

# LEGALFOXES LAW TIMES

## SERIES OF JUDICIAL APPROACH: CLARIFYING THE COMPENSATION PRINCIPLE FOR DELAYED PAYMENT OF INTEREST AMOUNT ON REFUNDS

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### **INTRODUCTION:**

It is a very well-known fact that either authority of law or the assigned department continuously collects taxes paid by the taxpayers. Numerous times taxpayers pay the wrong amount of taxes due to the wrong interpretation of the law. Taxpayers paying more than the needed amount leads to excessive tax collection in the hands of assessing officers or let's say the income tax officers, as sometimes such levy of tax becomes invalid.

The amount which has become an excessive tax in the hands of assessing officers should be refunded to the assessee within a valid duration of time as deprivation of that particular sum of money can cause loss to the assessee, as practically it will not be possible for the assessee to make use of the amount of money which has not been refunded to assessee.

This leads us to a question that tells us what kind of benefit will the assessee have if the assessing officer causes delayed payment of interest on refund of excessive tax collected by them. Will the assessee be prejudiced on the basis that it was either their fault for paying the excessive amount of taxes or the statutory provisions mention any safeguard to them?

The chain of various judicial approaches answers this question by stating that in case any assessing officer causes an excessively large duration of time i.e., inordinate delay in payment of interest on refund admittedly due to assessee then they will have to pay a certain interest amount to assessee in that case.

Hence, this article deals with the question or issue in the matter i.e., "Whether the assessee is entitled to be compensated by the income tax department for the delay in paying interest on the refunded amount admittedly due to it?"

The structure of the article will include the basic concept of the interest of refunds, compensation principle, legislative framework, judicial approaches and legal scrutiny of judicial decisions.

**Keywords:** Interest, Refund, Compensation and Excessive Tax.

**SANDVIK ASIA LTD. vs. COMMISSIONER OF INCOME TAX-I, PUNE & Ors.<sup>1</sup>**

In the case of Sandvik Asia (supra), it is important to note that the appeal which is filed by the appellant raised substantial questions of law which were of public importance in its general nature and also under the Income Tax Act, 1961. The case dealt with the following assessment years i.e., 1977-78, 1978-79, 1981-82 & 1982-83.

The main issue in the matter was “Whether the assessee is entitled to be compensated by the income tax department for the delay in paying to the assessee amounts admittedly due to it?”

Date-wise brief of the facts:

02.01.1987	The advance tax which was paid by assessee during the all four aforementioned assessment years, further interest was requested by the assessee on it.
12.01.1987	The request of the assessee was rejected on the ground that the interest under Section 244(1A) of the Income Tax Act, 1961 was not applicable in the instant case.
27.02.1987	Under Section 264 of the Income Tax Act, 1961 for grant of interest under sections 214 and 244 of the said act, four revision petitions for four different assessment periods were filed by the assessee.
28.02.1990	The following four petitions were rejected.
30.04.1997	The appellant being aggrieved by the rejection of the four revision petitions, appealed to the court to consider the petitions which have been filed in the light of “Modi Industries Ltd. Vs. CIT”

The main issue in the matter which court dealt which was whether based on principles, if we view generally, the assessee should be compensated for the inordinate delay in receiving monies properly due to it and is there any provision in the Income Tax Act, 1961 which provides for payment of compensation for delayed amounts due to assessee wherein these amounts include interest?

The court mentioned a compensation principle in the decision which states as follows the award of interest is mentioned on the refunded amount in the statute in the instant case. When the

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<sup>1</sup> SANDVIK ASIA LTD. vs. COMMISSIONER OF INCOME TAX-I, PUNE & Ors., MANU/SC/0752/2006.

revenue department causes an inordinate delay in payment of interest of refunds then the assesses are liable for the payment of compensation caused due to the inordinate delay in payment of interest on refunds.

In the instant case, there has been a delay for 17 years by the revenue to pay the appellant's money. This was an unjustifiable action done by the revenue as the amount which was withheld was 40 Lakhs rupees. The apex court mentioned that there cannot be an exception to the compensation principle in such a case where the income tax department withheld the money from the appellant for such an inordinate period causing him deprivation and loss of money.

The apex court further clarified that the administration of law and justice was seriously affected by the actions so unlawful with a period ranging up to 17 years, causing to question the authenticity of the department. It is very clear from the compensation principle that during the grant of interest on refund of taxes, first the refund amount should be adjusted towards taxes and secondly, the balance amount towards the interest.

The modalities of return of pre-deposits were clarified by conducting a close scrutiny of the circular dated 2.1.2002, wherein according to Supreme Court order, pre-deposits must be returned to the appellant within the period of 3 months from the date of order passed by any kind of authorities, unless there is a stay on order by the superior court. The delay of more than a period of 3 years by the income tax officers will clearly lead to disciplinary action against the defaulting officers.

Hence, under Section 244 or 244A of the Income Tax Act, 1961 the assessee is entitled to interest. The interest which was previously granted to the assessee has been computed, the payment of simple interest @ 9% p.a. from the date it became payable till the date it is to be paid needs to be paid to the assessee within one month. If the department fails to do so, the penal interest @ 15% p.a. needs to be paid by the department for the aforementioned period.

