Short Write Up on Impact Analysis of Hon'ble Apex court recent verdict in case of :*CHECKMATE SERVICES PVT LTD VS CIT-1 in CIVIL APPEAL 2833/2016 order dated 12 October 2022*

On issue of : Allowability/treatment of "delayed" Employee PF Contribution in hands of assessee under provisions of Income Tax Act (PGBP/Business Head)

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1. **Background of the controversy in brief**

Under income tax act,1961 (1961 Act) , chapter IV-D contains provisions relating to computation of income under head "profits and gains of business or profession" which chapter (IV-D) starts from sec. 28 and goes till sec. 44DB. The relevant provisions under 1961 Act on issue of employee contribution recd. by assessee towards provident fund(PF)/ employee state insurance (ESI) etc are : sec. 2(24)(x) (this provision makes the employee contribution recd. towards PF/ESI etc as income of assessee) ; sec 36(1)(va) (this provision states if assessee credits the employee contribution so recd. before due date as per relevant PF/ESI act towards the relevant fund then same can be allowed as *deduction* in computing business income) and sec. 43B (b) (this clause deals with deduction for sum payable by assessee as an employer by way of contribution to PF fund etc) and erstwhile omitted second proviso to sec 43B (omitted by Finance Act 2003). ***Hon'ble Apex court has simply noted in captioned order the recent amendment in sec 43B (explanation 5) and explanation 2 to sec 36(1)(va) as added by Finance Act 2021.***There has been cleavage of judicial opinion between Kerala (Commissioner of Income Tax v. Merchem Ltd., ITA No. 402/2009)&

Gujarat high court (Commissioner of Income Tax-I v Checkmate Services P. Ltd., Tax Appeal No. 680 of 2014, dated 14.10.2014.)taking the strict view that employee contribution could not be covered under sec. 43B where as all other high courts (high Courts of Bombay, Himachal Pradesh, Calcutta, Guwahati and Delhi favouring the interpretation beneficial to the assesses) taking the liberal view that sec. 43B would include employee contribution also thus entitling assessee to claim deduction if said amount is paid before return filing date .

2. **Adjustment on Mass level in Summary proceedings /Intimation u/s 143(1) of 1961 Act and further litigation thereon**

Before the amendment of Finance Act 2021 came, there has already been huge number of intimations u/s 143(1) of 1961 Act (summary proceedings) where adjustments were made on issue of employee contribution towards ESI/PF etc leading to mass appeals at first appeal *(which were mainly dismissed on basis that Finance 2021 amendment is retrospective in nature)* and further second appeals at ITAT (where large number of cases are hitherto decided bh ITAT across country taking view beneficial to assessee).

3. **Finance Act 2021 amendment and Hon'ble Delhi high court recent views (retrospective vs prospective saga)**

Recently Finance Act 2021 made amendments in sec 36(1)(va) vide expl 2 and sec 43B (explanation 5). In this context the seminal issue of retrospective vs prospective nature of the stated amendment by Finance Act 2021 came up for extensive consideration before Hon'ble Delhi high

court in case of ***PCIT vs TV Today Network Ltd (ITA 227/2022) order dated 27.07.2022*** where high court took the view that stated amendment are prospective in nature.

4. **Overview/outline of Recent SC *edict*** (in case of Checkmate Services Pvt Ltd vs CIT Civil appeal 2833/2016 order dated 12 october 2022 by **His lordship Hon'ble Justice S.Ravindra Bhatt)**

Though in Hon'ble SC latest order there is no discussion on retrospective vs prospective scope of amendment by Finance Act 2021, but Hon'ble SC in the present order has considered entire conspectus of the matter (*related history of sec 2(24)(x); sec 36(1)(va) (employee contribution) versus (employer contribution) vide sec 36(1) (iv) / sec 43B (b) / second proviso etc*) with specific reference to explanatory CBDT circulars Circular No. 372 dated 08-12-1983. & Circular No. 495 dated 22.09.1987 etc). Applying the rule of strict interpretation that taxing statutes are to be construed strictly, and that there is no room for equitable considerations (as per Ajmera Housing Corporation & Ors. vs. Commissioner of Income, 2010 (8) SCC 739.; Commissioner of Income Tax-III v Calcutta Knitwears, Ludhiana 2014 (6) SCC 444. ;Union of India & Ors. vs. Exide Industries Limited & Ors., 2020 (5) SCC 274.; Eagle Flask Industries Ltd. v. Commissioner of Central Excise, 2004 Supp (4) SCR 35.; State of Jharkhand v Ambay Cements, (2005) 1 SCC 368; ; Commissioner of Income Tax v. Ace Multi Axes Systems Ltd., 2018 (2) SCC 158; The Constitution Bench, in Commissioner. of Customs v. Dilip Kumar & Co 2018 (9) SCC 1.) and difference in character of EMPLOYER & EMPLOYEE contribution (SC Held: *"..When Parliament introduced*

Section 43B, what was on the statute book, was only employer's contribution (Section 34(1)(iv)). At that point in time, there was no question of employee's contribution being considered as part of the employer's earning. On the application of the original principles of law it could have been treated only as receipts not amounting to income. When Parliament introduced the amendments in 1988-89, inserting Section 36(1)(va) and simultaneously inserting the second proviso *of Section 43B, its intention was not to treat the disparate nature of the amounts, similarly...Parliament intended to retain the separate character of these two amounts, is evident from the use of different language....other words, there is a marked distinction between the nature and character of the two amounts – the employer's liability is to be paid out of its income whereas the second is deemed an income, by definition, since it is the deduction from the employees' income and held in trust by the employer.")* finally the view of Kerala and Gujarat high court is given imprimatur by SC and other high court views favoring assessee is held to be not laying down correct law.

