Absurdities in C.B.D.T. Circular on Fringe Benefit Tax

278 ITR (Jour.) 61 (Part-5)

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There are lot of ambiguities in the provisions of fringe benefit tax (FBT), which have been newly introduced in the Income-Tax Act, 1961 (the Act), vide the Finance Act, 2005. Therefore, tax-payers were expecting that the explanatory notes in respect of the aforesaid provisions, to be issued by the Central Board of Direct Taxes (CBDT), would clear up the uncertainties and ambiguities, etc., which have crept there into. The much awaited Circular No.8/2005, dated 29.8.2005, by way of explanatory notes on FBT, has now been issued by the CBDT. However, the aforesaid Circular, instead of bringing about a modicum of clarity in the aforesaid provisions, has created further confusion in respect thereof.

There are so many absurdities in the answers to a number of questions in the aforesaid Circular. The major absurdities are, however, to be found in the interpretation of deemed fringe benefits (DFB), as contemplated under Section 115WB(2) of the Act and in respect of items of income, which are exempt in the hands of the employees. I would confine myself to these two issues only, in the present Article.

The main absurdity is that the computation of deemed fringe benefits, as contemplated under Section 115WB(2) has gone totally beyond the purpose or object for which FBT has been brought in. Even the expenditure which is incurred in respect of persons other than the employees, has also been held to be liable to FBT as per the aforesaid Circular. This was never the object or purpose of enacting the provisions of FBT. Besides, the items of income like leave travel allowance, reimbursement of medical expenses upto Rs.15,000, etc., which have been specifically exempted from tax in the hands of the employees have also been held to be liable to FBT. Again this was never the object or purpose of the provisions of FBT.

It may also be stated here that a Circular of the CBDT is meant to soften the rigours of the provisions of the Act but the aforesaid Circular is prejudicial to the interests of the tax-payers on a number of issues. Therefore, the aforesaid Circular is *ultra vires* the provisions of Section 119(2) of the Act and accordingly, its validity is totally suspect and liable to be challenged in the Courts of law.

All the relevant issues in this context are discussed hereinafter.

1. Purpose / Object of Fringe Benefit Tax (FBT)

As could be seen from para (2) of the aforesaid Circular under the head '*Objective'*, the FBT provisions have been brought in for the purpose bringing within the tax-net, certain perquisites or benefits which were going untaxed in the hands of both the employees as well as the employer.

If one examines the charging section viz. Section 115WA, Explanatory Memorandum to the Finance Bill, 2005 and the Finance Minister's speech on various occasions, it would be absolutely clear that only that expenditure will fall within the ambit of FBT, which results in some personal benefit or gain for the employees. All other expenses will remain outside the purview of FBT. The aforesaid aspects may be discussed as follows-

I. Charging Section 115WA

Section 115WA is the charging section for FBT. This is, therefore, the most important Section of Chapter XII-H of the Act. Section 115WA reads as follows:-

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S.115WA

(1) In addition to the income-tax charged under this Act, there shall be charged for every assessment year commencing on or after the 1st day of April, 2006, additional income-tax (in this Act referred to as fringe benefit tax) in respect of the fringe benefits provided or deemed to have been provided by an employer to his employees during the previous year at the rate of thirty per cent on the value of such fringe benefits.

(2) Notwithstanding that no income-tax is payable by an employer on his total income computed in accordance with the provisions of this Act, the tax on fringe benefits shall be payable by such employer.

It may be seen from the aforesaid Section 115WA(1) that FBT is an additional income-tax in respect of the fringe benefits provided or deemed to have been provided by an employer to his employees during the previous year, at the rate of 30% on the value of such fringe benefits.

Thus, it is quite clear that FBT is a tax on the fringe benefits provided or deemed to have been provided by an employer to his employees. **It clearly indicates that FBT will not cover any expenditure, which does not involve any benefit or gain to the employees**.

It is a settled position in law that in case of a conflict between the charging section and other related section, the provisions of the charging section will override the provisions of the other related section. Similarly, in case of an ambiguity in other provisions, the provisions of charging section may be used as a torch light in order to enlighten us about the gray areas in the other provisions.

II. Relevant part of the Explanatory Notes & Finance Minister's speeches relating to Finance Bill, 2005

The avowed purpose of FBT is to tax benefits that are usually enjoyed collectively by the employees and cannot be attributed to individual employees.

