

Deductibility of Provident Fund Contributions Under Income Tax Act

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< EXECUTIVE SUMMARY >

◆ Provident Fund contributions constitute one of the major items of expenditure in a business house and hence the various aspects relating to its deductibility for the purpose of Income Tax Act is of great significance. The author in the article below envisages the various cases where the interpretation of the

statute regarding the deductibility of the Provident Fund Expenditure is not clear. The article also explains the concepts of the terms 'due date' & 'month' in relation to Provident fund which are of utmost significance for the interpretation of the related provisions of the Income Tax Act.



rovident Fund contributions constitute one of the major items of expenditure in a business house and so various aspects relating to its deductibility for the purpose of Income Tax Act is of great significance. Before discussing on the subject, it is better first to summarise relevant provisions of Income Tax Act as follows:-

1. Regarding employer's contribution to Provident Fund:-

Employer's contribution to Provident Fund is deductible subject to prescribed limits if the same is paid on or before the "due date" by which the assessee is required as an employer to credit an employee's contribution to the employee's account in the relevant fund under any Act or rule or otherwise, and where such payment has been made otherwise than in cash, the sum has

been realised within fifteen days from the due date. [Section 36(1)(iv) read with Section 43B].

2. Regarding employees' contribution to Provident Fund:-

- (i) Any sum received by the assessee from its employees as contributions to Provident Fund is treated as an income u/s. 2(24)(x).
- (ii) The deduction for payment of employees' contribution can be claimed by virtue of Section 36(1)(va) according to which it is deductible if such sum is credited by the assessee to employee's account in the relevant fund under any Act or rule or otherwise on or before the "due date".

Thus, it is clear that both employer's and employees' contributions are deductible if paid by the assessee on or before "due date" under relevant Act or rule. Let us discuss as to what is "due date" under Provident Fund law.

"Due Date" for the purpose of payment of Provident Fund Contributions:-

For determining "due date" for payment of

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Provident Fund contributions, clause (1) of Paragraph 38 of Employees' Provident Fund Scheme, 1952 is relevant. It reads as follows:-

"The employer shall, **before paying** the member his wages in respect of **any period or part of period** for which contribution are payable, **deduct the employee's contribution** from his wages which **together with his own contribution** as well as an administrative charge of such percentage [of the pay (basic wages, dearness allowance, retaining allowance, if any, and cash value of food concessions admissible thereon) for the time being payable to the employees other than an excluded employee and in respect of which provident fund contributions are payable, as the Central Government may fix], he shall **within fifteen days of the close of every month** pay the same to the Fund by separate Bank drafts or cheques on account of contributions and administrative charge."

It has been held in:-

(a) Fluid Air (India) Ltd. Vs. D.C.I.T. (1997) 63 ITD 182 (Mumbai)

and

(b) Madras Radiators & Pressings Ltd. Vs. D.C.I.T. (1996) 59 ITD 515 (Mad.) / (1996) 56 TTJ (Mad.) 662

that the term "month" has not been defined in the Scheme, there is ambiguity regarding interpretation of the words "fifteen days from the close of month" appearing in Paragraph 38 of Employees' Provident Fund Scheme as to whether it should be reckoned from the month in which such contributions are received by the assessee from its employees or from the month in respect of which such contributions are received by the assessee, in cases where wages are paid in subsequent month(s), and this ambiguity should be resolved in favour of assessee, i.e. fifteen days are to be reckoned from close of the month in which employees contributions are recovered i.e. the month of payment of wages.

With due respect to above decisions, in my opinion, there is no such ambiguity. Proper analysis of Paragraph 38 of E.P.F. Scheme reveals as follows:-

(i) Employer's liability to deduct employee's contribution arises before paying wages to employees (and not as and when wages are earned by employees) in respect of **any period or part of period**. Thus the employees' contribution comes in the hands of the employer during the wage disbursement month and not during the wage period (which may be a calendar month or any other period and not necessarily a period equal to one month.)

(ii) Employees' contribution thus deducted is to be deposited together with employer's contribution within 15 days of the close of month.

Thus, if both employees' and employer's contributions for Provident Fund is made within 15 days of the close of month in which wages are paid, it will be within due date. So, relevant month to be considered for determining due date is payment month i.e. wages disbursement month and not month or period to which wages relate.

Otherwise also, any other interpretation would produce absurd results in following cases:-

1. Where wage-period is not month. It may be weekly or daily and may cover portions of two months.
2. Where due to lock-out or strike or due to natural calamities or financial stringency, wages are paid after return of the situation to normalcy.
3. Increment in wages is effected with retrospective effect.

