

BE READY TO DEDUCT TAX AT SOURCE ON PAYMENTS MADE IN THE NATURE OF BUSINESS/SALES PROMOTION

Introducing TDS under Section 194R

The provisions of the new section will come into effect from **1st July 2022**.

Section 194R: A Background:

Section 28(iv) of the Income Tax Act, 1961 is an already existing provision, according to which the value of any benefit or perquisite, whether convertible in money or not, arising from business or profession shall be chargeable to income-tax under the head profit or gains from business or profession.

The government observed that in many cases, the recipients fail to report such benefits or perquisites in their return of income, leading to furnishing of incorrect particulars of income and consequent under payment of taxes.

Section 194R was introduced to combat this problem, wherein, the person providing any benefits which are taxable under section 28(iv) is responsible to deduct tax before providing such benefits/perks to the resident receiver.

This will effectively help the government in widening the tax base and also for successfully enforcing the provisions of section 28(iv).

Who should deduct tax under S.194R : Any person providing the benefit/perk

Tax should be deducted on : Value of benefit or perk arising from business or profession. (I.e. benefits taxable under section 28(iv)).

Receiver of such benefit or perk : Resident

Threshold limit : No TDS if the aggregate amount of benefits provided does not exceed Rs 20,000 in a financial year. **(CBDT has clarified that for FY 2022-23, the aggregate amount should be taken for the period 1st April, 2022 to 31st March, 2023)**

FAQ's:

1. Whether an individual or HUF should deduct tax under this section

- An individual or HUF should deduct tax if their turnover exceeds Rs. 1 crore (in case of business) or Rs. 50 Lakhs (in case of profession) in the financial year immediately preceding the financial year in which such benefit is provided.

2. What is the rate at which tax should be deducted under section 194R?

- Tax should be deducted at the rate of **10%**

3. When should the tax be deducted under this section?

- Tax should be deducted before providing the benefit to the recipient
- If the benefit is in kind or partly in cash and partly in kind, the person responsible for providing such benefit is required to ensure that the tax required to be deducted has been paid before releasing the benefit.
- **The CBDT has clarified that the provider can rely on a declaration along with a copy of the advance tax payment challan provided by the recipient as sufficient proof of depositing the required tax to the government. *The provider has to report this transaction along with the advance tax payment challan number in his 26Q for the appropriate quarter.***

4. Meaning of the term benefit or perquisite?

- The term “benefit or perquisite” has not been separately defined for the purpose of section 194R. However, it is essential that such a benefit or perk arises from business or profession of the assessee.
- There are different types of benefits or perquisites that are provided by businesses to their dealers, distributors, agents, channel partners like travel packages, gift cards/vouchers, products under incentive scheme like phones, vehicles etc.
- Freebies/benefits received by doctors from pharma companies are also taxable under this section.

5. Relevance of gifts, benefits etc provided during festivals

- In our opinion, since the benefits/gift/perks provided during special occasions like festivals do not arise as a result of carrying on business or profession, no tax needs to be deducted under section 194R.

6. Relevance of perquisites to employees

- It is clear that the provisions of section 194R will apply only on the benefits or perquisites arising in the course of business or profession.
- Since the perquisite received by an employee does not arise as a result of carrying out any business or profession by the employee, no tax needs to be deducted under section 194R on such perquisites.

Guideline issued by CBDT:

The CBDT on 16th June, 2022 has issued guidelines under 194R(2) for removal of difficulties, The extracts of the guidelines are as follows,

1. Is it necessary for the person providing the benefit to check if it is taxable in the hands of the recipient?

- No, the recipient is not required to check if the benefit is taxable in the hands of the recipient under section 28(iv).
- This means that, if the provider of the benefit satisfies the conditions given in Section 194R, he should deduct TDS under section 194R.

2. Is it necessary that the benefit or perquisite must be in kind?

- No, the provisions of section 194R will apply if the benefits are in cash or kind or partly in cash and partly in kind.

3. Whether sales discount, cash discount and rebates are benefits taxable under section 194R?

- Yes, they are considered to be benefits arising to the receiver under section 28(iv).
- However, if the same is subject to tax, the seller would be put under difficulty, to remove such difficulty, it is clarified that the **no tax** needs to be deducted under section 194R on sales discount, cash discount and rebates.

4. How is the benefit or perquisite valued?

- The benefit or perquisite is valued on **FMV (Fair market value)** basis except in the following cases,
 - i. The benefit/perk has been purchased by the provider before giving it to the recipient.
 1. In such case, the purchase price is the value of the benefit.
 - ii. The provider manufactures the benefits/perks before giving it to the recipient
 1. In such case, the price the provider charges to its other customers for such items is the value of the benefit.