## **COMMISSIONER OF INCOME TAX vs. GUJARAT FLUORO CHEMICALS<sup>2</sup>**

In the case of Gujarat Fluoro Chemicals (supra), the assessee entered into an agreement of technical collaboration with non-resident company. Income Tax Officer directed the assessee to deduct TDS (Tax deducted at source) under Section 195 on the payment which was made to

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<sup>2</sup> COMMISSIONER OF INCOME TAX vs. GUJARAT FLUORO CHEMICALS, MANU/SC/1289/2014.

the non-resident company. The amendment of section 10(6A) by finance act, 1983 mentioned that no grossing up of tax was needed to be done, while the payment was being given to a non-resident company under those agreements approved by the government of India, the assessee claimed refund. The income tax authorities denied the claim on the ground that provision of Section 244(1A) of the Income Tax Act, 1961 will not apply and the High Court relied on the judgment of Sandvik Asia (supra) and directed to pay the interests as per provisions of sec 244(1A) of the said act.

The decision of the two-judge bench was further put in front of the larger bench of the Supreme Court in the case of Gujarat Fluoro Chemicals (supra) wherein the larger bench has clarified the decision of Sandvik Asia (supra) and mentioned that the decision of latter has been wrongly interpreted by the assessee along with the revenue. They have interpreted that in the case of Sandvik Asia (supra) the court asked the revenue to pay interest on statutory interest in the cases of delayed payment. This wrong interpretation highlights that it is the obligation on revenue to pay interest on interest in case of failure to refund the interest within the statutory period.

The court has very well clarified that in the decision of Sandvik Asia there was an inordinate delay in refunding a certain amount which also included the statutory interest. This delay was caused on the part of the revenue. The court asked the revenue to pay compensation for the causing of the inordinate delay in paying that certain amount which included statutory interest and not interest on interest.

As per the clarification in the instant case, Section 244A of the said act provides for interest on various contingencies. The term various contingencies would only include the interest mentioned in the statute and not interest on such statutory interest.

Hence, the matter was remanded back to the High Court for the re-consideration of the stand of both sides.

### **UNION OF INDIA vs. WILLOWOOD CHEMICALS PVT. LTD. & ORS.<sup>3</sup>**

The nature of the issue involved in this case is a refund. From the date of filing of GSTR38, writ applicants in the case were entitled to 9% per annum interest. The matter in issue, in this

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<sup>3</sup> UNION OF INDIA vs. WILLOWOOD CHEMICALS PVT. LTD. & ORS.,  
MANU/SC/0508/2022.

case, was whether the High Court was justified in awarding 9% per annum interest to writ applicants?

Basically, the respondents are eligible for receiving the interests on delayed payments but the relevancy of 9% per annum was in question. As per the appellants, the 6% per annum interest could be awarded to respondents according to the statutory provision.

It was held that when a case of interest on refund is being governed under Section 56 of the CGST Act then this provision wherein states that the rate of interest would be 6% per annum and in the case when the inordinate delay takes place for a period of more than 20 years then the rate of interest which was to be awarded would exceed i.e., more than 6% per annum.

Comparing situations of both the cases i.e., in Sandvik Asia (supra) inordinate delay took place for 17 years which was unjustifiable and hence the rate of interest @ 9% per annum was granted whereas in the instant case the delay was only in the range of 94 to 290 days which is not even nearby to the range of Sandvik Asia (supra). Hence, the rate of interest @ 6% per annum was granted. The apex court clarified that only in the cases of inordinate delays a huge amount of rate of interest could be granted as in the case of Sandvik Asia (supra) which would fall under the proviso of Section 56 of the said act.

Apart from this the court in the instant case specified two different situations for granting the award of interest. First, when a statute specifies the rate of interest, then the rate of interest will be payable as per the terms mentioned in the provisions of the statute. Second, when a statute is silent about the provisions of awarding the interest or mentions no bar of awarding rate of interest expressly than the situation of delay in paying either compensation or the amounts which are due, would attract the grounds which are equitable to award rate of interest at a reasonable and justified rate.

## **CONCLUSION**

The chain of the judicial approaches provides us with a clear and transparent idea as to what the compensation principle comprises of in the context of delayed payment on the interest of refunds. All the way from the case of Sandvik Asia (supra) wherein it was held that in the cases where only inordinate delay occurs rate of interest @9% per annum needs to be paid by revenue to assessee while paying the amounts of interest on refunds admittedly due to it. Further, in the case of Gujarat Fluoro chemicals (supra) the larger bench of the Supreme Court clarified that

there was nothing as interest on interest i.e., statutory interest. In fact, the court only directed the revenue to pay the compensation for the delay of payment of interest on refunds. In the case of Willowood chemicals Pvt Ltd. (supra), the apex court stated the percentage of rate of interest while granting the revenue to pay compensation for the delay in payment of interest on refunds. Hence, the court states that only in the cases of inordinate delay simple interest of @9% per annum should be paid on compensation by revenue. Otherwise, as per Section 56 of the CGST act, only a simple interest of @6% per annum needs to be paid by the revenue wherein the inordinate delay has not taken place. Inordinate delay comprises a period of a longer stretch such as 20 years or more or if the court is satisfied such as in the case of Sandvik Asia the period of 17 years was considered to be an inordinate delay as well as unjustifiable to withheld appellant's monies.

Either way, it is very practical to say that deprivation of money to the assesseees and excessive tax collection in the hands of the income tax department is not justifiable on any grounds. Causing inordinate delays in refunding the amounts including the interests questions the authenticity of the authorities. Hence, entitlement under Section 244A of the Income Tax Act, 1961 should be referred to while entitling the assessee with the compensation amount on delayed payment of interest on refunds.