IN THE INCOME TAX APPELLATE TRIBUNAL
"C" Bench, Mumbai

Before Shri D.K. Agarwal, Judicial Member and
Shri B. Ramakotaiah, Accountant Member

ITA No.1667/Mum/2010
(Assessment year: 2007-08)

Pfizer Ltd., Pfizer Centre, Parel Centre, S.V. Road, Jogeshwari (West), Mumbai 400012 PAN:AAACP 3334 M	Vs.	Income Tax Officer (TDS) (OSD) Range-2, KG Mittal Ayurvedic Hospital Building, Charni Road, Mumbai 400002
(Appellant)		**(Respondent)**

ITA No.1765/Mum/2010
(Assessment year: 2007-08)

Income Tax Officer (TDS) (OSD) Range-2, KG Mittal Ayurvedic Hospital Building, Charni Road, Mumbai 400002	Vs.	Pfizer Ltd., Pfizer Centre, Parel Centre, S.V. Road, Jogeshwari (West), Mumbai 400012 PAN:AAACP 3334 M
(Appellant)		**(Respondent)**

Assessee by:	Shri Percy Pardiwalla, Ms. Vasanti Patel & Ms. Charul Toprani
Department by:	Shri A.C. Tejpal, CIT (DR)
Date of Hearing:	01/10/2012
Date of Pronouncement:	31/10/2012

O R D E R

Per B. Ramakotaiah, A.M.

These are the cross appeals by assessee and the Revenue against the orders of theCIT (A)-14 Mumbai dated 31.12.2009. The issue in this appeal is with reference to the levy of tax under Section 201(1) and interest under Section 201(1A) of the Income Tax Act on the reason that assessee defaulted on not deducting the TDS on certain expenditure/payments made by it.

2. Briefly stated, the proceedings under section 133A were conducted on assessee's premises on 8.9.2008 and AO passed the order under section 201(1) & 201(1A) dated 30.12.2008 considering the following broadly categorized amounts as amounts covered by TDS provisions on which TDS was not made:

a) Provision made but tax not deducted under section 40(a)(i) & 40(a)(ia)
b) Purchase of traded goods
c) Purchase of packing material
d) Clinical Trial Expenses

3. It was the contention of AO that assessee made provision for expenses for an amount of ₹.10,01,98,450/- and there was short deduction of tax at ₹.2,06,45,686/- which is to be disallowed under section 40(a)(i) and 40(a)(ia). Assessee was required to show cause why the said amount could not be considered for determining the liability to the TDS under section 201(1) and 201(1A). After considering assessee's objections AO determined the amount of tax to be deducted and the same was demanded from assessee under section 201(1). AO also levied interest under section 201(1A). Likewise, the amounts under three other heads were also determined by AO under the above provisions.

4. The CIT (A) after considering assessee's detailed submissions, however, did not agree with the assessee contentions on 'provision made but tax not deducted' and upheld the action of AO in determining the tax and interest under section 201(1) & 201(1A). With reference to the other three items following various case law and the orders of the jurisdictional High Court, the CIT (A) deleted the demands so made by AO holding that the provisions of TDS are not applicable to the payments made under these heads. Accordingly assessee is aggrieved on the amount confirmed under item (a), whereas the Revenue is aggrieved on the amounts deleted on the items (b) to (d).

ITA No. 1667/Mum/2010 :

5. The learned Counsel reiterated the submissions made before AO and the CIT (A) to submit that assessee is in the practice of making provision for expenses at the end of the year as it has multifarious locations and innumerable transactions and since all the bills would not be received, without making specific entries into accounts of the parties, makes provision for expenses. Next year the entire provision of expenses was written back and the actual amounts paid to the respective parties were credited to their respective accounts and TDS as per the provisions are being made. In this context the method of accounting followed by assessee, entries made in the books of account and the reliance on the Board's Circular No.288 of 1980 were relied upon. It was the contention that it is not a constructive payment made to any payee as per the provisions of the Act and when assessee is making payment, it was following the TDS provisions. It was further submitted that when payee is not known or determined, TDS can not be made and relied on the order of the ITAT in the case of Industrial Development Bank of India vs. Income Tax Officer, 107 ITR 45 (Mum).

6. It was further submitted that assessee has added back the entire amount of provision made and filed copies of the computation statements as well as the orders passed by AO affirming the disallowance so made in the computation made under section 40(a)(i). The learned Counsel also placed on record the statement indicating the amount of provision made under various heads and the actual amount paid in the later year including the tax deducted at source and reconciling the amounts on this issue.