5. Way forward : Impact of recent SC decision on ongoing litigation on issue of employee contribution

It is no doubt true that once Hon'ble SC declares law on any issue it operates /applies from the very inception as overruling is generally retrospective unless prospective overruling is applied to (**refer Delhi high court Lakshmi Sugar Mills vs CIT**) , and so viewed , it may be significant to analyze the implications of SC ruling in following two important situations:

A) **Where matter is already pending before first appeal (at CIT-A or /second appeal at ITAT and original disallowance was made in intimation u/s 143(1) of 1961 Act**:

In authors opinion one may still argue on jurisdictional ground of validity of the stated adjustment made in summary proceedings u/s 143(1) of 1961 Act given restricted and limited scope of proceedings u/s 143(1): Reference can be made to CBDT Circular 1/2009 on scope of permissible adjustment u/s 143(1)

relevant text of CBDT Circular 1/2009 on restricted /limited /narrow scope of permissible adjustment u/s 143(1):

"28. Correction of arithmetical mistakes and adjustment of incorrect claim under sub-section (1) of section 143 through Centralised Processing of Returns

28.1 *Generally, tax administrations across countries adopt a two-stage procedure of assessment as part of risk management strategy. In the first stage, all tax returns are processed to correct arithmetical mistakes, internal inconsistency, tax calculation and verification of tax payment. At this stage, no verification of the income is undertaken. In the second stage, a certain percentage of the tax returns are selected for scrutiny/audit on the basis of the probability of detecting tax evasion. At this stage, the tax administration is concerned with the verification of the income.*

28.2 *In India, the scheme of summary assessment being in force since the 1st day of June, 1999 does not contain any provision allowing for prima facie adjustment. The scope of the present scheme is limited only to checking as to whether taxes have been correctly paid on the income returned. Under the existing provisions of sub-section (1) of section 143, there is no provision for correcting arithmetical mistakes or internal inconsistencies. This leads to avoidable revenue loss. With an objective to reduce such revenue loss, sub-section (1) of section 143 of the*

Income-tax Act has been amended to provide that the total income of an assessee shall be computed under sub-section (1) of section 143 after making the following adjustments to the total income in the return:—

(a) any arithmetical error in the return; or

(b) an incorrect claim, if such incorrect claim is apparent from any information in the return.

***28.3** Further the meaning of the term "an incorrect claim apparent from any information in the return" has been defined by inserting an explanation in the said section. This term shall mean such claim on the basis of an entry, in the return:—*

(a) of an item, which is inconsistent with another entry of the same or some other item in such return;

(b) in respect of which, information required to be furnished under this act to substantiate such entry has not been so furnished; or

(c) in respect of a deduction, where such deduction exceeds specified statutory limit which may have been expressed as monetary amount or percentage or ratio or fraction.

***28.4** Further, it is clarified that above adjustments would be made only in the course of computerized processing without any human interface. In other words, the software would be designed to detect arithmetical inaccuracies and internal inconsistencies and make appropriate adjustments in the computation of the total income. For this purpose the Department is in the process of establishing a system for Centralized Processing of Returns. To facilitate this, sub-sections (1A), (1B) and (1C) have been inserted in section 143 to provide that —*

(a) the Board may make a scheme with a view to expeditiously determine the tax payable by, or refund due to, the assessee;

(b) the Central Government may issue a notification in the Official Gazette, directing that any of the provisions of this Act relating to processing of returns shall not apply or shall apply with such exceptions, modifications and adaptations as may be specified in the notification. However, such direction shall not be issued after 31-3-2009;

(c) every notification shall be laid before each House of Parliament as soon as such notification is issued. Along with the notification, the scheme referred above is also required to be laid before each House of Parliament.

