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## Deduction of tax at source from interest on securities

### **Who is responsible to deduct tax at source in the case of interest on securities**

**5.1** Under section 193, any person responsible for paying to a resident interest on securities is required to deduct income-tax at source at the rates in force on the amount of interest payable.

For this purpose, the following are treated as persons responsible for paying interest on securities.

1. In the case of interest on securities payable by the Central or a State Government, the appropriate disbursing officer is the person responsible for paying interest on securities.
2. In the case of interest on securities payable by any other person, the person responsible for paying interest is the local authority, corporation or company itself including the principal officer thereof.

### **When tax has to be deducted at source**

**5.2** Tax is to be deducted at the time of credit of such income to the account of payee or at the time of payment of interest on securities in cash or by issue of cheque or by draft or by any other mode, whichever is earlier. For this purpose, any sum credited to any account, whether called "suspense account" or "interest payable account" or by any other name, in the books of the account of the payer, is treated credit of such income to account of the payee.

**5.2-1 *Relevance of identity of deductee under TDS provisions*** - Section 190 makes it clear that the scheme of tax deduction at source is one of the methods of recovering the tax due from a person and it is notwithstanding the fact that the tax liability may only arise in a later assessment year. The tax liability is obviously in the hands of the person who earns the income, and tax deduction at source mechanism provides for method to recover such tax liability. Therefore, this tax deduction at source liability is a sort of substitutionary liability. Section 191 further makes this position clear when it lays down that in a situation TDS mechanism is not provided for a particular type of income or when the taxes have not been deducted at source in accordance with the provisions of Chapter XVII, income-tax shall be payable by the assessee directly. This provision, thus,

shows that tax deduction liability is a vicarious liability and the principal liability is of the person who is taxable in respect of such income. Section 199 makes it even more clear by laying down that the credit for taxes deducted at source can only be given to the person from whose income the taxes are so deducted. Therefore, when tax deductor cannot ascertain beneficiaries of a credit, the tax deduction mechanism cannot be put into service. Section 202 lays down that tax deduction at source provisions are without any prejudice to any other mode of recovery from the assessee, which again points out to the tax deduction liability being vicarious liability in nature. Section 203(1) then lays down that for all tax deductions at source, the tax deductor has to 'furnish to the person to whose account such credit is given or to whom such payment is made or the cheque or warrant is issued' which presupposes that at the stage of tax deduction the tax deductor knows the name of person to whom the credit is to be given, though whether by way of credit to the account of such person or by way of credit to some other account. This again shows that tax deduction at source liability is a vicarious liability to pay tax on behalf of the person who is to be beneficiary of the payment or credit, with a corresponding right to recover such tax payable from the person to whom credit is afforded or payment is made. Thus, the whole scheme of tax deduction at source proceeds on the assumption that the person whose liability is to pay an income knows the identity of the beneficiary or the recipient of the income. It is a *sine qua non* for a vicarious tax deduction liability that there has to be a principal tax liability in respect of the relevant income first, and a principal tax liability can come into existence when it can be ascertained as to who will receive or earn that income because the tax is on the income and in the hands of the person who earns that income. Therefore, tax deduction at source mechanism cannot be put into practice until identity of the person in whose hands it is includible as income can be ascertained.

*Transfer to interest payable account - When payees are not identifiable* - It is indeed correct that *Explanation* to section 193 lays down that even when an income is credited to any account in the books of account of the person liable to pay such income, such crediting shall be deemed to be credit of such income to the account of the payee and the provisions of this section shall apply accordingly, but the fact that the credit to any account is to be deemed to be credit to the payee's account also presupposes that identity of the payee can be ascertained. Therefore, this deeming fiction can only be activated when the identity of the payee can be ascertained. Therefore, the *Explanation* to section 193 cannot be invoked in a case where the person who is to receive the interest cannot be identified at the stage at which the provision for interest accrued but not due is made. This position is also accepted by the CBDT in its letter dated July 5,

1996 addressed to the Tata Iron & Steel Co. Ltd. [Letter No. 275/126/96 IT(B)]. In the instant case, the regular return bonds being transferable on simple endorsement and delivery and the relevant registration date being a date subsequent to the closure of books of account, the assessee could not have ascertained the payees at the point of time when the provision for 'interest accrued but not due' was made. Accordingly, no tax was required to be deducted at source in respect of the provision for interest payable made by the assessee which reflected provision for 'interest accrued but not due' in a situation where the ultimate recipient of such 'interest accrued but not due' could not have been ascertained at the point of time when the provision was made - *Industrial Development Bank of India v. ITO* [2006] 10 SOT 497 (Mum.). Similar ruling is given by the Delhi Tribunal in the case of *Apollo Tyres Ltd. v. DCIT* [2017] 78 taxmann.com 195.

