principle of confidentiality? Whether a declaration given by the deductee that he has filed the return of income be considered as a sufficient document for the deductor to conclude that deductee has duly filed the return of income? An option for status of the ITR filed by an assessee under the Income Tax portal is available, however the portal does not mention the Assessment Year and hence how does one ensure that the acknowledgement number provided is for the specified year or not?

The Income Tax Twitter handle has stated that a 'Compliance Check Utility' will be made available to the deductors on the Income Tax Portal for determining applicability of section 206AB. Once the compliance check function is made active, the deductors would be in a better position to analyse whether provision of section 206AB is applicable while deducting TDS or not.

Due dates of filing ROI u/s 139 get expired in middle of the year and different due dates for various assessee's

Going by the plain reading of the provisions, it seems that deductor will also have to check whether the due date for filing original return of income u/s 139(1) for the immediately preceding year has expired or not because in the initial months of the year, due date for filing return of income u/s 139(1) for the immediately preceding year would not have expired, however at a later stage the due date u/s 139(1) for the immediately preceding year would expire.

For instance, if a deductor has to deduct TDS on 01/01/2022, then the relevant two assessment years would be A.Y 2021-22 and A.Y 2020-21. Whereas, if the deductor had to deduct TDS on 15/07/2021, then the relevant two assessment years would be A.Y 2020-21 and A.Y 2019-20. Finding the due date for filing return of income u/s 139(1) in case of the deductee could well be a daunting task to the deductors as there are various due dates prescribed u/s 139(1) for different types of assessee's.

Illustration for “both the assessment year”

The below illustration is based upon the due dates applicable as on date for filing return of income u/s 139(1) for the A.Y 2021-22.

Sr. No	TDS is required to be deducted on	2 relevant years for examining conditions of section 206AB		Remarks
1	05/07/2021	A.Y.2020-21	A.Y.2019-20	Assuming the deductee is an Individual/HUF/Firm/partner in a firm not subject to audit.
2	05/10/2021	A.Y.2021-22	A.Y.2020-21	
3	05/10/2021	A.Y.2020-21	A.Y.2019-20	Assuming the deductee is a Company/Firm/HUF/Partner in a firm whose books of accounts are subject to audit.
4	05/12/2021	A.Y.2021-22	A.Y.2020-21	

However, one may interpret that for the entire year, two assessment years relevant as on the first day of the relevant year in which TDS is to be deducted has to be considered for the entire year i.e., irrespective of the date of deduction of TDS, the relevant two assessment years for the taxes to be deducted at source (under this provision) for the period 01/07/2021 to 31/03/2022 would be A.Y 2019-20 and A.Y 2020-21.

Examples

Below are few examples for better understanding of the above discussed provisions:

