

TDS on payment to contractors

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The meaning of Contractor and Sub-contractor

The contractor refers to any person who enters into a contract for a fixed price to carry out any work including the supply of labour for performing any work. The sub-contractor refers to any person who enters into a contract with the contractor for performing whole or part of the job

Who is Liable to Deduct TDS

(i) On Payments to Contractor

Any person (except an individual or HUF) who makes payment to a resident contractor is liable to deduct TDS.

(ii) On Payment to Sub-Contractor

Any resident contractor (except an individual or HUF) who makes payment to a resident sub-contractor, is liable to deduct TDS.

Proposed amendment:

That an individual or an HUF whose gross receipts or turnover in business are more than the monetary limit under Section 44AB (i.e., 40 lakh) shall be liable to deduct income tax under the relevant provisions of Sections 194A, 194C, 194H, 194I and 194J (w.e.f. 1.6.2002).

When Liability to Deduct TDS arises

(a) In case of payments to contractors

The payer is liable to deduct TDS on satisfaction of following conditions:

- (i) The contractor must be resident in India. In case of non-resident contractors, liability to deduct TDS will be as per section 195. (See relevant chapter).
- (ii) Payment should be made by any of the specified persons.
- (iii) Payment is to be made in pursuance of an oral or written contract.
- (iv) Consideration for each contract exceeds Rs. 20,000/-
- (v) In case the contract is expected not to exceed Rs. 20,000 but later on it exceeds Rs. 20,000 then TDS shall be deducted for earlier amount also.

(b) In case of payments to sub-contractors

A contractor is liable to deduct TDS on satisfaction of the following conditions :

- (i) The sub-contractor is resident in India.
- (ii) The contractor is a person other than individual or HUF.
- (iii) Payment is made for sub-contracting the whole or part of work including supply of labour.
- (iv) The consideration for each contract exceeds Rs. 20,000/-

Instance when there is no liability to deduct TDS

If the payee is the Central Government, State Government, the Reserve Bank of India, any corporation established under Central or State Act or any notified Mutual Fund, the payer shall not deduct TDS.

When TDS is to be Deducted

The payer, that is the person responsible for making the payment, shall deduct TDS either at the time of crediting such sum to the account of the payee or to 'Suspense Account' or at the time of payment, whichever is earlier.

Analytical application

1. Section 194C(1) clearly provides that TDS shall be deducted from any sum paid to the contractor. It is obvious, therefore that the requisite deduction is not to be made on any income for the contractor but is to be made on the sum paid for carrying out any work.

2. TDS on advance payments :

Where a contractor is paid an amount as advance towards a contract undertaken by him. TDS shall be deducted at the time of payment. The amount of TDS on advance payments shall be calculated as under :

$$\text{TDS} = \text{Amount of advance} \times \{100/100(-) \text{ rate of TDS}\} - \text{Amount of advance.}$$

3. When payment for each contract Exceeds Rs. 20,000

The liability to deduct TDS u/s 194C arises, if the payment made/to be made under a contract exceeds Rs. 20,000. In this connection, the CBDT has clarified vide Circular No. 93, dated 26.09.1972, that where payments are made under several contracts during a financial year and the total payments made exceeds Rs. 20,000 but the consideration for any individual contract does not exceed Rs. 20,000, the liability to deduct TDS shall not arise.

It was further clarified that if the total payment under the contract is likely to exceed Rs. 20,000 for the entire period during which the contract will remain in force income-tax will have to be deducted at source.

In a case where, at the time when contract was entered into, it was expected that the total payment thereunder would not exceed Rs. 20,000 but later on it is found that the payment exceeds that amount then deduction should be made in respect of earlier payments as well.

Situation 1: What if a person is given various contracts of work over a period of time on a continuous basis and (i) the value of an individual contract may or may not exceed Rs. 20,000. (ii) the value of an individual contract exceeds Rs. 20,000?

Opinion : TDS is to be deducted only from those contracts whose individual value exceeds Rs. 20,000.

Situation 2 : What if it is difficult to ascertain and establish when a contract ends and when a new contract begins since the work is being given on continuous basis.

Opinion : Under such circumstances, two individual contracts are generally distinguished on the basis of bills issued by the contractor.

Generally, when a work/contract is complete, the contractor will issue a bill. For example, when a printer is assigned a contract to print a book, he will issue a bill immediately after completion of printing of the book. In such case that bill will represent a separate contract, and if the bill amount exceeds Rs. 20,000, TDS will have to be deducted. But if the printer makes a consolidated bill for printing of different books, the job of printing each book will be a separate contract and TDS will be deducted only if the printing charges for any book exceed Rs. 20,000.

Situation 3: What if the contractor draws intermediate/provisional bill(s) and a final bill in the end?

Opinion : In such cases, the individual contract cannot be identified from the bills. Only after the work is complete, the final bill amount shall be relevant for consideration.

General Practice : Since the distinction of individual contracts is essential for the purpose of deducting TDS and the same is not easy as it will depend on the facts and circumstances of each case, practically when the total value of work done in a year exceeds Rs. 20,000, TDS is to be deducted on the entire sum, irrespective of whether the value under each contract exceeds Rs. 20,000 or not. This practice, though not in strict compliance of the law, is taken as convenient to all.

Caution : Any deliberate attempt to split a larger contract for single work in order to circumvent the provisions of TDS shall be construed as irregular and might attract penalty.