**5.2-2 Private arrangement of paying interest on securities as tax-free cannot discharge obligation under section 193** - Liability to deduct tax at source from interest on securities is absolute and it cannot be discharged merely because, under a private arrangement, the person who has issued securities has undertaken to pay interest free of tax.

#### **How to compute tax deduction at source**

**5.3** Tax is to be deducted under section 193 only on that income which is chargeable as "interest on securities" in the hands of recipients. If, therefore, a particular income is not taxable as interest on securities, tax is not deductible under section 193 [for a detailed discussion, see **Chapter 6**].

#### **Tax deduction account number**

**5.4** See para 1.4.

#### **Deposit of tax to the credit of the Central Government**

**5.5** Tax deducted at source is to be deposited to the credit of Central Government as follows :

**5.5-1 Where to deposit** - See para 1.5-1.

**5.5-1a e-Payment of tax** - After March 31, 2008, all corporate assesseees and other assesseees (who are subject to compulsory audit under section 44AB) will have to make electronic payment of tax through internet banking facility offered by authorized banks (irrespective of the assessment year or the financial year for which the payment of tax has to be made). Alternatively, these taxpayers can make electronic payment of tax through internet by way of credit or debit cards. For detailed discussion, see **para 1.5-1a**.

**5.5-2 Time of deposit of TDS/TCS** - After the substitution of Rules 30 and 37CA by the Income-tax (Sixth Amendment) Rules, 2010 (hereinafter referred to as Amending Rule), tax deducted/collected by a person shall be deposited to Government account as follows —

<i>Different situations</i>	<i>Time of deposit‡ of TDS/TCS</i>	
	<i>Time of deposit of TDS</i>	<i>Time of deposit of TCS</i>
1. Tax is deducted/collected by an office of the Government and tax is paid without production of an income-tax challan	On the same day on which tax is deducted	On the same day on which tax is collected
2. Tax is deducted/collected by an office of the Government and tax is accompanied by an income-tax challan	On or before 7 days from the end of the month in which tax is deducted	On or before 7 days from the end of the month in which tax is collected
3. Tax is deducted/collected by a person (not being an office of the Government)	<p>➤ <i>Where income or amount is paid or credited in the month of March</i> : Tax should be deposited by April 30</p> <p>➤ <i>Where income or amount is paid or credited before March 1</i> : Tax should be deposited within 7 days from the end of the month in which tax is deducted</p>	Within one week from the last day of the month in which tax is collected

**5.5-3 Challans for payment** - The tax deducted at source is required to be deposited on appropriate challan (ITNS 281).

**5.5-3a** *When tax is deducted/collected by a Government office and paid without production of a challan - See para 1.5-3a.*

**5.5-4 Claim for refund** - A claim for refund for TDS paid to the credit of the Central Government under Chapter XVII-B shall be furnished by the deductor in Form No. 26B electronically under digital signature.

**Issue of certificate for tax deduction from interest on securities**

**5.6** Every person deducting tax from interest on securities is required to issue quarterly certificate in Form No. 16A to the security holder.

➤ It may be noted that the recipient of income must be given a certificate in Form No. 16A within the stipulated time even if tax is borne by the payer of the income—*Circular No. 785, dated November 24, 1999.*

**5.6-1 TDS certificate in Form No. 16A** - TDS Certificates in Form No. 16A shall be issued by downloading from TIN website† by the following deductors -

- a. any deductor (including a Government deductor who deposits TDS in the Central Government Account through book entry), if tax is deducted on or after April 1, 2012, and

†Now, TRACES Portal.

‡ Where the due date of deposit of TDS falls during March 20, 2020 and June 29, 2020 and such amount is paid on or before June 30, 2020, then for the period of delay interest will be chargeable at the rate of 0.75 per cent per month (or part thereof). However, no penalty shall be levied (or no prosecution shall be sanctioned) in respect of such payment for the period of delay.

b. any company (including a banking company), if tax is deducted on or after April 1, 2011.