The purpose of FBT, as explained by the Finance Minister in his speech, while introducing the Finance Bill, 2005, and Explanatory Memorandum to the Finance Bill, 2005, is as follows:-

(i) Finance Minister's Speech

I have looked into the present system of taxing perquisites and I have found that many perquisites are disguised as fringe benefits, and escape tax. Neither the employer nor the employee pays any tax on these benefits which are certainly of considerable material value. At present, where the benefits are fully attributable to the employee, they are taxed in the hands of the employee; that position will continue. In addition, I now propose that where the benefits are usually enjoyed collectively by the employees and cannot be attributed to individual employees, they shall be taxed in the hands of the employer. However, transport services for workers and staff and canteen services in an office or factory will be outside the tax net. The tax is not a new tax, although I am obliged to call it by a new name, namely, Fringe Benefit Tax. The rate will be 30 per cent on an appropriately defined base. [273 ITR(St.) p.56].

(ii) Explanatory Memorandum to the Finance Bill, 2005

The taxation of perquisites or fringe benefits provided by an employer to his employees, in addition to the cash salary or wages paid, is subject to varying treatment in different countries. These benefits are either taxed in the hands of the employees themselves or the value of such benefits is subject to a 'fringe benefit tax' in the hands of the employer. The rationale for levying a fringe benefit tax on the employer lies in the inherent difficulty in isolating the 'personal element' where there is collective enjoyment of such benefits and attributing the same directly to the employee. **This is so especially where the expenditure incurred by the**

employer is ostensibly for purposes of the business but includes, in partial measure, a benefit of a personal nature.

Moreover, in cases where the employer directly reimburses the employee for expenses incurred, it becomes difficult to effectively capture the true extent of the perquisite provided because of the problem of cash flow in the hands of the employer. [Emphasis provided]

Therefore, it is proposed to adopt a two pronged approach for the taxation of fringe benefits under the Income-Tax Act. Perquisites which can be directly attributed to the employees will continue to be taxed in their hands in accordance with the existing provisions of Section 17(2) of the Income-Tax Act and subject to the method of valuation outlined in Rule 3 of the Income-Tax Rules. In cases, where attribution of the personal benefit poses problems, or for some reasons, it is not feasible to tax the benefits in the hands of the employee, it is proposed to levy a separate tax known as the fringe benefit tax on the employer on the value of such benefits provided or deemed to have been provided to the employees
-.[273 ITR (St.)pp.196 & 197]

(iii) Finance Minister's speech while introducing amendments to Finance Bill,2005, on May 2,2005

'*Therefore, by the presumptive tax method what we are trying to do* **is to tax that part which is clearly a perquisite, clearly a benefit but which is going untaxed both in the hands** *of the employer and the employee'* [Emphasis provided] [144 Taxman (St.) p.121]

(iv) Finance Minister's speech relating to amendments to the Finance Bill, 2005, on 5.5.2005

'We have excluded a number of benefits which accrue to us. For example, canteen expenditure has been excluded, transport and travelling has been excluded. Even under the fringe benefit, as amended by Lok Sabha, we have taken care to exclude what I realized would be legitimate business expenditure and perhaps not amenable to the categorization, fringe benefit. What has been included is 'fringe benefit.'- [145 Taxman (St.) p.30]

Thus, FBT is being introduced in order to tax that part of expenditure incurred by the employer, which is clearly a perquisite or a benefit for the employees, but which is going untaxed both in the hands of the employer and the employee. Besides, the expenditure in question is apparently incurred for the purposes of the business of the employer but the same is considered to include, in a partial measure, a benefit of personal nature for the employees.

It may, therefore, be concluded that only that expenditure will fall within the ambit of FBT which results in some kind of a personal benefit or gain for the employees. All other expenses will remain outside the purview of FBT.

In the light of the aforesaid discussion the interpretation of the deemed fringe benefits under Section 115WB(2) of the Act, as provided in the aforesaid Circular is totally against and in conflict with the charging section as well as the object and purpose of FBT.

The height of absurdity is to be seen in the provisions wherein expenditure having absolutely no nexus with any benefit or gain to the employees, has also been held to be liable to FBT. The interpretation in respect of the computation of deemed fringe benefits is a totally unjust, unfair and unreasonable. Take for example a partnership firm in which there are several working partners but only one employee. The firm does not allow the use of cars to the employee, who uses his own two wheeler. The employee is never sent on any tour including foreign tours. All such tours are undertaken by the partners themselves. Then there are other expenses which are incurred in respect of the customers like gifts, etc. but nothing is given to the employee. In such a situation, if the interpretation provided in the Circular is to be followed, then 20 per cent of the expenditure on tours including foreign tours of the partners, 20 per cent of the expenditure on maintenance of cars of the firm and 50 per cent of the expenditure on gifts to the customers will be the value of fringe benefit on which FBT would be payable. This is a case where no fringe benefit is enjoyed by the employee or provided by the employer and even then the employer would be deemed to have provided fringe benefits to the employee and would be required to pay tax on the same. This could never have been intended. Many similar illustrations may be cited in order to prove that the so called presumptive method of computation of fringe benefits, as clarified in the aforesaid Circular is not only unjust, unfair and unreasonable but also totally against the object of the FBT and in conflict with the charging section. It is, thus, clear that there are absurdities galore in the provisions of FBT and more so in the aforesaid Circular, which ironically seeks to provide a harmonious, purposive and contextual interpretation of the provisions of FBT.

