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Delay in Deposit of TDS: Prosecute if you can't Penalise?



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Introduction:

Tax Deducted at Source (TDS) is a crucial component of the Indian tax system, ensuring timely collection of taxes and reporting of taxable transactions. Non-compliance with TDS obligations can have serious ramifications, including prosecution, as stipulated under Section [276B](#) of the Income Tax Act, 1961 ("**Act**"). However, recent developments, such as the Supreme Court's ruling in the case of **US Technologies International (P.) Ltd. v. CIT** [[2023](#)] [149 taxmann.com 144/293 Taxman 27/453 ITR 644](#), have shed light on a perplexing aspect: while penalty cannot be imposed for delay in deposit of TDS under Section 271C of the Act, prosecution may be launched under Section 276B of the Act. In this article, we explore this dichotomy and the implications it has on taxpayers.

The Supreme Court's Ruling and the Absence of Penal Consequences?:

In the case of **US Technologies International (P.) Ltd.** (*supra*), the Supreme Court ruled that on mere belated remitting of the TDS after deducting the same by the concerned person / assessee, no penalty shall be leviable under [Section 271C](#) of the Act. This is due to the specific language of Section 271C which only covers failure to deduct tax and does not cover situation of belated deposit of tax, unlike the language in Section 201 of the Act which deals with levy of interest that covers both the situations. This landmark decision has created a significant paradox within the tax framework. On one hand, the law prescribes prosecution for delayed deposit of TDS under Section 276B of the Act. On the other hand, the absence of any penalty for such delays raises questions regarding the effectiveness and fairness of the legislation.

Interestingly, there is another penalty provision under the Act that lays down penal consequences if the taxpayer is treated as the assessee in default as defined under Section 201 of the Act; however, this provision was not discussed in the judgment of **US Technologies International (P.) Ltd's** case (*supra*). As per Section [221](#) of the Act, if the taxpayer fails to deduct or pay the tax in accordance with the provisions of the Act, the taxpayer shall be treated as an assessee in default and shall be liable to a penalty not exceeding the amount of tax in arrears.

Rationale behind insertion of Section 271C under the Act:

The Direct-tax Amendment Act, 1987 introduced Section [271C](#) in the statute with effect from 01.04.1987. The CBDT through Circular No. 551 dated 23.01.1990, explained the intent behind the introduction of Section 271C by stating that under the old provisions of the Act, no penalty was provided for failure to deduct tax at source and that the said default only attracted prosecution under Section 276B. Thus, it was decided that the default relating to failure to deduct the tax at source should be made liable to levy of penalty, while the default relating to failure to pay the tax deducted to the Government, which is a more serious offence, should continue to attract prosecution.

However, it is pertinent to note that prior to the introduction of this specific penal provision, a general penal provision under Section 221 of the Act was already in existence. Consequently, the co-existence of both provisions – one governing failure to deduct TDS and the other covering both failure to deduct and belated deposit of TDS – poses a challenge within the framework of the Indian tax system. Therefore, this dichotomy between prosecution and the introduction of specific penal provision under Section 271C of the Act for failure to deduct TDS creates a legal conundrum.

The Draconian Nature of the Law:

Section 276B of the Act, in its current form, can be deemed draconian. The true interpretation of this provision should acknowledge that the tax department already collects interest under Section 201(1A) of the Act for delayed deposit of TDS and can also levy the penalty under Section 221 of the Act. With interest being levied and recovered in addition to the penal consequences under Section 221 of the Act, the launching of a prosecution seems excessive and inequitable. There have been instances where the tax authorities have initiated criminal proceedings for even a meagre amount with a delay of a few days. In the case of **Asstt. CIT v. At Dev Prabha (TV)** [\[2023\] 150 taxmann.com 275/454 ITR 59 \(SC\)](#), SLP preferred by the Revenue against the High Court's order was dismissed by the Supreme Court, affirming the view of the High Court that where the amount of TDS deducted was not more than Rs. 50,000 and the TDS amount was deposited with interest prior to the initiation of criminal proceedings, such proceedings were liable to be quashed.

Considering this hardship faced by the taxpayers, the Central Board of Direct Taxes ("**CBDT**") has issued various notifications and circulars to facilitate ease of doing business and decriminalisation of offence. As per the latest circular (Circular No. 24/2019, dated 09.09.2019), CBDT has given instruction that "*cases where non-payment of TDS is ? 25 Lakhs or below, and the delay in deposit is less than 60 days from the due date, the same shall not be processed for prosecution in normal circumstances. In exceptional cases like, habitual defaulters, based on particular facts and circumstances of each case, prosecution may be initiated only with the previous administrative approval of the concerned authority.*"

The Elusive Relief for Reasonable Cause and Compounding of Offences:

Section [278AA](#) of the Act does provide relief from prosecution for belated TDS deposit if a reasonable cause can be demonstrated. However, the tax authorities hold discretionary powers in accepting pleas of reasonable cause. The Patna High Court in the case of **Sonali Autos (P.) Ltd. v. State of Bihar** [\[2017\] 84 taxmann.com 286/396 ITR 636](#), decided against the Income Tax Department and held that the oversight on the part of the accountant could be termed as reasonable cause. This has led to concerns about the effectiveness and fairness of this provision of establishing "*reasonable cause*".

Further, in case prosecution is launched against the principal officers of a Company, they can take the defence as provided under Section [278B](#) of the Act that the offence was committed without their consent or connivance or is not attributable to any neglect on their part.

Another relief from such prosecution is resort to Section [279\(2\)](#) of the Act which provides that any offence under the Chapter, either before or after institution of proceedings, may be compounded by the competent authority as specified in the provision. The revised guidelines (F.No.285/08/2014-IT(Inv.V)/196] on compounding of offences were issued by CBDT dated 16.09.2022 wherein the offences may be compounded by the competent authority on satisfaction of eligibility conditions such as conduct of person, magnitude of offence and facts and circumstances of each case. However, the compounding process is cumbersome and lengthy which is further subject to discretion of the authorities, and not considered a matter of right as per the CBDT guidelines. Nonetheless, the CBDT, through its Press Release dated 17.09.2022, has stated that the revised guidelines aim to curtail the discretionary powers of the competent authority, while concurrently streamlining and simplifying procedural complexities.

Conclusion:

The looming of prosecution for belated deposit of TDS, despite the collection of interest and imposition of penalty under Section [221](#) of the Act, raises questions about the proportionality of the punishment. Further, the recent Supreme Court ruling in the *US Technologies International (P.) Ltd.'s* case (*supra*) has highlighted the need for a comprehensive review of the relevant provisions. Striking a balance between compliance and stringency is key to fostering a fair and effective tax system that encourages voluntary compliance while considering the practical challenges faced by taxpayers.