

Optimizing cash flows by obtaining Income-tax refunds

Liquidity measures during challenges posed by COVID-19

Background

The COVID-19 pandemic has caused unprecedented disruption to the Indian economy and the public at large. Almost all businesses have been left scrambling for cash as liquidity becomes more important than ever.

Earlier announcements made by the Government in April 2020 for issuance of Income-tax refunds up to INR 500,000 failed to appease large businesses since they were effectively excluded from the relief measure.

Thereafter, in May 2020, the Government unveiled an economic stimulus spread over five tranches intended to push the economy back into action again. Marginal relief was provided to inject some liquidity by announcing that all pending Income-tax refunds would be issued immediately to non-corporates (e.g. Individuals, Partnership firms, LLPs, etc.). However, no such relief was provided to "Corporates" which has left these taxpayers without any liquidity relief so far.

With no Government assistance in sight, it is imperative that companies optimize their cash flows for better working capital management. Companies should have a closer look at amounts locked-in tax refunds claimed in Return of Income ('ROI').

Income tax refund - relevant aspects

Once a taxpayer files its ROI, the Assessing Officer ('AO') must process it and issue an intimation to the taxpayer determining a tax demand or refund¹.

It is likely that refunds relating to assessment years ('AY') 2017-18, 2018-19 and 2019-20 may not have been

issued till date, even though the due date for processing the ROI has elapsed in many cases as shown below:

Assessment Year	ROI filed during Financial Year ('FY')	Due date for processing ROI and issuing refunds
AY 2017-18	FY 2017-18 FY 2018-19 ²	31 March 2019 31 March 2020
AY 2018-19	FY 2018-19	31 March 2020
AY 2019-20	FY 2019-20	31 March 2021

Once the ROI is filed, the Centralized Processing Centre ('CPC') of the Income-tax department generates and issues an automated intimation to the taxpayer. However, in many cases, the refunds are not processed and the files are transferred to the jurisdictional AO for completing the assessments. In either case, the statutory time limit for processing refunds remains the same (as mentioned above).

Further, in many instances, where a notice of scrutiny assessment³ has been issued, the AO does not issue the refunds. Taxpayers may, therefore, consider evaluating the possibility of obtaining pending refunds after carefully analysing the below scenarios for each of the abovementioned years:

Possible scenarios	Scrutiny notice issued	Significant past demands/litigation	Refunds processed
Scenario 1	Yes	Yes	No
Scenario 2	Yes	No	No
Scenario 3	No	No	No

¹Section 143(1) of the Income-tax Act, 1961 ('the Act') provides that an intimation must be issued after processing the ROI within one year from the end of the financial year in which the ROI was filed and refund due to the taxpayer must be granted.

²Where revised ROI has been filed for AY 2017-18.

³As per Section 143(2) of the Act, the AO may issue a scrutiny notice to the taxpayer within six months from the end of the financial year in which the ROI is filed.

Scenario 1: As discussed above, the AO must mandatorily process the ROI and determine the tax demand/refund. However, as per section 241A of the Act, the AO has the discretion to withhold the refund (after due approval), where its grant may adversely affect the Revenue⁴.

Practically, it seems difficult that the Revenue will process such refunds as substantial demand is pending in the taxpayer's own case for earlier years. However, judicial precedents have held that refunds cannot be withheld merely due to pendency of scrutiny proceedings or on the grounds that issues in the scrutiny are similar to issues disputed in the past⁵.

In addition, in a situation where the company has significant demands, the Revenue authorities have the discretion to adjust the refund to the extent of such demands and issue the balance amount⁶. However, there are judicial precedents which have held that where the stay of demand has been specifically granted or the issue has been decided by a higher judicial authority in favour of the taxpayer in its own case, the demands cannot be recovered/adjusted against the refunds.

Therefore, taxpayers seeking large refunds may want to evaluate this carefully based on the facts of their case.

Scenario 2 and 3: A good case exists here for the taxpayer to expedite obtaining the pending refunds. The judicial precedents support the view that the Revenue must grant refunds where due and followed-up by taxpayers, and should not wait till the due date for processing the ROI.

Therefore, in all the above scenarios, companies may want to review their refund and litigation positions and approach the Revenue authorities for issuance of pending refunds.

Way forward

Due to the current situation, the Income tax department is operating at a limited capacity with Revenue authorities having restricted access to their systems from home. The Revenue is sitting on a huge pile of undisbursed refunds and it is unlikely that these will be automatically processed lest the taxpayers knock on the doors of the authorities with an appropriate plan in place.

Taxpayers with pending refunds may want to consider engaging in meaningful discussions with Revenue authorities for quick disbursement of refunds which will definitely help in easing the burden on cash flows in these difficult times.

⁴Please refer to Dhruva Alert on a recent Supreme Court decision in the case of Vodafone Idea Limited at: https://dhruvaadvisors.com/insights/files/Dhruva_Alert_SC_ruling_on_withholding_of_income_tax_refunds.pdf

⁵Please refer to Dhruva Alert on various High Court rulings on writ petitions relating to refunds at: https://dhruvaadvisors.com/insights/files/Dhruva_Direct_Tax_Alert_Writs_on_Refund_23Oct19.pdf

⁶Section 245 of the Act states that where a refund is due to any taxpayer, the AO may set-off such amount against any demand payable by that person after intimating him in writing.

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