2. Scope of fringe benefits as laid down under Section 115WB of the Act

This is the most important part of this Article. Here, we have to consider the scope of the '*deemed fringe benefits*', as laid down under Section 115WB of the Act. For a number of reasons to be discussed hereinafter, no part of the expenditure, where from the employee does not derive any personal benefit or gain, can be treated as deemed DFB. Thus, any expenditure which is incurred by the employer, for legitimate business purposes, from which the employees do not derive any personal

benefit or gain, cannot be treated as expenditure for providing FB or DFB. This conclusion is based on the following reasoning:-

(i) As per the provisions of charging S.115WA(1) of the Act, there shall be charged additional income-tax referred to as FBT in respect of the FBs provided or deemed to have been provided by an employer to his employees.

This means that any expenditure which involves no personal benefit or gain for the employees, will not fall within the mischief of Section 115WA(1) of the Act. Thus, any expenditure incurred on persons other than employees, for the legitimate business purposes, will not be covered within the purview of fringe benefits or deemed fringe benefits as laid down under Section 115WB of the Act.

(ii) As per Section 115WB(1), for the purposes of Chapter XII-H, '*fringe benefits*' means any consideration for employment, provided by way of……etc.
This provision also clearly indicates that expenditure in question must be in consideration for employment and not otherwise.

(iii) Under Section 115WB(3), the privilege, service, facility or amenity does not include perquisites in respect of which tax is paid or payable by the employee.

It means that any expenditure which is taxed or taxable in the hands of the employee by way of perquisites, will not fall within the purview of the privilege, service, etc.

(iv) In order to find the legislative intent or ascertain the purpose behind the legislation, the speech made by the Finance Minister or the Mover of the Bill, can be taken into consideration, in view of the following judgements:-

(a) *Kerala State Industrial Development Corporation Ltd. Vs. CIT [2003] 259 ITR 51 (S.C.)*
(b) *Sole Trustee Loka Shikshana Trust Vs. CIT [1975] 101 ITR 234 (S.C.)*
(c) *K.P. Verghese Vs. I.T.O. [1981] 131 ITR 597 (S.C.)*

The Finance Minister in his speech while introducing the Finance Bill, 2005, has stated-
'*In addition I now propose that where the benefits are usually enjoyed collectively by the*

employees and cannot be attributed to individual employees, they shall be taxed in the hands of the employer'.

The aforesaid part of the speech of the Finance Minister clearly proves that the intent is to tax the benefits to the employees and therefore, the provision has to be interpreted to reflect the legislative intent and not to tax any expenditure on non-employees, which does not result in any personal benefit or gain to the employees.

(v) In case of doubt or difficulties, the Explanatory Memorandum to the Finance Bill, may be used to ascertain the intention of the Legislature, as laid down in *M. Rangaswamy Vs. CWT [1996] 221 ITR 39 (Mad.)*
In the Explanatory Memorandum to the Finance Bill, 2005, it is stated-

(a) 'This is so specially where the expenditure incurred by the employer is ostensibly for purposes of the business, but includes, **in partial measure***, a benefit of a personal nature'.*
[Emphasis added]

(b)'In cases where the attribution of personal benefit poses problems, or for some reasons, it is not feasible to tax the benefits in the hands of the employees, it is proposed to levy a separate tax known as the fringe benefit tax on the employer on the value of such benefits provided or deemed to have been provided to the employees'.
-[273 ITR (St.)pp.196, 197]

Thus, the FBT is proposed to be levied on the benefits to the employees and therefore, the DFBs cannot include expenditure on non-employees, which does not result in any benefit or gain to the employees.

