Circular No 18 of 2022

F.No. 370142/27/2022-TPL
Government of India
Ministry of Finance
Department of Revenue
Central Board of Direct Taxes
(TPL Division)
*****

New Delhi, Dated 13th September, 2022

Sub: Additional Guidelines for removal of difficulties under sub-section (2) of section 194R of the Income-tax Act, 1961

Finance Act 2022 inserted a new section 194R in the Income-tax Act, 1961 (hereinafter referred to as "the Act") with effect from 1st July 2022.

2. The new section mandates a person, who is responsible for providing any benefit or perquisite to a resident, to deduct tax at source @10% of the value or aggregate of value of such benefit or perquisite, before providing such benefit or perquisite. The benefit or perquisite may or may not be convertible into money but should arise either from carrying out of business, or from exercising a profession, by such resident.

3. This deduction is not required to be made, if the value or aggregate of value of the benefit or perquisite provided or likely to be provided to the resident during the financial year does not exceed twenty thousand rupees.

4. The responsibility of tax deduction also does not apply to a person, being an Individual/Hindu Undivided Family (HUF) deductor, whose total sales / gross receipts / gross turnover from business does not exceed one crore rupees, or from profession does not exceed fifty lakh rupees, during the financial year immediately preceding the financial year in which such benefit or perquisite is provided by him.

5. Sub-section (2) of section 194R of the Act authorises the Board to issue guidelines, for removal of difficulties, with the approval of the Central Government. These guidelines are required to be laid before each House of Parliament and are binding on the income-tax authorities and the person providing the benefit or perquisite.

6. Accordingly, in exercise of the power conferred by sub-section (2) of section 194R of the Act, CBDT had issued guidelines in the form of the Circular no 12 of 2022 dated 16th June 2022. Subsequently, some more clarifications are requested by stakeholders on various issues. Accordingly, this Circular is also issued under sub-section (2) of section 194R to provide clarification on issues which will help to remove difficulties in implementation of this provision.

7. **It is clarified that this Circular is only for removing difficulties in implementation of provisions of section 194R of the Act and it does not impact the taxability of income in the hands of the recipient which shall be governed by the relevant provisions of the Act.**

Guidelines

Question 1: Refer question No 3 of the Circular No 12 of 2022: If loan settlement/waiver by a bank is to be treated as benefit/perquisite, it would lead to hardship as the bank would need to incur the additional cost of tax deduction in addition to the haircut that he has taken. Will section 194R of the Act apply in such a situation?

Answer: It is true that waiver or settlement of loan by the bank may be an income to the person who had taken the loan. It is also true that subjecting such a transaction to tax deduction under section 194R of the Act would put extra cost on such bank, as this would require payment of tax by the deductor in addition to him taking a haircut already. Hence, to remove difficulty, it is clarified that one-time loan settlement with borrowers or waiver of loan granted on reaching settlement with the borrowers by the following would not be subjected to tax deduction at source under section 194R of the Act:

(i) Public Financial Institution as defined in clause (72) of section 2 of the Companies Act 2013;

(ii) Scheduled Bank as defined in clause (ii) of the *Explanation* to clause (viia) of sub-section (1) of section 36 of the Act;

(iii) Cooperative bank (other than a primary agricultural credit society) as defined in the *Explanation* to sub-section (4) of section 80P of the Act;

(iv) Primary co-operative Agricultural and Rural Development Bank as defined in the *Explanation* to sub-section (4) of section 80P of the Act;

(v) State Financial Corporation being a financial corporation established under section 3 or section 3A or an institution notified under section 46 of the State Financial Corporation Act, 1951;

(vi) State Industrial Investment Corporation being a Government company within the meaning of sub-section (45) of section 2 of the Companies Act 2013, engaged in the business of providing long-term finance for industrial projects;

(vii) Deposit taking Non-Banking Financial Company as defined in clause (e) of the *Explanation* 4 to section 43B of the Act;

(viii) Systemically Important Non-deposit Taking Non-Banking Financial Company as defined in clause (g) of the *Explanation* 4 to section 43B of the Act;

(ix) Public company engaged in providing long term finance for construction or purchase of houses in India for residential purpose and which is registered in accordance with the guidelines/direction issued by the National Housing Bank formed under National Housing Bank Act 1987;

(x) Asset Reconstruction Companies registered under section 3 of Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SRFAESI) Act 2002.

As stated earlier, this clarification is only for the purposes of section 194R of the Act. The treatment of such settlement/waiver in the hands of the person who had got benefitted by such waiver would not be impacted by this clarification. Taxability of such settlement/waiver in the hands of the beneficiary will be governed by the relevant provisions of the Act.

