

## **Impact of section 206AA on the rates of TDS**

**By S.K. Tyagi**

Recently, an Article was published in the Chartered Accountant's Journal dt. 9.3.2011, regarding the impact of the provisions of section 206AA, on the TDS rates under Chapter XVII-B of the Income-Tax Act, 1961 (the Act). In the aforesaid Article, the Author has expressed an erroneous view regarding TDS rates in respect of income chargeable under the head, "Salaries" as per section 192, r.w.s. 206AA of the Act. A number of my clients from Delhi sought my opinion in respect of the contents of the aforesaid Article.

In the aforesaid Article, the Author has given an opinion that the provisions of section 206AA of the Act, will apply even in cases where the income chargeable under the head, "Salaries" does not exceed the taxable limit. The aforesaid opinion of the Author is totally erroneous. I, accordingly, forwarded an opinion, dt. 23.3.2011, to all my clients.

In view of the aforesaid incorrect interpretation of the provisions of section 206AA of the Act, I thought of converting my aforesaid opinion into an Article, in order to provide correct interpretation of section 206AA, in relation to the provisions of TDS under Chapter XVII-B of the Act.

A new section 206AA was inserted in the Act, vide the Finance (No.2) Act, 2009. As per section 206AA, any person whose receipts are subject to deduction of tax at source (TDS), i.e. the tax-deductee shall mandatorily furnish his Permanent Account Number (PAN) to the tax-deductor, failing which the deductor shall deduct tax at source at higher of the following rates.

- (i) The rate prescribed in the Act ;
- (ii) At the rate in force i.e., the rate mentioned in the Finance Act ; or
- (iii) At the rate of twenty (20) per cent.

In the present context, it will be necessary to examine the provisions of section 206AA of the Act. For the sake of ready reference section 206AA of the Act, is reproduced as follows :

-----  
**206AA. Requirement to furnish Permanent Account Number.**

*(1) Notwithstanding anything contained in any other provisions of this Act, any person entitled to receive any sum or income or amount, on which tax is deductible under Chapter XVIIIB (hereafter referred to as deductee) shall furnish his Permanent Account Number to the person responsible for deducting such tax (hereafter referred to as deductor), failing which tax shall be deducted at the higher of the following rates, namely:—*

- (i) at the rate specified in the relevant provision of this Act; or*

- (ii) *at the rate or rates in force; or*
- (iii) *at the rate of twenty per cent.*
- (2) *No declaration under sub-section (1) or sub-section (1A) or sub-section (1C) of section 197A shall be valid unless the person furnishes his Permanent Account Number in such declaration.*
- (3) *In case any declaration becomes invalid under sub-section (2), the deductor shall deduct the tax at source in accordance with the provisions of sub-section (1).*
- (4) *No certificate under section 197 shall be granted unless the application made under that section contains the Permanent Account Number of the applicant.*
- (5) *The deductee shall furnish his Permanent Account Number to the deductor and both shall indicate the same in all the correspondence, bills, vouchers and other documents which are sent to each other.*
- (6) *Where the Permanent Account Number provided to the deductor is invalid or does not belong to the deductee, it shall be deemed that the deductee has not furnished his Permanent Account Number to the deductor and the provisions of sub-section (1) shall apply accordingly.*

-----

From the aforesaid provisions of section 206AA(1), it may be seen that any person entitled to receive any sum / income / amount, **on which tax is deductible under Chapter XVII-B**, shall furnish his PAN to the person responsible for deducting such tax, failing which tax shall be deducted at higher of the aforesaid rates. It is, thus, clear that the provisions of section 206AA will apply only in a case where the sum /income / amount receivable by the tax-deductee is liable to TDS, under any of the sections falling under Chapter XVII-B of the Act. **In other words, it clearly implies that section 206AA will not apply in a case where tax is not deductible at source.**