➤ *Authentication of TDS certificate in Form No. 16A* - Deductors, issuing the TDS certificates in Form No.16A by downloading from the TIN website, can authenticate these certificates by either using digital signature or manual signature.

**5.6-2 Time limit within which the certificate shall be issued** - TDS certificate in Form No. 16A shall be issued on quarterly basis as given below—

<i>Different quarters</i>	<i>TDS certificate should be given on or before the dates given below</i>
For the quarter ending June 30 of the financial year	August 15 of the financial year
For the quarter ending September 30 of the financial year	November 15 of the financial year
For the quarter ending December 31 of the financial year	February 15 of the financial year
For the quarter ending March 31 of the financial year	June 15 of the financial year immediately following the financial year in which tax is deducted

**5.6-3 Issue of duplicate certificate** - See para 1.6-4.

#### **Return of tax deduction at source from interest on securities**

**5.7** The following returns are to be submitted by the person responsible for paying interest on securities.

**5.7-1 Annual return [Rule 37]** - Annual return has to be filed in Form No. 26, only in respect tax deducted up to March 31, 2005.

**5.7-2 Quarterly statement TDS deposited** - In respect of tax deducted at source, the person deducting tax at source should submit quarterly statement of tax deposited [Form No. 26Q].

➤ *Due date of submission of quarterly return* - The above quarterly returns shall be submitted within the time-limit given below—

	<i>Due date of submission of quarterly TDS return</i>
For the quarter ending June 30 of the financial year	July 31 of the financial year
For the quarter ending September 30 of the financial year	October 31 of the financial year

	<i>Due date of submission of quarterly TDS return</i>
For the quarter ending December 31 of the financial year	January 31 of the financial year
For the quarter ending March 31 of the financial year	May 31 of the financial year immediately following the financial year in which tax is deducted

➤ *Mode of furnishing quarterly returns* - The following persons shall submit quarterly TDS/TCS returns electronically (along with the verification of the statement in Form No. 27A)—

1. When deductor or collector is an office of the Government.
2. When deductor/collector is the principal officer of a company.
3. When deductor/collector is a person who is required to get his account audited under section 44AB in the immediately preceding financial year.
4. When the number of deductee's/collectee's records in a statement for any quarter of the financial year are 20 or more.

Barring the cases given above, any other deductor/collector can submit quarterly TDS/TCS returns either in paper format or electronically.

➤ *Mode of uploading return* - With effect from February 19, 2013, the aforesaid electronic return can be submitted/uploaded under any one of the following options -

*Option 1* - Uploading quarterly returns with digital signature.

*Option 2* - Furnishing quarterly return electronically along with the verification of the statement in Form No. 27A.

*Option 3* - Furnishing quarterly return electronically along with electronic verification of the statement in Form No. 27A.

➤ *Other requirements* - The deductor or collector at the time of preparation of quarterly statement of TDS/TCS shall—

- a. quote his/its TAN;
- b. quote his/its PAN (except in the case where deductor/collector is an office of the Government);
- c. quote PAN of all deductees/collectees;
- d. furnish particulars of tax paid to the Central Government including book identification number or challan identification number;
- e. furnish particulars of amount paid or credited on which tax is not deducted in view of the issue of certificate of no deduction by the Assessing Officer under section 197; and

f. furnish particulars of amount paid or credited to the transport contractors (when PAN is submitted to the deductor and tax is not deducted under section 194C).

➤ *Other points* - The following points should be noted—

1. Quarterly return cannot be submitted before deposit of TDS and before deposit of interest (for late deposit) under section 201.
2. TAN of the deductor should be quoted correctly, otherwise a penalty of Rs. 10,000 can be imposed by the Assessing Officer.
3. A deductee should intimate his PAN to the deductor. Failure to do so may attract penalty of Rs. 10,000 on deductee.
4. The deductor should correctly quote PAN of deductees in quarterly returns/TDS certificates (if intimated by the deductees). Otherwise penalty of Rs. 10,000 can be imposed on the deductor.