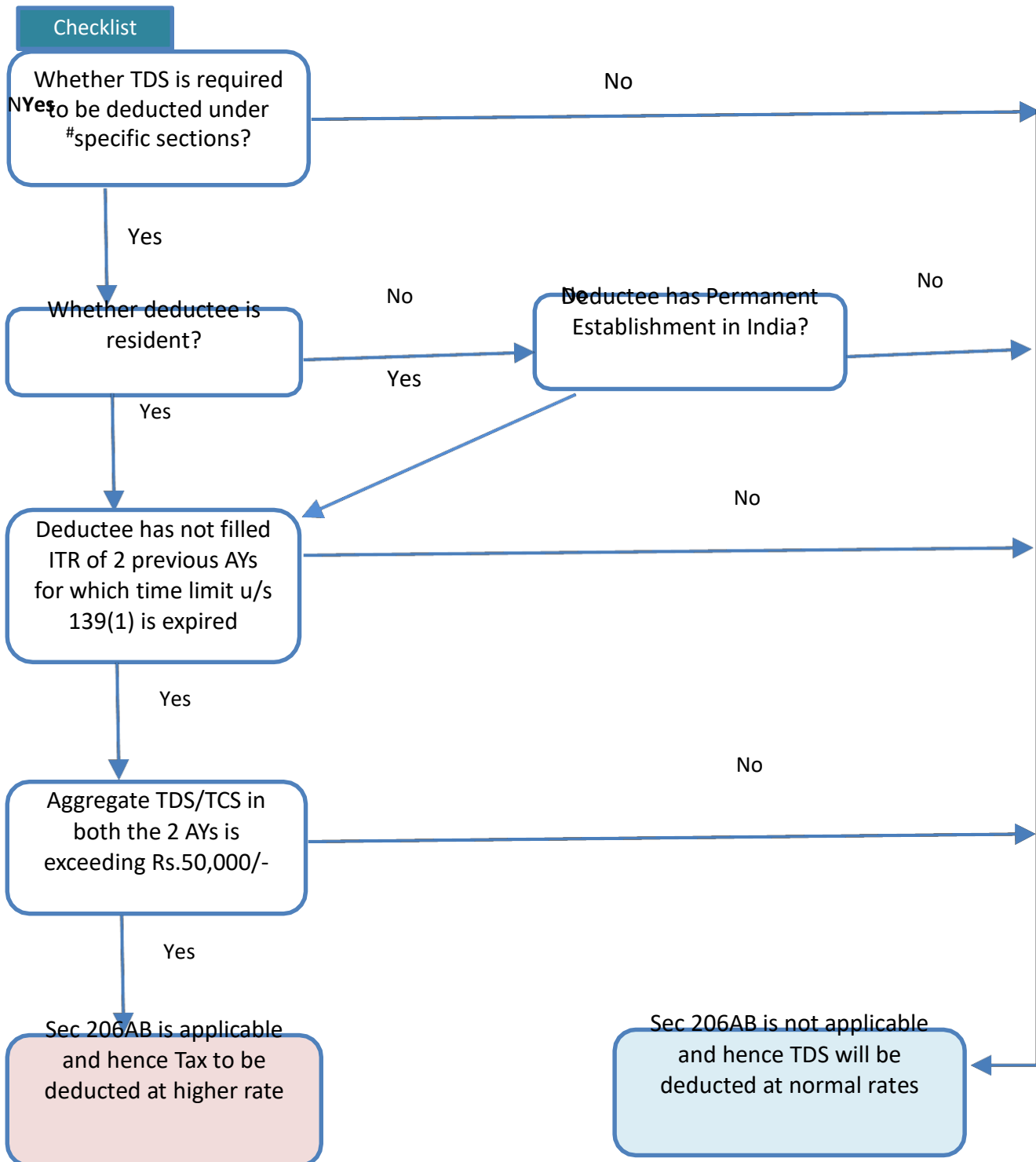
1. Chris provided professional services worth Rs.10,00,000/- to ABC Ltd on 20/05/2021. Chris informs ABC Ltd that he has not filed return of income for the A.Y 2019-20 but has filed return of income for the A.Y 2020-21. From the records of ABC Ltd, amount of TDS deducted in the A.Y 2019-20 and A.Y 2020-21 is Rs.55,000/- in each year. Whether ABC Ltd is required to deduct TDS at higher rates as prescribed u/s 206AB?
 - The provisions of section 206AB of the IT Act are applicable with effect from 01/07/2021 and hence there is no need to check for any of the conditions laid down in the new provisions and accordingly there is no question of deducting TDS at higher rates.
2. What if the date of service in the above example is 10/07/2021 instead of 20/05/2021?
 - One of the condition for a person to fall under the meaning of specified person is that he should not have filed the income tax return for both the assessment year preceding the year in which payment is to be made. Here, although Chris has not filed the income tax return for the A.Y 2019-20, but has filed the income tax return for the A.Y 2020-21 and therefore ABC Ltd is not required to deduct tax at higher rates as prescribed under section 206AB.
3. United Ltd is likely to pay a rent of Rs.2,25,000/- to Mr Evra for the period July 2021 to March 2022. Total TDS deducted by United Ltd in the preceding two years is Rs.60,000/- each. Mr Evra informs United Ltd that he has not filed the return of income in any of the previous years. Whether United Ltd requires to deduct TDS at a higher rate as prescribed u/s 206AB while making payment to Mr Evra?
 - The total amount of rent payable for the entire year 2021-22 is below threshold limit as prescribed under section 194-I of the Income Tax Act, 1961 and hence no TDS is required to be deducted while making payment by United Ltd to Mr Evra, irrespective of the fact that Mr Evra falls under the category of specified person.