In the present context, we may also refer to the relevant part of Circular No.5 of 2010, dt. 3.6.2010, [324 ITR (St) 293], which contains Explanatory Notes to the provisions of Finance (No.2) Act, 2009. The provisions relating to the newly inserted section 206AA are explained in para 51 of the aforesaid Circular. For the sake of ready reference the aforesaid para 51 is reproduced as follows :

-----

**51. Improving compliance with provisions of quoting PAN through the TDS regime**

**51.1 Statutory provisions mandating quoting of Permanent Account Number (PAN) of deductees in Tax Deduction at Source (TDS) statements exist since 2001 duly backed by penal provisions.**

*The process of allotment of PAN has been streamlined so that over 75 lakh PANs are being allotted every year. Publicity campaigns for quoting of PAN are being run since the last three years.*

*51.2 The average time of allotment of PAN has come down to 10 calendar days. Therefore, non-availability of PAN has ceased to be an impediment. In a number of Explanatory Circular for Finance (No.2) Act, 2009 Page 56 of 63 cases, the non-quoting of PANs by deductees is creating problems in the processing of returns of income and in granting credit for tax at deducted at source, leading to delays in issue of refunds. In order to strengthen the PAN mechanism, a new section 206AA has been inserted in the Income Tax Act to provide that any person whose receipts are subject to deduction of tax at source i.e. the deductee, shall mandatorily furnish his PAN to the deductor failing which the deductor shall deduct tax at source at higher of the following rates:*

- (i) the rate prescribed in the Act;*
- (ii) at the rate in force i.e., the rate mentioned in the Finance Act; or*
- (iii) at the rate of 20 per cent.*

*51.3 TDS would be deductible at the above-mentioned rates will also apply in cases where the taxpayer files a declaration in form 15G or 15H (under section 197A) but does not provide his PAN. Further, no certificate under section 197 will be granted by the Assessing Officer unless the application contains the PAN of the applicant.*

*51.4 These provisions will also apply to non-residents where TDS is deductible on payments or credits made to them. To ensure that the deductor knows about the correct PAN of the deductee, it is provided that both the deductor and deductee will mandatorily quote PAN of the deductee in all correspondence, bills and vouchers exchanged between them.*

*51.5 Applicability - This amendment has been made applicable with effect from 1<sup>st</sup> April, 2010 and will accordingly apply in relation to assessment year 2011-12 and subsequent assessment years.*

-----

From the Explanatory Notes, in para 51.2 of the aforesaid Circular, it may be seen that section 206AA has been inserted in the Act in order to provide that any person whose receipts are subject to deduction of tax at source, shall mandatorily furnish his PAN to the tax-deductor and in case of failure to furnish the PAN to the tax-deductor, the tax will be required to be deducted at source at higher of the aforesaid three rates. Thus, from para 51.2 of the aforesaid Circular, also, it is clear that section 206AA will apply in respect of a person whose receipts are subject to TDS.

In the present context, it will be very relevant to refer to the charging section for TDS, viz. section 4(2) of the Act. In the present context, it will be necessary to examine the provisions of section 4 of the Act. For the sake of ready reference, section 4 of the Act, is reproduced as follows :

-----  
**4. Charge of income-tax.**

*(1) Where any Central Act enacts that income-tax shall be charged for any assessment year at any rate or rates, income-tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions (including provisions for the levy of additional income-tax) of, this Act in respect of the total income of the previous year of every person :*

***Provided** that where by virtue of any provision of this Act income-tax is to be charged in respect of the income of a period other than the previous year, income-tax shall be charged accordingly.*

*(2) In respect of income chargeable under sub-section (1), income-tax shall be deducted at the source or paid in advance, where it is so deductible or payable under any provision of this Act.*

-----  
 From the aforesaid provisions of section 4(1), it may be seen that income-tax shall be charged on the total income of the previous year of every person, at the rates provided in the Finance Act. Thus, total income is the tax base. Therefore, if the total income is below taxable limit, then no income-tax will be chargeable.

