1072. Applicability of the provisions in respect of income paid or credited to a member of co-operative bank

1. Under section 194A of the Income-tax Act, 1961 tax is deductible at source from any payment of income by way of interest other than income by way of interest on securities. Clause (*v*) of sub-section (3) of section 194A exempts such income credited or paid by a co-operative society to a member thereof from the requirement of TDS. On the other hand, clause (*viia*) of sub-section (3) of section 194A exempts from the requirement of TDS such income credited or paid in respect of deposits (other than time deposits made on or after 1-7-1995) with a co-operative society engaged in carrying on the business of banking.

2. Representations have been received in the Board seeking clarification as to whether a member of a co-operative bank may receive without TDS interest on time deposit made with the co-operative bank on or after 1-7-1995. The Board has considered the matter and it is clarified that a member of a co-operative bank shall receive interest on both time deposits and deposits other than time deposits with such co-operative bank without TDS under section 194A by virtue of the exemption granted *vide* clause (*v*) of sub-section (3) of the said section. The provisions of clause (*viia*) of the said sub-section are applicable only in case of a non-member depositor of the co-operative bank, who shall receive interest only on deposits other than time deposits made on or after 1-7-1995 without TDS under section 194A.

3. A question has also been raised as to whether nominal members, associate members and sympathizer members are also covered by the exemption under section 194A(3)(*v*). It is hereby clarified that the exemption is available only to such members who have joined in application for the registration of the co-operative society and those who are admitted to membership after registration in accordance with the bye-laws and rules. A member eligible for exemption under section 194A(3)(*v*) must have subscribed to and fully paid for at least one share of the co-operative bank, must be entitled to participate and vote in the General Body Meetings and/or Special General Body Meetings of the co-operative bank and must be entitled to receive share from the profits of the co-operative bank.

Circular : *No. 9/2002, dated 11-9-2002.*

From: Rupesh Srivastava <ropsrivastava@gmail.com>

To: Chandargi Umesh <bchandargi@gmail.com>, Umesh Bolmal <umesh_bolmal@rediffmail.com>

Subject: Circular : F. No. 201/21/84-ITA-II

Date: Wed, 13 Oct 2010 18:04:17 IST

---------- Forwarded message ----------
From: **Taxmann** <sales@taxmann.com>
Date: Wed, Oct 13, 2010 at 5:45 PM
Subject: Circular : F. No. 201/21/84-ITA-II
To: Rupesh Srivastava <ropsrivastava@gmail.com>

Dear Rupesh,
As per your requirement, kindly find Circular : F. No. 201/21/84-ITA-II and rs\- 551.5 have been debited in your account. Kindly make payment for uninterrupted services for your subscription of Direct Tax online for 2010.

Bad and doubtful debts/irrecoverable loans - Interest thereon— Suspense accou maintained for the purpose of - Instructions regarding

1. Attention is invited to Board's Instruction No.1186 (F. No. 201/7/78/ITA-II), dated 20 1978 (Clarification 2) wherein it was clarified that interest on doubtful debts credited to suspense account by the banking companies is includible in the taxable income. It was furth stressed that all pending assessments may be completed keeping in view the said instructio and an immediate review be undertaken and remedial action by way of initiation of proceedi under section 147(b) or section 263 be taken in respect of assessments which have be completed not including such interest in the taxable income in accordance with the Boar earlier instructions.

2. These instructions have resulted in increased litigation between the Income-t Department and the Banking companies. On a subject like this, it appears futile that t organisations of the Government both functioning under the Ministry of Finance, should resort litigation over extended periods of time. Obviously, this leads to delays and other consequent difficulties. Hence, the matter has been re-examined.

3. It has been decided that interest in respect of doubtful debts credited to suspen account by the Banking Companies will be subject to tax but interest charged in an accou where there has been no recovery for three consecutive accounting years will not be subject to tax in the fourth year and onwards. However, if there is any recovery in the fourth year later, the actual amount recovered only will be subjected to tax in the respective years. T procedure will apply to the assessment year 1979-80 and onwards. The Board's Instruction N 1186, dated 20-6-1978 is modified to that extent.