The view that payment month is relevant for considering due date for payment of Provident Fund contribution is also supported by Calcutta Tribunal 'E' Bench's decision dated 28-5-2001 rendered in the case of Kanoi Paper & Industries Ltd., Calcutta Vs. ACIT, Co. Circle 7(2), Calcutta [ITA No.1260(Cal) of 1996], an unreported decision till the date of this write-up, which held in para 6 of its order as follows:-

"Clause 38 of the Employees' Provident Fund Scheme, 1952, fixes the time limit for making payment in respect of contribution to the provident fund to be 15 days from the close of the month concerned. However, the issue here is whether the "month" should be considered to be the month to which the wages relates or the month in which the actual disbursement of the wages is made. We are of the considered opinion that the expression "month" should mean here the month during which the wages/ salary is actually disbursed irrespective of the month to which the same relates. Thus, the scheme of the Govt. in this regard is that once a deduction is made in respect of the employees' contribution to the provident fund from the salary/ wages of the employee or the employer also makes his contribution, factually at the time of disbursement of the salary the payment in respect of such contribution should be made forth with. If for some reason or other the payment of salary for a particular month be held up for considerable period of time it cannot be said that the employer would be liable to make

payments in respect of the "employer's" as well as "employees" contribution in respect of wages for such period within a period of 15 days from the close of the month to which the wages relates. On the other hand, in our view, most appropriate interpretation would be that the employer' **would be at liberty to make payment of the contribution concerned within 15 days (subject however to the further grace period) from the end of the month during which the disbursement of the salary is actually made and the contribution of the provident fund are, thus, generated."**

Since the due date has to be determined under the provisions of the Employees Provident Fund & Misc. Provisions Act 1952, let us examine some other provisions of E.P.F. Scheme framed under the said Act.

While returns and forms are required to be filed with reference to the month (meaning calendar month as per provisions of the General Clauses Act), or currency period (referring to period of financial year of Government i.e. period commencing in April and ending in March next), mention of wage period(s) is required specifically. Form No.12 is captioned as follows:-

"Statement of Contributions for the month of19....

Wage Period from to"

Form No.3A on annual contribution card requires tabulation of date for the currency period on calendar-monthly basis and the first month mentioned is

"March paid in April".

The last month mentioned is

"February paid in March".

The intention is apparent that wages paid between April to March and contributions deducted therefrom are to be reported in this form, although the wages may relate to any period from March to February next.

In Form No.12A(revised), monthly statement of contributions requires report on amount of contribution "recovered from the workers". As per paragraph 38, recovery of contributions can be made only at the time of disbursement of wages. Thus the data required to be produced should relate to the payment-month irrespective of the wage period.

Also, five days of grace period has been allowed to employers for payment of Provident Fund contributions by clause (iii) of CPFC'S Circular No.E.128(1) 60-III dated 19-3-1964 as modified by circular No.E11/128 (section 14-B Amendment)/73 dated 24-10-1973.

CONCLUSION REGARDING ISSUE OF 'DUE DATE':

Due date for payment of Provident Fund contributions is 15 days from the end of month in which wages are paid (plus grace period of 5 days). Thus, if wages pertaining to April' 2003 is paid on, say, 7th May' 2003, due date for payment of Provident Fund contribution is 20th June' 2003 [i.e. 15th June' 2003 as increased by grace period of 5 days].

EMPLOYER'S CONTRIBUTION TO PROVIDENT FUND PAID IN NEXT FINANCIAL YEAR BUT WITHIN DUE DATE

This issue may be discussed with the help of an illustration. Suppose wages for the month of March' 2002 is paid on last day of the month i.e. 31-3-2003, so, due date for payment of provident fund contribution will be 20-4-2003 [i.e. 15-4-2003 + 5 days grace period]. Now, if provident fund contribution is paid on 20th April' 2003, it is within due date and hence deductible, but the question is whether it is deductible in Assessment Year 2003-04 or in 2004-05. Let us look at second proviso to section 43B which is relevant here which states that the deduction is to be allowed if paid on or before due date. Upto 31-3-1989, the proviso so required payment on or before the due date during the previous year. The words "during the previous year" were omitted w.e.f. 1-4-1989 from second proviso to section 43B which is a notable omission. It can therefore be said that employer's contributions paid on next year but within due date is deductible in the year to which it relates. In the illustration cited above, it is deductible in the Assessment Year 2003-04. In *Travancore Titanium Products Ltd. Vs. D.C.I.T. 57 ITD 16 (Cochin)* and *Fluid Air (India) Ltd. Vs. DCIT 63 ITD 183 (Mumbai)*, the Hon'ble Tribunals also hold the same view. The literal construction of Sec. 43B(1) providing for allowance only in computing the income of that previous year in which such sum is actually paid by an assessee subject again to the further requirement of payment within due date is therefore not to be preferred.