As per section 4(2) in respect of income chargeable under section 4(1), income-tax shall be deducted at source or paid in advance, where it is so deductible or payable under any provisions of the Act. It will, therefore, clearly imply that no tax will be deductible at source in a case where the total income is below taxable limit.

*We may now examine the impact of the provisions of section 206AA of the Act, on the TDS rates as provided under Chapter XVII-B of the Act.*

In order to examine the implications of the provisions of section 206AA in respect of the various TDS provisions under Chapter XVII-B of the Act, it would be necessary to broadly examine the provisions of sections 192 to 196D of the Act.

As regard the aforesaid sections 192 to 196D, the same may be divided into three categories, viz.

- (i) Section 192, which relates to TDS from income under the head, “*Salaries*”
- (ii) Sections where TDS is applicable only in case the income / sum / amount payable during the financial year exceeds certain amount specified there under; e.g. sections 194C, 194-I, 194J, etc.
- (iii) Sections where tax is deductible at source in respect of any income / sum / amount payable during the financial year without reference to any limit in respect thereof, e.g. sections 194E, 194F, 195, 196B, 196C, 196D, etc.

The impact of the provisions of section 206AA on the aforesaid categories of sections under Chapter XVII-B of the Act, is discussed as follows :

### **1. TDS under section 192 in respect of income from salaries**

The provisions of section 192 in relation to TDS from income under the head “*Salries*” are quite unique and different from the provisions under other sections falling within Chapter XVII-B of the Act. The reason for the same is that TDS under section 192 is deductible on the estimated income of the assessee under the head “*Salaries*”, for the relevant previous year / financial year.

It may be seen from the provisions of section 192 that as per sub-section (2), there is a provision for taking into consideration the salary received by an employee from other employer also, during the relevant financial year, for the purposes of TDS under section 192(1) of the Act. In addition under sub-section (2B) at the option of the employee, the income of the employee under other heads of income may also be taken into consideration for the purpose of computing TDS under section 192 of the Act. Further, vide sub-section (3) there is a provision for adjustment for excess or deficit of TDS.

It is in view of the aforesaid unique provisions of section 192(1) that the tax is computed on the estimated income under the head “*Salaries*”, as if that is the total income of the employee for the relevant financial year and accordingly, tax is calculated on the basis of slab rates applicable in respect of individuals. In the light of the aforesaid reasons, no tax is deductible at source under section 192(1), if the estimated income under the head “*Salaries*” for the relevant financial year is below taxable limit. In other words no tax is deductible at source under section 192(1), if the income from salaries for the relevant financial year is below taxable limit.

If we now look at the provisions of section 206AA, it would clearly imply that the provisions of section 206AA will not apply if the income under the head “*Salaries*” for the relevant financial year is below taxable limit.

In order to make the position absolutely clear in this regard, it would be appropriate to refer to Circular No.8 of 2010, dt.13.12.2010, issued by the CBDT [330 ITR (St) 22]. The aforesaid

Circular relates to – *Income-tax deduction from salaries during the financial year (FY) 2010-11, under section 192 of the Income-Tax Act, 1961.*

Para (3) of the aforesaid Circular deals with : *Broad scheme of tax deduction at source from “Salaries”*. Further, para 3.1 thereof, deals with “*Method of tax calculation*”. For the sake of ready reference, the aforesaid para 3.1 is reproduced as follows :

-----

### 3.1. *Method of tax calculation*

*Every person who is responsible for paying any income chargeable under the head “Salaries” shall deduct income-tax on the estimated income of the assessee under the head “Salaries” for the financial year 2010-11. The income-tax is required to be calculated on the basis of the rates given above subject to provisions of section 206AA of the Income-tax Act and shall be deducted at the time of each payment. **No tax will, however, be required to be deducted at source in any case unless the estimated salary income including the value of perquisites, for the financial year exceeds Rs. 1,60,000 or Rs. 1,90,000 or Rs. 2,40,000, as the case may be, depending upon the gender and age of the employee.** (Emphasis added)*