(vi) The Finance Minister in his speech in the Parliament on 2.5.2005, has stated:
'FBT is a presumptive tax. As I said in my Budget speech, there are a large number of allowances, perquisites which are given, which go untaxed.....Therefore, by the presumptive tax method what we are trying to do is to tax that part which is clearly a perquisite, clearly a benefit but which is going untaxed both in the hands of the employer and employee'. [144 Taxman (St.)p. 121]

(vii) As is already clear, the very purpose of the provisions of Chapter XII-H, is to tax the untaxed FBs to the employees. To adopt a contrary view may result in a very heavy and unjust levy on the employer. It may result in the taxation of disproportionately high expenditure on non-employees, which does not involve any benefit or gain to the employees.

For example, if expenditure on use of hotel, boarding and lodging facilities is incurred only on customers and not on any of the employees, at all, then treatment of such an expenditure as a DFB will be totally unjust and absurd, because no benefit therefrom accrues to the employees.

There may be a case of a person who has no employees at all. For example, a partnership firm may be run by the partners themselves without the aid of any employee. It would, therefore, be totally unjust and absurd to levy any FBT on the so called DFBs, which do not involve any benefit or gain for the employees of the firm.

(viii) Besides, deeming provisions are required to be construed strictly as laid down in *CIT Vs. Khimji Nershi [1992] 194 ITR 192 (Bom.).* Therefore, the provisions relating to DFBs must be strictly construed to cover only those expenses, which involve any benefit or gain for the employees.

(ix) In addition, along with the introduction of FBT provisions-

(a) Section 17(2)(vi) has been amended with effect from AY2006-07, so as to provide that FBs chargeable to FBT under Chapter XII-H, will not be included as the income of employees by way of perquisite,

(b) Rule 3 of the Income-Tax Rules, 1962, has been amended in order to exempt certain perquisites from taxation.

(x) In this context, the answer to a question by the Finance Minister in an interview to 'Economic Times on 2.3.2005, is quite relevant. The relevant part of the interview is as follows:-

Q. The industry is looking for an assurance from you that no legitimate business expenses are taxed.

A. That I have made clear. My speech said only perquisites which are disguised as fringe benefits will be taxed. No legitimate business expenditure will be taxed.

From the aforesaid discussion it is quite clear that no part of the expenditure, wherefrom the employee does not derive any personal benefit or gain, can be subjected to FBT. Thus, any expenditure, which is incurred by the employer for legitimate business purposes, from which the employees do not derive any personal benefit or gain, cannot be treated as an expenditure incurred for providing FBs or DFBs.

In the light the aforesaid discussion, it is again quite clear that any expenditure incurred in respect of persons other than the employees will remain outside the purview of FBT.

3. Whether apportionment of expenditure is permissible

In case of composite expenditure i.e. expenditure jointly incurred on the employees as well as customers, etc., the total expenditure will have to be apportioned to ascertain the expenditure attributable to the employees and charge FBT on the same.

In this context, it has to be understood that the FBT has been introduced in the Income-Tax Act, in order to tax that **part of expenditure** which is clearly a benefit or gain for the employees but which is not taxed either in the hands of the employees or the employer. Take for example a case where after a business meeting with a customer, few employees also join the lunch or dinner arranged for the customer and his associates. Basically, the expenditure on lunch or dinner in respect of the employees, is also an expenditure for the purpose of the business of the employer and the same was allowable as such, so far. It is now considered that the expenditure incurred on lunch or dinner of the employees partly involves a personal benefit or gain for the employees. What part of such expenditure is attributable to such personal benefit or gain of the employees, is to be computed on presumptive basis. For instance, if such expenditure on lunch or dinner is Rs.1,000, and there are two persons on behalf of the customer and two employees. In such a situation expenditure on the lunch or dinner of the employees would be 50% of Rs.1,000 i.e. Rs.500. Then on presumptive basis the personal benefit or gain of the employees is computed at 20% of Rs.500, i.e. Rs.100. On the amount of Rs.100, additional tax by way of FBT @ 30% is to be charged in the hands of the employer. Thus, the FBT, payable by the employer would be Rs.30 plus surcharge and education cess.

Therefore, any composite expenditure, will have to be apportioned in order to ascertain the expenditure, which involves a personal benefit or gain for the employees. In support of such apportionment of the aforesaid expenses, reliance may be placed on the following judgements:

(i) CIT Vs. Mysore Minerals Ltd. [1986] 162 ITR 562 (Karn.)

(ii) CIT Vs. Expo Machinery Ltd. [1993] 190 ITR 576 (Del.)