***28.5** Similar amendment has also been carried out in section 115WE of the Income-tax Act, relating to fringe benefits.*

***28.6** Applicability - These amendments have been made applicable with effect from 1-4-2008."*

***& Hon'ble SC decision in case of Vodafone Idwa Limited vs ACIT 424 ITR 664** (on scope of sec 143(1) vis a vis sec 143(2): Held precisely : The power under sub-section (1) of Section 143 of the Act is summary in nature designed to cause adjustments which are apparent from the return while that under sub-sections (2) and (3) is to scrutinize the return and cause deeper probe to arrive at the correct determination of the liability of the assessee.*

*& specific decisions of **Delhi bench of ITAT in case of : SVS Guarding Services Pvt Ltd ITA 231/Del/2022 (order dated 24.05.2022:** In the present appeal before us, addition of aforesaid amount of Rs. 29,52,674/- has been made by way of adjustments and intimation u/s 143(1) of Income Tax Act, on a debatable and controversial issue, and Ld. CIT(A) did err in law, in not deleting this addition.) and **Ahmedabad bench ITAT in case o Arham Pumps (ITA 206/Ahd/2021 order dated 27.04.2022** Held : On going through the above intimation made under section 143(1), CPC has not followed the above provisos by giving proper opportunity to the assessee to defend its case as per the first proviso to section 143(1)(a) . Further, the NFAC order is also silent about the intimation to the assessee. Therefore, we find that intimation issued under section 143(1) dated 19.10.2019 is against first proviso to section 143(1)(a),*

and therefore, the entire 143(1) proceedings is invalid in law.) & delhi bench ITAT decision in Maskat Technologies Pvt Ltd decision in ITA 1540/Del/2020 order dated 30.06.2021

(Further one may refer to following judicial pronouncement on limited & restricted scope of sec 143(1): **Bombay high court 196 ITR 55; Calcutta High court 228 CTR 72)**

Thus from above it can be concluded that if adjustment on account of employee contribution disallowance is made in intimation u/s 143(1) then same may be assailed in light of above jurisprudence.

However where there is already an addition in otherwise valid asst. completed u/s 143(3) and then appeal is still pending on this subject issue, then it may be difficult to contest the same in light of SC decision .

Further if assessee has hitherto claimed such employee contribution u/s 43B taking shelter of then prevailing favorable High court decisions , and no further addition is made on this count either u/s 143(1) or sec 143(3) and no pending proceedings are there ,then, may be revenue could now in light of present sc decision if limitation period u/s 154 is otherwise not expired (sec 154(7): Four years from end of concerned year in which order to be amended was passed) then rectification could be done qua the same and so viewed sec. 148 ought not to be used (refer Bombay high court decision in Hindustan Unilever case (***Hindustan Unilever Ltd. v. Dy. CIT (2011) 325 ITR 102 (Bom.)(HC) Reopening for rectifying mistakes are invalid.***).

But still, if rectification period u/s 154 is over then may be if revenue tries to explore sec 148/148A under new reopening regime , then, assessee may try argue on basis of ***statutory defense available u/s 149(1)(b) (beyond three year reopening : special conditions to be fulfilled incl. monetary threshold of Rs 50lacs per year) and erstwhile first proviso to sec. 147 (beyond four years reopening where already regular asst has taken place) etc.***

B) **Where matter is already decided by ITAT in assessee favor applying favorable view on merits which favorable view is overruled by SC in present decision**: Though subject to monetary threshold stipulated in extant CBDT instructions (monetary limit for appeal fining by revenue), revenue can also approach to high court u/s *260A (if relevant tax effect exceeds Rs 1 crore)* against order of ITAT where relief is granted to assessee (**time limit of 120 days**) and also may try remedy u/s 254(2) as mistake apparent from record (**within six months**). *In appeal u/s 260A, condonation can also be requested.* ***Here if assessee has taken jurisdictional plea on limited/narrow scope of adjustment u/s 143(1) also in its appeal then suitable cross objection/defense plea may be raised regurgitating /resurrecting the said jurisdictional plea before high court/ITAT , being pure question of law (jurisdictional issue) and/or suitable prayer may be made for decision by ITAT on the said jurisdictional plea. This may make entire scenario revenue neutral in cases where adjustment is made in intimation u/s 143(1).***

6. ***Vires of subject amendment made vide Finance Act 2021 in sec 36(1)(va) and sec 43B :*** **Simply put, now specially after /from Finance Act 2021 when plainly seen in light of amendments made u/s 36(1)(va) (explanation 2) and sec 43B (explanation 5), it is clear that once given /prescribed dead line of due date under relevant law (qua employee contribution) is missed then disallowance of employee contribution becomes *permanent* and can never be claimed (in authors humble understanding).** The constitutional validity of this amendment under sec 36(1)(va) read with sec 43B to make it permanent disallowance is yet to be tested and is still a open constitutional question in authors humble opinion , on touchstone of article 14 of constitution of india (specially manifest arbitrariness aspect and proportionality ground) **– scope of constitutional challenge on such basis may be referred in Hon'ble SC latest dictum in Ganpati Dealcom case reported at 447 ITR 108 (by Justice NV Ramana).**

7. There can be no question of any sort of any concealment penalty etc u/s 271(1)(c) and /or under reporting /misreporting penalty u/s 270A on this issue being apparent matter of extensive judicial debate.

8. **Closing remarks**:

In authors humble opinion it would have been in fitness of things and much better if Hon'ble *Apex court could make this a case of prospective overruling in peculiar nature of the controversy where maximum high courts took consistent view (albeit favoring assessee) based on long standing Hon'ble SC order in Alom Extrusions case (2010) 1 SCC 489 and in line with well acknowledged principle of STARE DECISIS.*