-----

From the aforesaid para 3.1 relating to method of tax calculation, it may be seen that the income-tax deductible at source under section 192, in respect of salaries, is required to be calculated on the basis of the rates given earlier, subject to the provisions of section 206AA of the Act. **However, thereafter, it is clarified that no tax will be required to be deducted at source in any case unless the estimated salary income, including the value of perquisites, for the financial year exceeds the taxable limit.**

In this connection, we may also refer to para 4.8 of the aforesaid Circular, which specifically deals with section 206AA. For the sake of ready reference, the aforesaid para 4.8 is reproduced as follows :

-----

### 4.8 *Section 206AA*

4.8.1. *Finance (No.2) Act, 2009, w.e.f. 1.04.2010 has inserted section 206AA in the Income-tax Act which makes furnishing of PAN by the employee compulsory in case of payments liable to TDS. If employee (deductee) fails to furnish his / her PAN to the deductor, the deductor shall make TDS at a higher of the following rates :*

- i. *at the rate specified in the relevant provision of this Act; or*

ii. at the rate or rates in force; or

iii. at the rate of twenty per cent.

4.8.2. The deductor has to determine the tax amount in all the three conditions and apply the higher rate of TDS. **This section applies to any person entitled to receive any sum or income or amount, on which tax is deductible under Chapter XVII-B of the Income-tax Act.** As Chapter XVII-B covers all payments including salaries, salaries are also covered by section 206AA. In case of salaries there can be following situations :

- (a) Where the income of the employee computed for TDS under section 192 is below taxable limit.
- (b) Where the income of the employee computed for TDS under section 192 is above taxable limit.

***In first situation, as the tax is not liable to be deducted, no tax will be deducted.*** In the second case, if PAN is not furnished by the employee, the deductor will calculate the average rate of income-tax, based on rates in force as provided in section 192. If the tax so calculated is below 20 per cent., deduction of tax will be made at the rate of 20 per cent. and in case the average rate exceeds 20 per cent., tax is to be deducted at the average rate. Education cess at 2 per cent, and Secondary and Higher Education Cess at 1 per cent. is not to be deducted, in case the TDS is deducted at 20 per cent. under section 206AA of the Income-tax Act. ( Emphasis added )

-----  
From the aforesaid para 4.8.2, it may be seen that in case of salaries there can be the following two situations :

- (a) Where the income of the employee computed for TDS under section 192 is below taxable limit.
- (b) Where the income of the employee computed for TDS under section 192 is above taxable limit.

**It has been specifically stated in the aforesaid situation (a) that as the tax is not liable to be deducted, no tax will be deducted.** In other words, where the income of the employee computed for TDS under section 192 is below taxable limit, no tax will be required to be deducted at source, even if the employee does not furnish his PAN to the employer.

**2. Sections where TDS is applicable only in case the income / sum / amount payable during the financial year exceeds certain amount specified there under**

We may now refer to second category of sections under Chapter XVII-B. These are the sections where tax is deductible at source only if the income / sum / amount payable during the financial year, exceeds an amount specified there under, e.g.

- (i) Under section 194C, no tax is deductible at source if the sum payable does not exceed ₹ 30,000.
- (ii) Under section 194-I, no tax is deductible at source where the amount of such income or the aggregate amount of such an income payable during the financial year does not exceed ₹ 1.8 lakhs; and
- (iii) Similarly under section 194J, no tax will be deductible at source, where the amount payable during the financial year, does not exceed ₹ 30,000.

Therefore, the provisions of section 206AA will not apply if the amount payable does not exceed the limit specified under the aforesaid sections. In other words, if on any income / sum / amount no tax is deductible at source under Chapter XVII-B of the Act, then the provisions of section 206AA will not be attracted and accordingly, no tax will be required to be deducted at source, even if the payee does not furnish his PAN to the payer.