4. Interpretation of the provisions of deemed fringe benefits in consonance with the object of the levy of FBT

As already pointed out, the expenditure under each of the sixteen (16) heads of expenditure, as specified in clauses (A) to (P) of Section 115WB(2), will have to be bifurcated in two parts, one part would represent only those items of expenditure under the relevant heads, which involve directly or indirectly some benefit or gain to the employees and the expenditure in this account / part would be the base for the purpose of Section 115WB(2) and 20 per cent of this expenditure, in relation to eleven (11) heads of expenditure would represent the value of fringe benefits under Section 115WC. The other part would represent that expenditure which is incurred on persons other than the employees and which does not result into any direct or indirect benefit or gain to the employees. This expenditure will remain totally outside the purview of FBT.

In this context a question may be raised as to why the Legislature should have provided for only 20 per cent of the expenditure which has been identified and isolated as expenditure representing some benefit or gain to the employees. The answer to this question is simple. All the expenditure incurred by an employer is for the purposes of his business. No employer will be foolish enough to incur an expenditure which is not for the purposes of his business. Here it may be said that certain expenses though incurred for the purposes of business, may incidentally result into some benefit or gain to the employees. It is for this reason that only 20 per cent of such expenditure is to be deemed as a fringe benefit on presumptive basis. In this context, the following part of the Explanatory Memorandum to the Finance Bill 2005, is relevant.

'This is so especially where the expenditure incurred by the employer is ostensibly for purposes of the business, but includes **in partial measure** *a benefit of a personal nature*.' [Emphasis added] – 273 ITR (St.) p.196.

Thus, it may be concluded that 80 per cent of such expenditure is meant for the purposes of business whereas 20 per cent thereof, goes by way of a benefit or gain to the employees.

There are other reasons for this conclusion which may be stated as follows-

(i) As per the charging Section 115WA(1), tax is to be charged *'in respect of fringe benefits provided or deemed to have been provided by an employer to his employees'* and therefore, all items of expenditure under various heads enumerated in Section 115WB(2) which do not involve any benefit or gain to the employees, should get excluded for the purpose of computing the chargeable value of fringe benefits and the provisions of Section 115WB(2) should be construed, accordingly.

(ii) As per Section 115WB(2), the fringe benefits shall be deemed to have been provided by the employer to the employees '*if the employer has, in the course of his business or profession, incurred any expense on or made any payment for the following purposes namely, (A)Entertainment……..*' In this sub-section, therefore, after the word '*incurred*' the words '*in providing any benefit to any employee*', should be implied. For this proposition, legal precedents have been cited *supra*.

(iii) As per Section 115WB(1), '*Fringe benefits*' mean any consideration for employment provided by the employer to his employees and therefore, an item of expenditure which does not involve any consideration for employment provided by the employer to the employees cannot be regarded as fringe benefit and on the basis of the same reasoning even for deemed fringe benefit, the particular item of expenditure must involve some benefit or gain to the employees, howsoever small it may be. In view of the aforesaid reason, the gross business expenditure under various heads enumerated in Section 115WB(2), cannot be regarded as base for computing the value of deemed fringe benefit under the various heads.

In the light of the aforesaid reasons, no FBT can be levied on expenditure incurred on persons not employed by the employer. For example expenditure incurred on the conference of agents or dealers, etc. will remain totally outside the ambit of FBT. Similarly, expenditure incurred by a firm on its partners in respect of travel, foreign tours, motor-cars and conveyance, etc. would not be treated as a fringe benefit liable to FBT. As a corollary, the words '*any person*', in Section 115WB(2)(B) should be construed as family member or a person closely related to the employee. Similarly, the word '*conference*' must be confined to such conferences in which employees have participated. Further, on the same lines, separate accounts should be maintained in respect of expenditure on sales promotion which involves any benefit to the employees or their family members and only this amount should be taken as base for computing the value of deemed fringe benefit. In sum and substance, only

expenditure which results into any benefit or gain to employees, should be segregated and used as the base for computing the value of deemed fringe benefits.

5. Relevant legal precedents regarding correct interpretation in respect of deemed fringe benefits

As already pointed out, the provisions relating to deemed fringe benefits, as interpreted in the aforesaid Circular, are unjust, unfair and unreasonable. This would affect their constitutional validity. In this context, it may also be considered whether it is necessary to read down the aforesaid provision so as to render them just, fair and reasonable.