I also take the opportunity to discuss about Gauhati High Court's recent ruling in *CIT Vs. Assam Tribune* reported in (2002) 253 ITR 93, wherein, following its earlier ruling in *CIT Vs. Bharat Bamboo And Timber Suppliers (1996) 219 ITR 212*, it held that where the contribution towards provident fund, etc. has been paid before the filing of the return by the assessee, the amounts

would be deductible. The point to note here is that the issue in Bharat Bamboo And Timber Suppliers's case (supra) was deduction of Sales Tax paid after close of accounting year but before due date for filing of return of income in view of the Explanation 2 to Section 43B. Explanation 2 deals with clause (a) of Section 43B which is applicable to payment of tax, duty, cess or fee and not with clause (b) of Section 43B dealing with employer's contribution to provident fund. Therefore, with due respect to Hon'ble High Court, in my opinion, decision in Assam Tribune's case (supra) requires reconsideration.

It is also relevant to discuss about Kerala High Court's decision in Kerala State Financial Enterprises Ltd. V. CIT 225 ITR 999, wherein it was held that for claiming deduction for provident fund contributions, year of payment is relevant and not year for which contributions are payable. This case related to Assessment Year 1995-96 when second proviso to Section 43B was not available in the statute. So this decisions seems to be not applicable after amendment in Section 43B by insertion of provisos to it.

EMPLOYEES' CONTRIBUTION TO PROVIDENT FUND PAID IN NEXT YEAR BUT WITHIN DUE DATE:-

The only requirement for deductibility of employees contribution as mentioned in Section 36(1) (va) is its payment with due date. So, if wages for March 2003 is paid on 31st March 2003 and the corresponding employees contributions is paid on April, 2003 before its due date on 20-4-2003, employees contribution is treated as income of assessment year 2003-04 and is also deductible in Assessment year 2003-04, if the wages for March 2003 is paid in April 2003, the employees contribution is realised in financial year 2002-03 and accordingly it will be income u/s 2(24)(x) in assessment year 2003-04. In that view of the matter, in such a case, payment of employees contribution to Provident Fund will be an expense allowable in assessment year 2003-04. In any case, it is notable that Section 43B is not applicable to payment of Employees contributions to Provident Fund, because Sec. 43B encompasses only sums payable by the employer as his contribution to provident Fund and other funds specified therein.

DEDUCTIBILITY OF PROVIDENT FUND IN CASE OF FEW DAYS DELAY

Now, the issue to be discussed is where there is only few days delay in deposit of Provident Fund contribu-

tions and that too not without reasonable cause, whether their deductibility is lost forever. If the reply is in affirmative, it will be against the intention of the legislature. As per CBDT Circular No. 372 dated 8-12-83, the intention of Sec. 43-B is to thwart claims for deductions although payments of taxes, duties, P.F. etc. are not made. So, deductibility of Provident Fund contributions should not be denied forever just for few days delay in its payment backed by some reasonable cause. It has been held in following cases **that for all payment of provident fund contributions made within the accounting year, deduction ought to be allowed** despite few days delay:-

- (i) Hunsur Plywood Works Ltd. Vs. D.C.I.T. (1995) 54 ITD 394 (Bang.)/(1996) 54 TTJ (Bang) 260.
- (ii) Fluid Air (India) Ltd. Vs. D.C.I.T. (1997) 63 ITD 182 (Mumbai)
- (iii) Madras Radiators & Pressings Ltd. Vs. D.C.I.T. (1996) 59 ITD 515 (Mad.)/(1996) 56 TTJ (Mad.) 662.
- (iv) D.C.I.T. Vs. Udaipur distillery Co. Ltd. (2002) 74 TTJ (Jd) 193.

However Kerala High Court has held in CIT V. South India Corporation Ltd. (2000) 242 ITR 114 (Ker.) that right to deduction would be lost if the same is credited after due date. It cannot be an indefinite date left to the choice of the assessee. Hon'ble High Court of Calcutta has held in CIT V. K.L. Thirani And Co. Ltd. (1996) 218 ITR 149 (Cal.) that contributions to Provident fund are allowable only if the payment are made within due date. With due respect to above decision, in my opinion, strict and literal construction in this case would deprive assessee the deduction for ever even in genuine cases which cannot be the intention of the legislature. It is well settled that in such circumstances, interpretation should lead to rational result, if necessary by court modifying the lanugage used to achieve the intention of the legislation as held in CIT Vs. J.H. Gotla 156 ITR 323 (SC), K.P. Verghese Vs. ITO 131 ITR 597 (SC), CIT v. Smt. Bharati C. Kothari 244 ITR 352 (Cal.), etc. The only rational result in such situation would be allow deduction of provident fund contribution despite some delay in its deposit, if supported by genuine cause.

The above interpretations, particularly in respect of the issue of due date for payment of Provident Fund contributions, would be of help not only for purpose of Income Tax, but also in respect of provident fund laws wherein penal actions initiated on the basis of incorrect determination of delay in deposit of the contributions could be avoided. ■