**Consequences of failure to deduct or pay tax, furnish returns, etc.**

**5.8** The following are consequences of the different defaults :

**5.8-1** *Failure to deduct and/or pay tax* - See para 1.8-1.

**5.8-2** *Failure to comply with the provision of section 203A regarding tax deduction account number* - See para 1.8-2.

**5.8-3** *Failure to issue certificates, or submit returns* - See para 1.8-3.

**5.8-4** *Forfeiture of deduction in respect of interest on securities [Sec. 40(a)(ia) \*]* - Provisions of section 40(a)(ia) deal with disallowance of expenditure if there is a TDS default. This section covers the following expenses –

➤ *Up to the assessment year 2014-15* - Interest, commission, brokerage, rent, royalty, fees for technical/professional services payable to a resident or amounts payable (for carrying out any works contract) to a resident contractor/sub-contractor.

➤ *From the assessment year 2015-16* - Any sum payable to a resident.

The above payments are subject to tax deduction under different sections of Chapter XVII-B. If tax is deductible but not deducted or if tax is deducted but not deposited (or deposited late) with the Government, then these expenses are not allowed as deduction according to the provisions of section 40(a)(ia). These provisions are given below.

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\*Provisions of section 40(a)(ia) are not harsh and discriminatory and cannot be declared *ultra vires*—*Rakesh Kumar & Co. v. Union of India* [2009] 178 Taxman 481 (Punj. & Har.).

<i>Cases</i>	<i>Is such expenditure deductible in the current previous year</i>	<i>Is such expenditure deductible in any subsequent previous year</i>
<i>Case 1 - Tax is deductible but not deducted</i>	<p>&gt; 100 per cent of the expenditure will be disallowed in the current previous year (applicable up to the assessment year 2014-15)</p> <p>&gt; 30 per cent of the expenditure will be disallowed in the current previous year (applicable from the assessment year 2015-16)</p>	If tax is deducted in any subsequent year, the amount disallowed earlier will be deducted in the year in which TDS will be deposited by the assessee with the Government†
<i>Case 2 - Tax is deductible (and is so deducted) during the previous year but it is not deposited on or before the due date of submission of return of income under section 139(1)</i>	<p>&gt; 100 per cent of the expenditure will be disallowed in the current previous year (applicable up to the assessment year 2014-15)</p> <p>&gt; 30 per cent of the expenditure will be disallowed in the current previous year (applicable from the assessment year 2015-16)</p>	If tax is deposited with the Government after the due date of submission of return of income, the amount disallowed earlier will be deductible in that year in which tax will be deposited.†

**ILLUSTRATION**

Consider the following cases—

1. X Ltd. pays a sum of Rs. 1 lakh as rent of office building during the previous year 2023-24. As the amount is not more than Rs. 2,40,000, tax is not deducted at source under section 194-I.

Since tax is not deductible, disallowance under section 40(a)(ia) is not applicable.

2. A consultancy fees of Rs. 90,000 is credited by Y Ltd. to the account of payee on January 1, 2024 without tax deduction at source under section 194J. Tax is not deducted up to March 31, 2024. 30 per cent of Rs. 90,000

† Tax is not deducted by X Ltd. on commission payment of Rs. 1,00,000 during the previous year 2013-14. It is disallowed for the assessment year 2014-15. On April 20, 2023, X Ltd. deposits TDS on Rs. 1,00,000. The entire commission is Rs. 1,00,000 will be allowed as deduction for the assessment year 2023-24.

In respect of the amount disallowed for the assessment year 2014-15 (or earlier), the deduction for the whole of the amount [disallowed under section 40(a)(ia)] shall be allowed in the previous year in which TDS is deposited – Circular No. 1/2015, dated January 21, 2015.



(i.e., Rs. 27,000) will not be allowed as deduction for the previous year 2023-24 by virtue of section 40(a)(ia).

Suppose, tax is deducted on April 1, 2024 and it is deposited on April 20, 2024, Rs. 27,000 will be allowed as deduction for the previous year 2024-25.

3. Interest of Rs. 80,000 on company deposit is paid by Z Ltd. on January 10, 2023. Tax is deducted on the same day. Tax is deposited with the Government through internet banking on August 10, 2023 (i.e., before the due date of submission of return of income: September 30, 2023), it will be allowed as deduction for the previous year 2022-23.