7. The learned DR, however, submitted that assessee having made provision for expenses in the books of account should have deducted the tax and therefore, the orders of AO and the CIT (A) required to be confirmed.

8. We have considered the issue. There is no dispute with reference to the fact that assessee made provision for expenses to an extent of ₹.10,01,98,459/- on about 23 items in the books of account. There is also no dispute to the fact that entire provision so made was disallowed in the computation under the head 'tax deductible but not deducted on provisions as on 31st March, 2007' in the computation of income. Therefore, the entire provision so made was disallowed under section 40(a)(i)/(ia) while filing the return of income by the itself.

9. As explained the general entries passed by Pfizer Ltd, in the books of account are as under:

"**Annexure-1**

Journal Entries passed by Pfizer in the books of account:

a) At the time of making the year end provision

Particulars	Debit (₹.)	Credit(₹.)
Expense a/c Dr.	XXX	
To provision for expenses a/c		XXX

b) At the time of reversal on first day of the next financial year

Particulars	Debit (₹.)	Credit (₹.)
Provision for expenses a/c Dr.	XXX	
To Expenses a/c		XXX

c) At the time of making payment to parties on the basis of the actual invoices received by Pfizer.

Particulars	Debit (₹.)	Credit (₹.)
Expenses a/c DR.	XXX	
To party's a/c		XXX
To TDS payable a/c		XXX"

10. As can be seen from the above entries, when the payment/ credit was made to the individual payee identified, all the provisions

of TDS are made applicable whether to a resident or to a non-resident as the case may be. In the absence of any identifiable payee, the provisions of TDS are not applicable as was held by the ITAT in the case of IDBI vs. I.T.O 107 ITD 45(Mum). In that the case the facts are as under:

> *"The assessee, a financial institution, was following financial years as its accounting year. It issued 'regular return bonds'. The terms and conditions for payment of interest on these bonds provided that the assessee was liable to pay interest at the rate of 16 per cent annually in respect of regular return bondholders, that the interest was payable on 9th June of each calendar year, except in the year of maturity, when interest was payable on maturity, that the interest, except at the lime of maturity, was to be paid to the person whose name was registered in the records of the assessee company as on 15th May of each calendar year, and that the bonds were transferable by endorsement and delivery, and the assessee did not, in any way, control such transfer of ownership. The assessee at the end of the relevant previous year as on 31.3.1994 made a provision for 'interest accrued but not due" in respect of regular return bonds and claimed deduction of the same in computation of business income. The assessee further credited the said provision to the interest payable account and reflected the same in the balance sheet. The assessee did not deduct tax at source in respect of the provision so made, The Assessing Officer noticed that the assessee did not deduct tax in terms of provision so made though in terms of the provisions of section 193, particularly read with Explanation thereto, it was required to deduct tax at source from the credit to 'interest payable account' and deposit the same with the Government. The Assessing Officer was of view that the assessee knew the identity of all the bondholders as on 31-3-1994 because it was maintaining a register of bondholders, and, therefore, it could not be said that the assessee did not know the names of the persons to whom interest was to be credited. The Assessing Officer, therefore held that the assessee did not comply with provisions of section 193 and imposed penalty under section 201 upon the*

assessee on account of non-deduction of tax at source in respect of interest liability credited to 'interest payable account· He also imposed the penalty under section 221 upon the assessee. On appeal, the Commissioner (Appeals) upheld the impugned order".

It was held that

"*the liability of tax deduction at source* is *in the nature of a vicarious or substitutionary liability, which presupposes existence of a principal or primary liability. Chapter XVII-B* is *titled*