Question 2: Refer question No 7 of the Circular No 12 of 2022- If under the terms of the agreement, the expense incurred by the service provider is the cost of service recipient and such cost is reimbursed by the service recipient to service provider, how is it benefit/perquisite if the bill is not in the name of service recipient?

Answer: In answer to question No 7 of the Circular No 12 of 2022, it has been clarified that any expenditure which is the liability of a person carrying out business or profession, if met by the other person is in effect benefit/perquisite provided by the second person to the first person in the course of business/profession.

Now, if service provider incurs some expense in the course of rendering service to service recipient and the bill is in the name of service provider, then in substance (irrespective of the terms of the agreement) this expense is the liability of the service provider and not of service recipient. It is service provider who gets input credit of GST included in the expenses incurred by him. If it was the liability of the service recipient, then GST input credit would have been allowed to him (service recipient) and not to service provider. Hence, the answer to question No 7 in the Circular No 12 of 2022 correctly clarifies that in such a situation reimbursement of such an expense is benefit/perquisite on which tax is required to be deducted under section 194R of the Act.

Subsequently, it has been brought to the notice that in GST, if service provider incurs an expense as "pure agent", then GST input credit is allowed to service recipient and not to service provider. Broadly speaking a pure agent is one who while making a supply to the recipient, also receives and incurs expenditure on some other supply on behalf of the recipient and claims reimbursement (as actual, without adding it to the value of his own supply) for such supplies from the recipient of the main supply. While the relationship between them (provider of service and recipient of service) in respect of the main service is on a principal to principal basis, the relationship between them in respect of other ancillary services is that of a pure agent. Under the GST Valuation Rules 2017 "pure agent" is given the following meaning.

"pure agent" means a person who

a) enters into a contractual agreement with the recipient of supply to act as his pure agent to incur expenditure or costs in the course of supply of goods or services or both;

b) neither intends to hold nor holds any title to the goods or services or both, so procured or provided as pure agent of the recipient of supply;

c) does not use for his own interest such goods or services so procured; and

d) receives only the actual amount incurred to procure such goods or services in addition to the amount received for supply he provides on his own account.

The GST valuation rules provide that expenditure incurred as a pure agent, will be excluded from the value of supply, and thus also from aggregate turnover. However, such exclusion of expenditure incurred as a pure agent is possible only and only if all the conditions required to be considered as a pure agent and further conditions stipulated in the rules are satisfied by the supplier in each case. The supplier would have to satisfy the following conditions (in addition to the condition required to be satisfied to be considered as a pure agent and discussed above) for exclusion from the value as under:-

i. the supplier acts as a pure agent of the recipient of the supply, when he makes payment to the third party on authorization by such recipient;

ii. the payment made by the pure agent on behalf of the recipient of supply has been separately indicated in the invoice issued by the pure agent to the recipient of service; and

iii. the supplies procured by the pure agent from the third party as a pure agent of the recipient of supply are in addition to the services he supplies on his own account.

In case these conditions are not satisfied, such expenditure incurred is included in the value of supply under GST. However, in the abovementioned case of "pure agent", if all the conditions are satisfied, the GST input credit is allowed to the recipient and it is not considered as supply of the pure agent, it is clarified that amount incurred by such "pure agent" for which he is reimbursed by the recipient would not be treated as benefit/perquisite for the purpose of section 194R of the Act.

Question 3: Refer question No 7 of the Circular No 12 of 2022- Question No 30 of CBDT Circular No 715 dated 8th August 1995 clarifies that tax deduction under section 194C and 194J is required to be made from the gross amount of bill including the reimbursement. A person has provided service to a Company and out of pocket expenses are charged by him to the Company along with service fee in the same bill. Company deducts tax under section 194J of the Act on both service fee component as well as on out of pocket expense in accordance with this circular. Is there a non-compliance with the provision of section 194R of the Act?

Answer: Relevant portion of CBDT Circular No 715 dated 8th August 1995 is as under

Question 30 : Whether the deduction of tax at source under sections 194C and 194J has to be made out of the gross amount of the bill including reimbursements or excluding reimbursement for actual expenses?

Answer : Sections 194C and 194J refer to any sum paid. Obviously, reimbursements cannot be deducted out of the bill amount for the purpose of tax deduction at source.

If out of pocket expenses (reimbursement) are already part of the consideration in the bill on which tax is deducted under the relevant provisions of the Act, other than section 194R, in accordance with the Circular No 715 dated 8th August 1995, it is clarified that there will not be further liability for tax deduction under section 194R of the Act.