4. Courts of Law have held that subsequent withdrawal of beneficial circulars/instructio

can be with prospective effect only. As such the question of taxability of interest of doubt debts credited by Banking Companies to suspense account will have to be decided up assessment year 1978-79 in the light of the Board's Circular No. 41(V6), dated 6-10-1952 as t said circular was withdrawn only in June, 1978. The new procedure as laid down in para 3 abc will be applicable for and from assessment year 1979-80. All pending disputes on this iss should be settled in the light of these instructions.

Circular : F. No. 201/21/84-ITA-II, dated 9-10-1984 [Source : Oriental Bank of Commerce IAC [1989] 31 ITD 519 (Delhi) 529, 530]

Thanking you,
Jothi

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Rupesh Srivastava
E.mail:ropsrivastava@gmail.com
PH: 09225908041, 09986028041

INSTRUCTION NO. 17 OF 2008, DT. 26TH NOV., 2008

26/11/2008

Subject : Assessment of banks—Checklist for deductions—Regarding

BUSINESS EXPENDITURE

SECTION 36(1)(vii), 36(1)(viia), 37(1)

Kindly refer to above.

2. In a recent review of assessment of banks carried out by C&AG, it has been observed that while computing the income of banks under the head 'Profit and gains of business & profession', deductions of large amounts under different sections are being allowed by the Assessing Officers without proper verification, leading to substantial loss of revenue. It is, therefore, necessary that assessments in the cases of banks are completed with due care and after proper verification. In particular, deductions under the provisions referred to below should be allowed only after a thorough examination of the claim on facts and on law as per the provisions of the Income-tax Act, 1961.

(i) Under section 36(1)(vii) of the Act, deduction on account of bad debts which are written off as irrecoverable in the accounts of the assessee is admissible. However, this should be allowed only if the assessee had debited the amount of such debts to the provision for bad and doubtful debt account under section 36(1)(viia) of the Act, as required by section 36(2)(v) of the Act.

(ii) While considering the claim for bad debts under section 36(1)(vii), the Assessing Officer should allow only such amount of bad debts written off as exceeds the credit balance available in the provision for bad & doubtful debt account created under section 36(2)(viia) of the Act. The credit balance for this purpose will be the opening credit balance i.e., the balance brought forward as on 1st April of the relevant accounting year.

(iii) Section 36(2)(viia)(a) of the Act provides that in respect of any provision for bad and doubtful debts of the type referred to in that sub-clause made by a bank, an amount not exceeding 5 per cent upto 31st March, 2003 and thereafter 7.5 per cent of the total income (computed before making any deduction under this clause and Chapter VI-A of the Act) and an amount not exceeding 10 per cent of the aggregate average advances made by 'rural branches' of such banks computed in the manner prescribed under the Income-tax Rules, 1962, shall be allowed as deduction. For this purpose—

(a) total income of the year should be worked out after adjusting brought forward losses, if any, but before making any deductions under Chapter VI-A of the Act.

(b) The deduction for provision for bad and doubtful debts should be restricted to the amount of such provision actually created in the books of the assessee in the relevant year or the amount calculated as per provisions of section 36(1)(viia), whichever is less.

(c) For working out the aggregate average advances by rural branches, the Assessing Officer should verify whether the branch(es) in question actually qualify to be categorized as 'rural branches' as per the definition in Explanation (ia) below section 36(1)(viia). The aggregate average advances of such rural branches should thereafter be computed in accordance with rule 6ABA of Income-tax Rules, 1962.