4. DEF Ltd has to pay a sum of Rs.1,25,000/- to Mr Ron on account of professional services. Mr Ron has not filed his return of income for the two previous years as he was not required to file the return of income. DEF Ltd has deducted TDS in the earlier two years in excess of Rs.50,000/-. Whether DEF Ltd requires to deduct TDS at a higher rate as prescribed u/s 206AB while making payment to Mr Ron?
- Going by the strict wordings of the Income Tax Act, 1961, as Mr Ron has not filed the return of income for the two years, he may be treated as a specified person and accordingly DEF Ltd may have to deduct TDS at higher rate as prescribed u/s 206AB while making payment to Mr Ron.
 - Alternate view is also possible that as Mr Ron was not liable to file his return of income for the preceding 2 years, provisions of section 206AB are not applicable as the intention of the legislature was to catch non-filers of income tax return and not the persons who are not required to file the return of income.
5. Abhishek Ltd has to pay an interest of Rs.5,00,000/- to Mrs Kavita on 31/07/2021. Abhishek Ltd is informed that Mrs Kavita has not filed her income tax return for the A.Y 2019-20 and A.Y 2020-21. Aggregate TDS/TCS deducted/collected of Mrs Kavita in the A.Y 2019-20 was Rs.51,000/- and A.Y 2020-21 was Rs.46,500/-. Whether Abhishek Ltd is required to deduct TDS at the higher rate as prescribed under section 206AB?
- One of the condition is that the aggregate TDS in the case of the deductee has to exceed Rs.50,000/- in each of the two previous years. Here, in the A.Y 2020-21, aggregate Tds deducted by Abhishek Ltd against payment made to Mrs Kavita is below Rs.50,000/- and hence Abhishek Ltd should not be required to deduct higher rate of TDS as prescribed u/s 206AB.

6. MU Ltd is likely to deduct TDS while making payment to a Non Resident of India, Mr Bruno on 31/07/2021 on account of professional services. Mr Bruno has a permanent establishment in Mumbai and has not filed the return of income for the A.Y 2019-20 and A.Y 2020-21. Aggregate TDS deducted of Mr Bruno in the A.Y 2019-20 and A.Y 2020-21 is Rs.55,000/- and Rs.61,000/- respectively. Whether MU Ltd is required to deduct TDS at a higher rate as prescribed u/s 206AB?

- Provisions of section 206AB are not applicable to a Non-resident of India, who do not have a permanent establishment in India. Here in the given case, Mr Bruno has a permanent establishment in India and hence the provisions of section 206AB would be applicable. Mr Bruno has not filed the return of income for the previous two assessment years and the aggregate TDS deducted by MU Ltd is above Rs.50,000/- in both the years and hence MU Ltd TDS will have to deduct at a higher rate as prescribed u/s 206AB.

Flowchart for applicability of higher rate of TDS



#Section other than section 192/192A/194B/194BB/194LBC/194N

Consequences of deduction at a lower rate

If the deductor has deducted taxes in accordance with the provisions of relevant section viz., 194, 194A, 194C, 194J, 194-I, etc and if it is held that the deductor under the circumstances was required to deduct TDS at the rates prescribed under section 206AB of the Income Tax Act, 1961, then:

- a. Assessee-in-default proceeding can be initiated against the deductor (payer) and shortfall amount of tax can be recovered from the deductor along with interest.
- b. Penalty proceeding can also be initiated for failure to comply with TDS provisions.

The deductor can avoid assessee-in-default proceedings if;

1. Payee/deductee is a resident and has filed return of income for the relevant year AND
2. Payee has taken into account such sum for computing income in the return AND
3. Payee has paid the tax due on the said income AND
4. Presents Form 26A from a Chartered Accountant.

Similar amendment for TCS at higher rate if payment received from specified persons

E. Section 206CCA:

- a. A similar Section 206CCA has been inserted to provide that the collector shall collect tax at a higher rate if the collectee is a specified person. The collector shall collect tax under this provision at the higher of the following rates:
 - i. Twice the rate specified in the relevant provision of the Act; or
 - ii. At a rate of 5%.
- b. If the collectee has neither furnishes PAN or Return of income , then the collector shall collect tax at rates
 - i. Provided in this section or
 - ii. At the rate of 5%, whichever is higher.

Comments

Although all transactions may not get covered under this new provision, but the onus is on the deductor to ensure that they properly comply with the provisions as every transaction wherein deduction of TDS is required, has to be passed through this test of non-filer of ITRs and deductor is responsible to check whether the deductee falls under the category of specified person or not. To discourage non-filers of the Income Tax Returns, a higher rate of TDS/TCS is made applicable with shouldering responsibility on the deductors, who cannot afford to put a foot wrong while complying with the provisions given the fact that non-compliance may lead to severe consequences.

There are number of uncertainties with reference to the meaning of the term “in his case” and whether or not the deductor has to consider the immediately preceding year after the period of filing return of income u/s 139(1) for that immediate preceding year gets expired. Thus, guidelines or FAQs from the CBDT can clear the doubts in the minds of the deductors and may also lead to a welcome step towards bringing uniformity.

10 June 2021

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