In this context, there are a number of legal precedents which are relevant. The same are discussed as follows-

I. The object and purpose of the legislation must be the prime criterion for its interpretation

(i) In determining the legislative intent, the Court is required to consider three factors, viz. the context and the object of the statute, the nature and precise scope of the relevant provisions and the damage suffered not of the kind to be guarded against- *Rajkot Municipal Corporation Vs. Manjulben J. Nakum, (1997) 9SCC 552, 565.*

(ii) The task of interpretation of a statutory provision is an attempt to discover the intention of the Legislature from the language used – *CIT Vs. J.H. Gotla [1985] 156 ITR 323, 339 (S.C.)*

(iii) It must not be forgotten that the duty of the Court is to interpret the law made by the Legislature with a view to ascertaining its true interpretation and not to interpret it in a manner which may run counter to the legislative intent and purpose – *CIT Vs. Sterling Foods (Goa) [1995] 213 ITR 851,856-857(Bom.)*

This judgement has been approved by the Supreme Court in *CIT Vs. Relish Foods [1999] 237 ITR 59 (S.C.)*

(iv) The rule of reasonable construction must be applied while construing a statute. Literal construction should be avoided, if it defeats the manifest object and purpose of the Act – *Goodyear India Ltd. Vs. State of Haryana [1991] 188 ITR 402,440 (S.C.)*

II. The machinery sections must subserve the charging section

It is a settled law that distinction has to be made by Courts, while interpreting the provisions of taxing statute, between charging provisions which impose the charge to tax and machinery provision which provide the machinery for the levy and collection of tax so imposed. It is the duty of the Court while interpreting the machinery provisions of a taxing statute to give effect to its manifest purpose.

Further the machinery provisions should be interpreted liberally and generously so long as the principal object of the provision is not frustrated – *Fertilizer Corporation of India Ltd. Vs. State of Bihar [1988]68 STC 158,164 (S.C.).*

Besides, the principle governing the interpretation of a machinery provision is that interpretation or construction which makes the machinery workable, should be followed and the machinery sections should be so construed as to effectuate the charging section. *India United Mills Ltd. Vs. CEPT [1955] 27 ITR 20,25 (S.C.)*

In the light of the aforesaid principles of interpretation, the provisions of section 115WB(2), must subserve the provisions of section 115WA(1) of the Act.

III. Absurdities to be avoided

If strict literal construction leads to an absurd result, that is, a result not intended to be subserved by the object of the legislation ascertained from the scheme of the legislation, then, if another construction is possible apart from strict literal construction then that construction should be preferred to the strict literal construction – *CIT Vs. J.H. Gotla [1985] 156 ITR 323,339 (S.C.)*

Further, it is now a well settled rule of construction that where the plain literal interpretation of a statutory provision produces a manifestly absurd and unjust result which could never have been intended by the Legislature, the Court may modify the language used by the Legislature and even do some violence to it, so as to achieve the obvious intention of the Legislature and produce a rational construction – *CIT Vs. J.H. Gotla [1985] 156 ITR 323,339(SC)* and *Luke Vs. Inland Revenue Commissioners [1964] 54 ITR 692,709-710 (HL).*

The Court may also in such a case read into the statutory provision a condition which though not

expressed, is implicit as constituting the basic assumption underlying the statutory provision – *K.P. Varghese Vs. ITO [1981] 131 ITR 597,605-606 (S.C.).*

Besides, where a literal interpretation leads to absurd and unintended result, the language of the statute can be modified to accord with the intention of the Parliament and to avoid absurdity – *C.W.S.(India) Ltd. Vs. CIT [1994] 208 ITR 649,656(S.C.)*

From the aforesaid legal precedents, it is amply clear that the provisions of Section 112WB(2) relating to the computation of deemed fringe benefits, must be construed in accordance with the provisions of the charging Section as well as the intention of the Legislature enacting the provisions of FBT.

6. Items of income which are specifically exempt in the hands of the employees, are not liable to FBT

As per the aforesaid Circular of the CBDT, items which are exempt from tax in the hands of the employees like LTA, medical expenditure upto Rs.15,000 per annum and conveyance allowance, etc. have been held to be liable to FBT.

There are certain allowances provided to the employees and also certain specifically exempt perquisites, which are not liable to tax in the hands of the employees under Section 10 and Section 17(2) of the Act. Such items may be listed as follows-

(i)	Leave Travel Assistance	- Section 10(5), r.w.r. 2B
(ii)	House Rent Allowance	- Section 10 (13A), r.w.r. 2A
(iii)	Conveyance Allowance	-Section 10 (14)(i), r.w.r.2BB(1)
(iv)	Transport Allowance	- Section 10(14)(ii), r.w.r.2BB(2)
(v)	Expenditure on medical treatment	- Proviso to Section 17(2)(vi),r.w.r. 3A
(vi)	Transport services for workers and staff	- Explanation to S.17(2)(iii)

The aforesaid items could not be treated as liable to FBT, by any stretch of imagination. The reason for the same is that FBT has been introduced in order to tax the hitherto untaxed perquisites and not to tax the specific allowances and perquisites which has been specifically exempted from taxation in the hands of the employees. In other words, Chapter XII-H has not been introduced in order to bring to tax those items which have been specifically exempted under other provisions of the Act.