'Collection and recovery of tax - deduction of tax at source: This title also indicates that the nature of tax deduction at source obligation is obligation for collection and recovery of tax. Under the Act, tax is *on the income and it* is *in the hands of the person who receives such income, except in the case of dividend distribution tax which* is *levied under section* 115-0, *a section outside the Chapter providing for collection and recovery mechanism and set out under a separate chapter 'Determination of tax in certain special cases - special provision relating to tax on distributed profits of domestic companies: A plain reading of section 190 and section* 191, *which are first two sections under the Chapter XVII, and of sections* 199, *202 and 203(1), would show this underlying feature of the tax deduction at source mechanism. 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 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 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 tad 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 it 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. 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 identify 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 5-7-1996 addressed to the Tata Iron & Steel Co. Ltd (Letter No.257/126 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, 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 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. Assessee had duly deducted the tax source at the time of payment i.e. on 9.6.1994 and there was no loss of revenue as such. Therefore, assessee did not have any liability to deduct tax at source in respect of provision for interest accrued but not due in respect of regular return bonds, made on 31.3.1994. When there was no obligation to deduct tax at source, there could not be any question of levy of penalty or interest. The next question for consideration in the instant case was as to whether AO could have imposed the penalty at all under section 221 upon assessee. A Coordinate Bench of the Mumbai Tribunal in the case of ITO v. Titagarh Steel Ltd (2001) 79 ITD 532, dealing with the consequences of non-deduction or short deduction of tax at source, had held that post 1-4-1989, penalty for non-deduction of tax at source or short deduction of tax at source can only be imposed under section 271C. The CBDT itself had in Circular No.551, dated 23-1-1990 accepted that until section 271C was inserted in the Act, 'no penalty was provided for failure to deduct tax at source'. It was not only merely a question of mentioning a wrong section, which could perhaps be covered by recourse to section 292B, it was also important to bear in mind that the impugned penalty was levied by an Officer of the rank of the Income Tax Officer, whereas penalty under section 271C could only have been levied by an Office of the rank of the Deputy (now Joint) Commissioner. The ITO was, from this point of view, not competent to impose the impugned penalty. Further, in the instant case, even according to the revenue, the default was on account of deduction of tax at source. Such a default could not be visited with penalty under section 221. Hence, the impugned penalty under section 221 was unsustainable in law".

11. In view of the above decision of coordinate bench, since the payee is not identifiable in this case also at the time of making provision, no TDS need to be made on the above amount. Further the entire provision has been written back in the next year and the actual amounts paid/credited were subjected to TDS as per the detailed statements filed before the authorities on which there is no dispute. Therefore, assessee is following the provisions of TDS as and when the amounts are paid/credited to respective parties.

12. As already explained and evidenced from the computation of income as well as the orders of AO in the assessment proceedings, the entire provision has been disallowed under section 40(a)(ia) and section 40(a)(i). Once the amount has been disallowed under the provisions of section 40(a)(i) on the reason that tax has not been deducted, it is surprising that AO holds that the said amounts are subject to TDS provisions again so as to demand the tax under the provisions of section 201 and also levy interest under section 201(1A). We are unable to understand the logic of AO in considering the same as covered by the provisions of section 194C to 194J. Assessee as stated has already disallowed the entire amount in the computation of income as no TDS has been made. Once an amount was disallowed under section 40(a)(i)/(ia) on the basis of the audit report of the Chartered Accountant, the same amount cannot be subject to the provisions of TDS under section 201(1) on the reason that assessee should have deducted the tax. If the order of AO were to be accepted then disallowance under section 40(a)(i) and 40(a)(ia) cannot be made and provisions to that extent may become otiose. In view of the actual disallowance under section 40(a)(i) by assessee having been accepted by AO, we are of the opinion that the same amount cannot be considered as amount covered by the provisions of section 194C to 194J so as to raise TDS demand again under section 201 and levy of interest under section 201(1A). Therefore,

assessee's ground on this issue are to be allowed as the entire amount has been disallowed under the provisions of section 40(a)(i)/(ia) in the computation of income on the reason that TDS was not made. For this reason alone assessee's grounds can to be allowed. Considering the facts and reasons stated above assessee's grounds are allowed.

13. Assessee has raised one more contention that interest under section 201(1A) should be levied till the date of payment and not till the date of order. Anyhow this issue became academic in nature, as we have already held that demand under section 201 cannot be raised once the entire amount has been disallowed in the computation of income under section 40(a)(i) and 40(a)(ia). In view of this even though the contention is correct being a legal issue, there is no need for adjudicating the matter as the grounds raised have been held in favour of assessee. AO is directed to delete the said demand so raised. Appeal is accordingly allowed.

ITA No.1765/Mum/2010

14. As briefly stated above, AO raised demand on 1.purchase of traded goods, 2.purchase of packing material and 3.clinical trials. The order of the CIT (A) on the three issues are as under:

1. **Finished/Traded Goods:**

> *"11. I have carefully considered the facts of the case, various agreements with third party, submission and legal propositions made by the Appellant. From the agreement it is clear that the assessee has exercised right for quality specification and quality control as agreed by the third party. This is common practice in pharma industries, wherein the purchaser of traded goods purchases goods only when it is up to their quality requirement. Further from the agreement it is clear that all other right and Obligation is with the seller of traded goods and the property in goods passes after it is delivered to the door step of the appellant. It is also a fact that no raw material is supplied by the appellant (purchaser)*

to the manufacturers. The manufacturing activities are also carried out by the manufacturers in their own premises. The manufacturers have also paid excise duties VAT/sales tax as applicable on the goods manufactured/sold. After going through the agreement and its various clauses and facts of the case in its entirety, it is concluded that the contract with the various parties are contract for purchases of traded goods and not of the works contract. I have also noted that the above issue is covered in the favour of the Appellant by the decision of Mumbai Tribunal in case of Novartis HealthCare Pvt. Ltd. v. ITO 29 SOT 425 (Mum) and Glenmark Pharmaceuticals Ltd. v. ITO (TDS) 30 SOT 19 (Mum) wherein the Hon'ble tribunal on identical facts has held that TDS is not required to be deducted on purchase of traded goods.

