



## ERGO

*Analysing developments impacting business*

### DELAYED DEPOSIT OF TDS LEADS TO PROSECUTION.

20 September 2019

In a recent judgment [*ITO(TDS)-2(3) v/s M.S.Shah Developers Private Limited and Ors., CC No. 53/SW/2014*] (Judgment), the Hon'ble Court of Additional Chief Metropolitan Magistrate, 38<sup>th</sup> Court, Ballard Pier, Mumbai (Court) has ordered 3-months imprisonment (along with a monetary fine of INR 5,000) for the directors of M/s M.S.Shah Developers Private Limited (Company) for delayed deposit of tax deducted at source (TDS) by the Company, pertaining to Financial Year (FY) 2009-10.

#### Background

Under the Income-tax Act, 1961 (IT Act), certain payments to resident taxpayers are subject to TDS - i.e. the payer has to deduct the applicable tax at source (1<sup>st</sup> Obligation) and deposit the same with the government within stipulated timeframe (2<sup>nd</sup> Obligation). Failure to comply with these obligations is an offence and attracts penal consequences - monetary (interest, penalty, fine) as well as non-monetary (imprisonment ranging from 3 months to 7 years). However, IT Act also provides that a person would not be punished for such failure if he proves that there was 'reasonable cause' for such failure.

Where such an offence is committed by a company, IT Act provides that (i) the company would be liable to pay fine; and (ii) the director, manager, secretary or other officer of the company to whom such neglect can be attributed would be liable for prosecution. Further, in such cases of prosecution, the IT Act also contains a presumption - *though rebuttable* - as to the culpable mental state of the accused (Rebuttable Presumption).

#### Judgment

In the instant case, during FY 2009-10, the Company had made certain payments which were subject to TDS (payments to contractors, payment of rent, and payment of professional fees). Though the Company complied with the 1<sup>st</sup> Obligation (i.e. deducted the applicable tax at source amounting to INR 6.08 lakhs), it failed to comply with the 2<sup>nd</sup> Obligation (i.e. it did not deposit the taxes so deducted with the government within stipulated timeframe). Subsequently, after a delay of more than 12 months, the Company deposited the TDS amount and also paid the applicable interest, penalty.

Despite this, the tax authorities launched proceedings against the Company and its directors (together, referred as Accused) for delay in depositing the TDS amount. The tax authorities alleged that the Accused had wilfully defaulted in the 2<sup>nd</sup> Obligation without any 'reasonable cause'. In defence, the Accused had contended that (i) this

non-compliance had happened on account of the financial crisis / liquidity crunch in the Company and as the office of the Company was locked by some financial institutions, (ii) subsequently, the Company deposited entire TDS amount and paid the applicable interest and penalty.

While dealing with the Accused's defences, the Court noted that the burden was on the Accused to produce material on record to substantiate its defences, since the IT Act contains 'Rebuttable Presumption'. The Court observed that the Accused did not produce any material on record by leading oral and documentary evidence to substantiate its defence and to prove that it had 'reasonable cause' for such non-compliance. Further, the Court also held that delayed deposit of TDS does not absolve criminal liability. Consequently, the Court ruled that the Accused were guilty, and thus, ordered (i) a fine of INR 5,000 on the Company, and each of the directors, and (ii) 3-months imprisonment for each of the directors.

### Comments:

Lately, in cases of delayed deposit of TDS with the government, the instances of initiation of prosecution proceedings against the directors has been on the rise. The fact that the IT Act does not make a distinction between a complete failure to deposit the TDS with the government OR a delayed deposit of TDS with the government, the tax authorities have generally been observed to launch prosecution proceedings even in case of delayed deposit of TDS with the government.

The fact that the IT Act contains 'Rebuttable Presumption' in such type of cases puts the burden on the company / its directors to prove (by producing evidence) that (i) there was no culpable mental state concerning the offence, (ii) there was a 'reasonable cause' for the failure on their part. Resultantly, it becomes important for corporate taxpayers to be cautious in their TDS compliances to avoid any such harsh penal consequences.

It is noteworthy that considering the stringency in such punishments, with a view to ensure that minor default cases don't get selected for prosecution, recently, the government has brought out a set of guidelines ([please see our Ergo dated 13 September 2019](#)) which, *inter alia*, provides that for cases pertaining to delay in deposit of TDS amounting to INR 25 lakhs or less, (i) such cases would normally not be selected for prosecution if the delay does not exceed 60 days from the due date, and (ii) even in exceptional circumstances (like habitual offenders), prosecution may be initiated only with the prior approval of a collegium of two senior tax officers.

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