In this context, we may also rely on the Finance Minister's speech while introducing the Finance Bill 2005, as well as amendments thereto and also Explanatory Memorandum to the Finance Bill, 2005. The aforesaid speeches and Memorandum have already been discussed. At this stage, it will suffice if only the relevant parts thereof are referred to. The same are as follows-

(i) Finance Minister's Speech while introducing the Finance Bill 2005 [273 ITR(St.)p.56]

'In addition, I now propose that where the benefits are usually enjoyed collectively by the employees and cannot be attributed to individual employees, they shall be taxed in the hands of the employer'.

The aforesaid part of the Finance Minister's speech clearly indicates that any specific allowance to an employee or other such specific benefit, will not be covered under Chapter XII-H.

(ii) Explanatory Memorandum [273 ITR (St.) pp.196,197]

'Perquisites which can be directly attributed to the employees will continue to be taxed in their hands in accordance with the existing provisions of Section 17(2) of the Act.'

(iii) Finance Minister's speech while introducing amendments to Finance Bill, 2005 [144 Taxman (St.)p.121]

'*Therefore, by the presumptive tax method, what we are trying to do is to tax that part which is clearly a perquisite, clearly a benefit, but which is going untaxed both in the hands of the employer and the employee'.*

In the light of the aforesaid declarations and explanation, regarding the legislative intent behind the newly inserted Chapter XII-H, it may be safely concluded that allowances and other perquisites which are specifically covered or exempted under other provisions of the Income-tax Act, will not fall within the ambit of FBT.

In view of the aforesaid discussion, these items are dealt with as follows-

(i) Leave Travel Assistance (LTA)

LTA is specifically exempt under Section 10(5) of the Act. Otherwise also, at times a part of the LTA may be taxed, if the requisite conditions are not fulfilled.

Therefore, LTA is totally out of the purview of FBT.

(ii) House Rent Allowance (HRA)

In view of the reasons given for LTA, HRA is also outside the purview of FBT.

(iii) Conveyance Allowance

For the aforesaid reasons in (i), conveyance allowance is also out of the purview of FBT.

(iv) Transport Allowance

Transport allowance also is out of the purview of FBT, in view of the reasoning in aforesaid clause (i).

(v) Expenditure on medical treatment

Expenditure on medical treatment is exempt, vide proviso to Section 17(2)(vi) of the Act. Therefore, it will also not fall within the ambit of FBT.

(vi) Transport services for workers and staff – Explanation to Section 17(2)(iii)

As per Explanation to Section 17(2)(iii), the use of any vehicle by a company or an employer for journey by the assessee from his residence, to office or other place of work, or from such office or place to his residence, cannot be regarded as a benefit or amenity granted or provided to him free of cost or at a concessional rate, for the purposes of this sub-clause.

Thus, the expenditure on transport for workers and staff for commutation between office and residence has been specifically exempted from income-tax.

Besides, in this context, the relevant part of the Finance Minister's speech, 273 ITR(St.)p.56, may also be referred. The same is as follows-

'*However, transport services for workers and staff and canteen services in office or factory will be outside the tax net'.*

The Finance Minister has reiterated the aforesaid exclusions from the FBT in his speech relating to the amendments to Finance Bill, 2005, on 5.5.2005, 145 Taxman (St.) p.30. The relevant part thereof, is reproduced as follows:-

'*We have excluded a number of benefits which accrue to us. For example, canteen expenditure has been excluded, transport and travelling has been excluded'.*

In view of the aforesaid reasons, the transport services provided to the workers and staff for commutation between residence and office will be outside the purview of FBT.

In the light of the aforesaid discussion, the items of income which have been specifically exempted from taxation in the hands of the employees, under other provisions of the Act, cannot be subjected to FBT, by any stretch of imagination. Accordingly, the Explanatory Notes in the aforesaid Circular, are incorrect in that regard.