If on the other hand, tax is deductible at source on the income / sum / amount payable and the payee does not furnish his PAN to the payer, then the tax will be deductible at source at the higher of the following rates, namely :

- (i) At the rate specified in the relevant provision of the Act; or
- (ii) At the rate or rates in force, i.e. the rate mentioned in the Finance Act ; or
- (iii) At the rate of twenty (20) per cent.

**3. Sections where tax is deductible at source in respect of any income / sum / amount payable during the financial year without reference to any limit in respect thereof.**

We may now refer to the third category of sections under Chapter XVII-B. These are the sections where tax is deductible at source without any reference to any limit in respect of the income / sum / amount, e.g.

- (i) Under section 194E, which relates to payments to non-resident sportsmen, etc., tax is deductible at source from any income payable, without reference to any monetary limit in respect thereof.

- (ii) Similarly under section 195, tax is deductible at source in respect of any payment to a non-resident or a foreign company by way of interest or any other sum chargeable under the provisions of the Act, without reference to any monetary limit in respect thereof.

In this regard, it has to be clearly understood that tax is deductible under section 195 of the Act, only if the payment by way of interest or any other sum, is chargeable under the provisions of the Act. In other words, if the aforesaid interest or any other sum is not chargeable to tax under the Act, then the provisions of section 206AA will not apply.

*In this connection please also refer to my Article under the title “A non-resident is not under an obligation to apply for PAN, for TDS purposes, as per section 206AA”, published in 324 ITR (Jour) p.1.*

- (iii) Similarly under section 196B, tax is deductible at source in respect of income from units without reference to any monetary limit in respect thereof.

Therefore, the provisions of section 206AA will be attracted in respect of the aforesaid TDS provisions, if the payee does not furnish his PAN to the payer of income / sum / amount.

In other words, if in respect of income / sum / amount falling under any of the aforesaid sections of Chapter XVII-B, the payee does not furnish his PAN to the payer, then the provisions of section 206AA will be attracted and accordingly, tax will be deductible at source at higher of the following rates, namely:

- (i) At the rate specified in the relevant provision of the Act, or
- (ii) At the rate or rates in force, i.e. the rate mentioned in the Finance Act ;or
- (iii) At the rate of twenty (20) per cent

#### **4. Conclusion**

In the light of the discussion in the preceding paras, it may be concluded that :

- (i) The provisions of section 206AA of the Act will not apply in respect of TDS under section 192, where the income of the employee computed for TDS purposes is below taxable limit.

In other words, no tax will be required to be deducted at source under section 192, r.w.s. 206AA of the Act, where the income of the employee computed for TDS purposes, is below taxable limit, even if the employee does not furnish his PAN to the employer.

- (ii) As regards the second category of sections falling under Chapter XVII-B, the provisions of section 206AA will not apply if the payment in respect of income / sum / amount, made during the financial year is below the limit specified there under.

For example, the provisions of section 206AA will not apply if the payment falling within the purview of section 194J, does not exceed ₹ 30,000.

In other words, no tax will be required to be deducted under section 194J, r.w.s. 206AA of the Act, where the income of the payee is less than ₹ 30,000, even if the payee does not furnish his PAN to the payer.

- (iii) As regards the third category of sections falling under Chapter XVII-B, tax is deductible at source there under without any reference to any limit in respect of the income / sum / amount payable during the financial year.

Therefore, provisions of section 206AA will come into play if the payee does not furnish his PAN to the payer in respect of income / sum / amount falling within the purview of the third category of sections under Chapter XVII-B of the Act.

---

<b>S.K.TYAGI</b>	☎ Office	: (020) 26133012	Flat No.2, (First floor)
M.Sc., L.L.B., <b>Advocate</b>		: (020) 40024949	Gurudatta Avenue
Ex-Indian Revenue Service	Residence	: (020) 40044332	Popular Heights Road
<b>Income-Tax Advisor</b>	Email	: sktyagidt@airtelmail.in	Koregaon Park
			PUNE-411 001

---