Suppose, tax is deposited on October 10, 2023, then by virtue of section 40(a)(ia) Rs. 24,000 (being 30 per cent of Rs. 80,000) will be disallowed while calculating income of Z Ltd. for the previous year 2022-23. However, Rs. 24,000 will be allowed as deduction for the previous year 2023-24.

**5.8-4a** *Amendment made by the Finance Act, 2012* - The above provisions have been amended by the Finance Act, 2012 with effect from the assessment year 2013-14<sup>†</sup>. Under the amended provisions, a relief is given in *Case 1* (and not in *Case 2*). This relief will be available if the following conditions are satisfied –

1. Tax is deductible on the aforesaid payments but it is not deducted (wholly or partly) by the payer (i.e., *Case 1* of **para 5.8-4**).

2. The payer is not deemed to be an assessee-in-default under the first proviso to section 201(1). Under the first proviso to section 201(1), the payer is not deemed to be an assessee-in-default if –

- a. the recipient has furnished his return of income under section 139;
- b. the recipient has taken into account the above income in such return of income;
- c. the recipient has paid the tax due on the income declared in such return of income, and
- d. the payer electronically furnishes a certificate to this effect from a chartered accountant in Form No. 26A.

If the above conditions are satisfied, then for the purpose of section 40(a)(ia) it shall be deemed that the payer has deducted and paid the tax on

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<sup>†</sup> The Courts have been unanimous in holding that amendments, which are intended to remove unintended hardships, are declaratory in nature and, therefore, will operate retrospectively. The Delhi High Court in *CIT v. Ansal Land Mark Township (P.) Ltd.* [2015] 61 taxmann.com 45 had occasion to decide about retrospectivity of this amendment. Even though this amendment is made effective from the assessment year 2013-14, yet the Court held that it to be declaratory and curative in nature and, therefore, applicable retrospectively from the assessment year 2005-06.

such amount on the date of the furnishing of return of income by the resident recipient.

➤ *Provisions illustrated* - Consider the following cases -

1. X Ltd. pays a sum of Rs. 45,000 as commission to Y Ltd. (an Indian company) on April 20, 2023 without deducting tax at source. Y Ltd. pays advance tax on the due dates on its income (including Rs. 45,000). Entire tax liability is paid by Y Ltd. during the financial year 2023-24 by way of advance tax. Return of income of Y Ltd. for the assessment year 2024-25 is submitted on September 29, 2024. X Ltd. has uploaded certificate to this effect from a chartered accountant in Form No. 26A.

In this case, tax is not deducted by X Ltd. in the financial year 2023-24. By virtue of section 40(a)(ia), 30 per cent of the payment of Rs. 45,000 (*i.e.*, Rs. 13,500) will be disallowed in computing the income for the assessment year 2024-25. However, X Ltd. cannot be treated as an assessee-in-default under the provisions of first proviso to section 201(1), as the following conditions are satisfied -

- a. Y Ltd. has furnished his return of income under section 139;
- b. Y Ltd. has taken into account the above income in such return of income;
- c. Y Ltd. has paid the tax due on the income declared in such return of income, and
- d. X Ltd. has a certificate to this effect from a chartered accountant in Form No. 26A.

Under the amended provisions, it will be assumed that X Ltd. has deducted and paid tax on September 29, 2024. As a consequence, Rs. 13,500 will be allowed as deduction in the hands of X Ltd. for the financial year 2024-25.

2. On July 10, 2023, X Ltd. pays Rs. 10,80,000 as interest on debentures to B (a resident individual) after deducting tax at the rate of 10 per cent under section 193. The tax so deducted by X Ltd. is not deposited till March 31, 2025. However, B submits his return of income on July 15, 2024 after including Rs. 10,80,000 in his income. As per his return of income a refund of Rs. 4,00,000 is due to him.

In this case, the amended provisions are not applicable (the amended provisions are applicable only when the payer fails to deduct the whole or any part of tax). If tax is deducted but not paid, the amended provisions [as well as the first proviso to section 201(1)] are not applicable. In the hands of X Ltd., 30 per cent of Rs. 10,80,000 (*i.e.*, Rs. 3,24,000) will be disallowed for the assessment year 2024-25. X Ltd. cannot claim deduction of Rs. 3,24,000 for the assessment year 2025-26.

**5.8-4b** *Frequently asked questions* - The following questions are frequently asked—