7. A Circular of the CBDT is not binding on the assessees / tax-payers

A Circular of the CBDT is not binding on the assessees / tax-payers. In this context, we would have to examine the provisions of Section 119(2) of the Act. The CBDT has been empowered under Section 119(1) of the Act to issue such orders, instructions and directions to other I.T. authorities as it may deem fit for the proper administration of this Act and such authorities and all other persons employed in the execution of this Act, are required to observe and follow such orders, instructions and directions of the CBDT. Under Section 119(2), however, it has been laid down that the Board may issue directions or instructions for the purpose of proper and efficient management of work of assessment and collection of revenue, **provided such directions or instructions are not prejudicial to the assessees**.

Therefore, any direction or instruction to be issued by the Board should not adversely affect the interests of the assessees or the tax-payers. If such directions are issued, then, they have to be held *ultra vires,* the scope of Section 119(2) of the Act. This proposition is supported by the judgement of Madras High Court in the case of *Madura Coats Vs. Dy. CIT [2005] 195 CTR 138 (Mad.).*

In view of the aforesaid reasons, the contents of the aforesaid Circular of the CBDT are not, at all, binding on the assessees / tax-payers.

The Gujarat High Court has admitted writ petitions against the legality of Circular No.8/2005, dated 29.8.2005, as published in '*Taxman*', Volume 148, Part –4, the Gujarat High Court has admitted two writ petitions challenging the validity and legality of Circular No.8/2005, dated 29.8.2005, issued by the CBDT in respect of FBT.

As an interim measure the Gujarat High Court has directed that the tax-payers may pay FBT as per their interpretations and in respect of disputed items of expenditure, the petitioners and other similar assessees may deposit disputed FBT liabilities in a separate bank account to be opened in their name in a schedule bank until further orders of the Court.

However, in the light of the aforesaid discussion in earlier paras, the tax-payers should pay FBT only as per the interpretation provided herein. This will be sufficient compliance with the provisions of the FBT.

8. The provisions of FBT are not applicable to guest house expenses

As already pointed out any expenditure incurred on persons other than employees of the tax-payer, will remain outside the purview of FBT.

Besides, any accommodation provided for the use of employees cannot be considered as a guest house and therefore, the expenses incurred on its maintenance cannot be deemed to be a fringe benefit for the levy of FBT.

In support of this proposition, the meaning of the term '*Guest house*', may be relied upon as explained in the followings judgements and dictionary-

(i) *CIT Vs. Parshwa Properties Ltd. [1987] 164 ITR 673 (Cal.)*
(ii) *CIT Vs. Aruna Sugars Ltd. [1980] 123 ITR 619 (Mad.)*
(iii) *The meaning of* '*Guest house*', *as per Oxford English Dictionary*

The fringe benefit tax,, in substance, is a tax on portion of deductible business expenditure. Such tax cannot be termed as tax on any income earned by the employer. It is not a tax on the income of the employee also.

As per Section 115WA(1), which is the charging section, there shall be charged additional income-tax(referred to as fringe benefit tax) in respect of fringe benefits provided or deemed to have been provided by an employer to his employees during the previous year at the rate of thirty per cent on the value of such fringe benefits. Thus, '*additional income-tax*', is only an ostensible name given to this new tax though the same is a tax on expenditure.

Any amount spent by the employer cannot be considered to be income of the employer, even if as a result of such expenditure, some benefit may accrue to the employers or any third party. Further, no tax can be imposed on benefits which are not ascertainable.

In this context, reference may be made to the judgement of the Apex Court in the case of *Union of India Vs. A. Sanyasi Rao & Ors. [1996] 219 ITR 330 (S.C.).* In this case, the non-obstante clause in Section 44AC, which had the effect of excluding the provisions of Sections 28 to 43C relating to regular assessments in cases falling under Section 44AC, providing for presumptive tax, was held to be unreasonable and accordingly, struck down. In the FBT provisions, no alternate method has been provided for calculating FBT on the basis of valuation of actual fringe benefits involved and segregated in the accounts. In view thereof, the presumptive valuation which has been made obligatory, would create extreme hardship in large number of cases and on this ground these provisions could be challenged as unreasonable and may be struck down.

In view of the aforesaid reasons, the validity of the FBT is quite doubtful.

9. Conclusion

In the light of the aforesaid detailed discussion, it may, *inter-alia,* be safely concluded that-

(i) No part of the expenditure which does not result into any personal benefit or gain for the employees, can be subjected to FBT. This will be so, irrespective of the Explanatory Note contained in Circular No.8/2005 of the CBDT.

(ii) The allowances and perquisites, which have been specifically exempted under other provisions of the I.T. Act, will not fall within the ambit of FBT.

(iii) The contents of the aforesaid Circular of the CBDT, are not binding on the assessees / tax-payers.

The employers, concerned, may arrange their affairs, accordingly.

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