Based on the above, I am of the opinion that the provisions of Chapter XVII·B of the Act cannot be said to be applicable on purchase of finished/traded goods Accordingly, there is no default on the part of tile Appellant in complying with the provisions of Chapter XVII-B of the Act while making payment for purchase of finished/traded g0o.dS without deducting tax at source This ground of appeal is allowed in favour of the appellant".

2.Purchase of Packing Material:

"13. I have perused the facts of the case as well as the submissions of the appellant. I am of the opinion that this ground is covered in favour of the Appellant by the decision of jurisdictional High Court in the case of BDA Ltd vs. Income Tax Officer (TDS) 281 ITR 99 (Bom.) wherein the Hon'ble High Court has held that TDS is not required to be deducted under section 19cC on purchase of packing material.

Based on the above, I am of the opinion that the provisions of Chapter XVII-B of the Act cannot be said to be applicable on purchase of packing material. Accordingly, there is no default on the part of the Appellant in complying with the provisions of Chapter XVII-B of the Act while making payment for purchase packing material without deducting tax at source. In the result this ground is allowed".

3.Clinical Trials

"15. I have gone through the facts of the case and submissions of the appellant. As far as the appellant's contention that the above expenditure of ₹.11,35,14,000/- includes an amount of ₹.3,66,90,204/- on which TDS is not deductible on the following grounds:

a) Purchase of various materials.

b) Expenditure on food and travelling

c) Availability of tax exemption certificate

d) Payment of regulatory fees.

Prima facie TDS is not deductible on all the four items mentioned above. However, this particular break up has not been provided to AO. I therefore, direct AO to verify the above break up given by the appellant. If the above break up of expenditure given by the appellant is found to be correct, then I hold no TDS is required to be deducted on the above payments. AO is directed accordingly".

With regard to balance expenditure amount of ₹.7,68,21,907/- is concerned, the appellant has deducted TDS of ₹.42,45,914/- on the same. However, it is seen that payment in question is in the nature of professional fees. In order to carry out clinic trial, the person who carries out the trial must possess medical qualification and the person should be highly qualified and should possess technical expertise. Therefore, payment made in this respect is nothing but fees for professional/technical services. Accordingly, I hold that the above payment of ₹.7,68,21,907/- is a payment to professional fees, therefore, tax should have been deducted as per provisions of section 194J. ***Therefore, the action of AO is confirmed so far as the applicability of section 194J is concerned****. However, AO is directed to calculate TDS liability under section 194J. Whatever TDS liability comes under section 194J credit for taxes paid of ₹.42,45,914/- is to be allowed and balance amount needs to be recovered from the appellant. This ground of appeal is disposed off accordingly".*

15. After considering the rival contentions and perusing the order of the CIT (A), we are of the opinion that there is no need to differ from the order of the CIT (A). The learned CIT (A) has followed the

principles established by the Hon'ble High Court in the case of BDA Ltd vs. Income Tax Officer (TDS) 281 ITR 99 (Bom.) and CIT vs. Glenmark Pharmaceuticals Ltd, 324 ITR 199. Since the issues are crystallized in favour of assessee by the orders of the jurisdictional High Court, respectfully following the same we affirm the order of the CIT (A).

16. In the result Revenue appeal is dismissed.

17. In the result appeal filed by assessee in ITA No: 1667/Mum/2010 is allowed, while the appeal filed by the Revenue in ITA No.1765/Mum/2010 is dismissed.

Order pronounced in the open court on 31st October, 2012.

Sd/-	Sd/-
(D.K.Agarwal)	**(B. Ramakotaiah)**
Judicial Member	**Accountant Member**

Mumbai, dated 31st October, 2012.

Vnodan/sps

Copy to:

1. *The Appellant*
2. *The Respondent*
3. *The concerned CIT(A)*
4. *The concerned CIT*
5. *The DR, "C" Bench, ITAT, Mumbai*

By Order

Assistant Registrar
Income Tax Appellate Tribunal,
Mumbai Benches, MUMBAI