Based on the above provisions and the guideline issued by CBDT, we have compiled an illustrative list of benefits for which TDS under Section 194R may or may not apply.

| S. No | Nature of Benefit | Whether a benefit taxable under section 28(iv) | Whether taxable under section 194R |
|-------|---|--|--|
| 1 | Sales discount, cash discount and rebates | Yes | No , Even though it is a benefit taxable under Section 28(iv), the CBDT has excluded sales/cash discount and rebates from taxability under section 194R owing to difficulties the sellers may face if the same is subject to tax. |

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| 2 | Sales Incentives given – in the nature of car, TV, computers, gold coin, mobile phones, watches etc | Yes | Yes |
| 3 | Sponsoring a trip of the recipient and his/her family or relatives upon achieving certain targets | Yes | Yes |
| 4 | Providing free ticket for an event | Yes | Yes |
| 5 | Medicine samples provided to doctors | Yes | Yes |
| 6 | Products given to Social media influencers to make audio/video about the product | Yes – If the product is not returned (i.e. retained) after making the video/audio. No – if the product is returned after making the video/audio. | Yes No |
| 7 | Reimbursement of out of pocket expenditure | To be decided on a case to case basis | Refer Note 1 below |
| 8 | <p>Dealer conference to educate the dealers about the products of the company</p> <ol style="list-style-type: none"> 1. Prime objective of the dealer conference is to educate the dealers about the product 2. Expense attributable to leisure trip or leisure component, even it is incidental to the dealer conference 3. Expenditure incurred for family members accompanying the dealers/customers attending the conference 4. Expenditure on account of prior stay or over stay beyond the dates of the conference | <p>No</p> <p>Yes</p> <p>Yes</p> <p>Yes</p> | <p>No</p> <p>Yes (CBDT has not clarified yet regarding how the value should be split between leisure and education activity)</p> <p>Yes</p> <p>Yes</p> |

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|----|--|---|--|
| 9 | Samples given as gift during purchase of other items (e.g. providing a sample shampoo sachet for purchase of a magazine) | Yes | Yes |
| 10 | Remission or cessation of trading liability (i.e. creditor balance written back or circumstances wherein the creditor waives the amount owed to him) | No, it is a deemed profit taxable under section 41(1) of the Income tax Act, 1961 | No |
| 11 | Amount paid to assessee in pursuance of a court settlement for breach of contract | Yes | Yes |
| 12 | Principal Loan waived by bank under one time settlement | Yes | Yes |
| 13 | Value of rent free accommodation, furniture and fixtures given to director. 1. If the director is an employee of the company (i.e. part of the employee payroll) 2. If the director provides his services in a professional capacity | No Yes | No Yes |
| 14 | Car given to a guru by his disciple who had been benefited from his preaching | Yes | Yes, taxable in the hands of the guru. |
| 15 | Shares allotted to the director of the company under an agreement with the promoters | Yes | Yes |
| 16 | Land gifted to a person for carrying out his profession | Yes | Yes |
| 17 | Car received as gift by a brand ambassador from a company. (The car is not a part of the professional contract between the company and the brand ambassador – given out of love and affection) | Yes | Yes |

Notes:

1. Taxability of out of pocket expenditure

a. **Situation: A is providing consultancy services to XYZ Ltd. A has to travel to another place to provide services to XYZ Ltd and incurs expenditure on travel and lodging for the same.**

i. **Case 1: A makes payment for the travel/foreign expenditure & receives the bill for the same in his name, which he subsequently gets reimbursed from XYZ Ltd**

- In such cases, the reimbursement received by A is a benefit accruing to him in the course of his business or profession and hence is taxable under section 194R.

ii. **Case 2: A makes payment for the travel/foreign expenditure & receives the bill for the same in the name of the company, which he subsequently gets reimbursed from XYZ Ltd.**

- In such cases, the reimbursement received by A is not a benefit arising from his business or profession and hence is not taxable under section 194R.

Our contention:

Section 28(iv) and the consequent TDS provision under section 194R is a tough nut to crack and is generally based on various interpretations of the law. It is safe to assume that the assessing officer will contest all the payments made under business/sales promotion as income under section 28(iv) and invoke the TDS provisions under section 194R. It will be the burden of the assessee to prove otherwise and hence we opine that all the business promotion expenses in the nature of gifting any movable property or other items be made after deducting TDS, if not, to maintain sufficient evidence to refute the assessing officers claim to treat it as benefit arising out of business or profession.

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