(iv) Third proviso to section 36(1)(viia) of the Act, allows a scheduled bank or non-scheduled bank, at its option, to claim a further deduction in excess of the limits specified in the preceding two provisos, for an amount upto the income derived from redemption of securities made in accordance with a scheme framed by Central Government. Before allowing deduction under this provision, it should be ensured that such

income has been disclosed in the return of income under the head "Profits and gains of business or profession"

(v) Section 44C of the Act provides that in the case of a non-resident, head office expenditure be allowed at the rate of five per cent of the adjusted total income or the amount of so much of expenditure in the nature of head office expenditure incurred by the assessee as is attributable to the business of the assessee in India, whichever is less. As per the Explanation below sub section (1) of section 92, the deduction for any expenditure or interest arising from an 'international transaction' shall be determined having regard to its arm's length price. Therefore, in the cases of foreign banks or bank branches assessable in India, the Assessing Officer should carefully examine the claim for head office expenses in the light of these provisions as also the relevant clause(s) of the applicable DTAA, before allowing such claims.

(vi) In cases where an assessee bank purchases securities under capital account at a price inclusive of any accrued interest, the entire purchase consideration is in the nature of capital outlay. Therefore, any interest element included in the purchase consideration is not allowable as expenditure against income accruing on those securities. [Vijaya Bank vs. Addl. CIT (1991) 94 CTR (SC) 216 : (1991) 187 ITR 541 (SC)]

(vii) As per RBI guidelines dated 16th October, 2000, the investment portfolio of the banks is required to be classified under three categories viz. Held to Maturity (HTM), Held for Trading (HFT) and Available for Sale (AFS). Investments classified under HTM category need not be marked to market and are carried at acquisition cost unless these are more than the face value, in which case the premium should be amortised over the period remaining to maturity. In the case of HFT and AFS securities forming stock in trade of the bank, the depreciation/appreciation is to be aggregated scrip wise and only net depreciation, if any, is required to be provided for in the accounts. The latest guidelines of the RBI may be referred to for allowing any such claims.

(viii) Section 14A of the Act read with rule 8D of the Income-tax Rules, 1962, provides that for the purpose of computing total income under the Act, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to income, which does not form part of the total income. Therefore, expenditure in respect of exempted incomes should not be allowed as deduction.

(ix) Section 43B(b) of the Act envisages that deduction towards contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees is allowable in computing total income of the assessee only on actual payment basis. Therefore, it should be verified as to whether the expenditure claimed in respect of above heads has actually been met.

(x) Section 35DDA of the Act provides that where an assessee incurs any expenditure by way of payment of any sum to an employee at the time of his retirement in accordance with any scheme of voluntary retirement, one fifth of the amount so paid shall be deducted in computing the profits and gains of the business and the balance shall be deducted in equal instalments for each of the four immediately succeeding years. Therefore, only one-fifth of such expenditure should be allowed in each of the five years.

(xi) Section 37 of the Act envisages that an amount debited in the P&L account in respect of an accrued or ascertained liability only is an admissible deduction, while any provision in respect of any unascertained liability or a liability which has not accrued, do not qualify for deduction. However, it has been found that banks are claiming provisions on different accounts, probably under the RBI guidelines [e.g. provision for wage arrears for which negotiations are yet to be finalized, provision for standard asset etc...]. A contingent liability cannot constitute deductible expenditure for the purposes of Income-tax Act. Thus, putting aside of money which may become expenditure on the happening of an event would normally not constitute an allowable expenditure under the Income-tax Act. The Assessing Officers should verify such claims as to whether these are admissible as per the Income-tax Act.

(xii) Under section 145 of the Act, income under the heads 'Profits and gains of business' or 'Income from other sources' is required to be computed in accordance with either cash or mercantile system of

accounting, regularly employed by the assessee. Under the RBI guidelines and the Indian Companies Act, 1956, banks have to follow the mercantile system of accounting and prepare accounts on accrual basis. The Assessing Officers should ensure that this system is strictly followed by the banks (in respect of all sources of income).

This may be brought to the notice of all concerned for strict compliance.

[F. No. 228/3/2008-ITA-II]

(2008) 220 CTR (St) 41