In the above example, out of pocket expense is part of the consideration in the bill for professional fee that is charged to the Company and the tax is deducted under section 194J of the Act on the entire consideration including on out of pocket expense. In such a case, the out of pocket expense is already included as part of professional fee. Hence, there is no further benefit/perquisite which requires tax deduction under section 194R of the Act.

Question 4: Refer question No 8 of the Circular No 12 of 2022- If there is a dealer conference to educate the dealers about the products of the company – (i) is there a requirement that all dealers must be invited in the conference, (ii) what if dealers arrive one day before and leave one day after and (iii) how to identify benefit against individual dealers in a group activity?

Answer: Representations have been received from various stakeholders seeking clarity on these questions arising out of answer to question No 8. It is clarified that

(i) it is not necessary that all dealers are required to be invited in a dealer/business conference for the expenses to be not considered as benefit/perquisite for the purposes of tax deduction under section 194R of the Act.

(ii) Expenditure on participants of dealer/business conference for days which are on account of over stay prior to the dates of conference or beyond the dates of such conference would be considered as benefit/perquisite for the purposes of section 194R of the Act. However, a day immediately prior to actual start date of conference and a day immediately following the actual end date of conference would not be considered as over stay.

(iii) It is brought to the notice that there may be expenses during such dealer/business conference which need to be classified as benefit/perquisite and tax is required to be deducted under section 194R of the Act. However, there may be practical difficulties in identifying such benefit/perquisite to actual recipient due to the fact that it is a group activity and reasonable allocation is not possible. Noncompliance of the provision of section 194R of the Act, in such a case, would not only result in disallowance under clause (ia) of section 40 of the Act but may also result in treating the benefit/perquisite provider as assessee in default under section 201 of the Act with all other consequences.

In order to remove these practical difficulties, it is clarified that if benefit/perquisite is provided in a group activity in a manner that it is difficult to match such benefit/perquisite to each participant using a reasonable allocation key, the benefit/perquisite provider may at his option not claim the expense, representing such benefit/perquisite, as deductible expenditure for calculating his total income. If he decides to opt so, he will not be required to deduct tax under section 194R on such benefit/perquisite and therefore he will not be treated as assessee in default under section 201 of the Act. Thus, in such a case he must add back the expenditure, representing such benefit/perquisite, to calculate his total income if such expenditure is debited in the account.

Answer to question No 8 in the Circular No 12 of 2022 is modified to this extent.

Question 5: Refer question No 9 of the Circular No 12 of 2022- Company "A" gifts a car to its dealer "B" and deducted tax on this benefit under section 194R of the Act. Dealer "B" uses this car in his business. Will he get deduction for depreciation in calculating his income under the head "profits and gains of business or profession"?

Answer: Once Company "A" has deducted tax on gifting of car in accordance with section 194 R of the Act (or released the car after dealer "B" showed him payment of tax on such benefit) and dealer "B" has included this benefit as income in his income tax return, it would be deemed that the "actual cost" of the car for the purposes of section 32 of the Act shall be the amount of benefit included by dealer "B" as income in his income-tax return. Hence, dealer "B" can get depreciation on fulfillment of other conditions for claiming depreciation.

Question 6: Whether Embassy/High Commissions are required to deduct tax under section 194R of the Act?

Answer: For the removal of difficulty it is clarified that the provision of section 194R is not applicable on benefit/perquisite provided by, an organization in scope of The United Nations (Privileges and Immunity Act) 1947, an international organization whose income is exempt under specific Act of Parliament (such as the Asian Development Bank Act 1966), an embassy, a High Commission, legation, commission, consulate and the trade representation of a foreign state.

Question 7: Whether issuance of bonus share/right share is a benefit or perquisite if issued by a company in which the public are substantially interested as defined in clause (18) of section 2 of the Act and whether tax is required to be deducted under section 194R of the Act?

Answer: In case of bonus shares which are issued to all shareholders by a company in which the public are substantially interested as defined in clause (18) of section 2 of the Act, it has been represented that this does not result in any benefit to shareholders as the overall value and ownership of their holding does not change. Further cost of acquisition of bonus share is taken as nil for capital gains computation when this share is sold. Similar representations have been received seeking clarity on issuance of right shares.

It is clarified that the tax under section 194R of the Act is not required to be deducted on issuance of bonus or right shares by a company in which the public are substantially interested as defined in clause (18) of section 2 of the Act, where bonus shares are issued to all shareholders by such a company or right shares are offered to all shareholders by such a company, as the case may be.

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