आयकर अपीलीय अधिकरण, मुंबई न्यायपीठ "सी", मुंबई

IN THE INCOME TAX APPELLATE TRIBUNAL BENCH "C" MUMBAI

BEFORE HON'BLE S/SHRI JOGINDER SINGH (JM), AND RAJESH KUMAR,(AM)

I.T.A. No.1525 and 3649/Mum/2013
(निर्धारण वर्ष / Assessment Years :2008-09 and 2009-10)

Central Bank of India, 4th floor, CAD(B/S), Chaner Mukhi, Nariman Point, Mumbai-400021	बनाम/ Vs.	Asstt. Commissioner of Income Tax –Circle 2(1), Room No.561, 5h floor, Aayakar Bhavan, M K Road, Mumbai-400020

Appellant	Respondent

PAN:AAACC2498P

I.T.A. No.1561 and 3438/Mum/2013
(निर्धारण वर्ष / Assessment Years : 2008-09 and 2009-10)

Dy. Commissioner of Income Tax –Circle 2(1), Room No.561, 5h floor, Aayakar Bhavan, M K Road, Mumbai-400020	बनाम/ Vs.	Central Bank of India, 4th floor, CAD(B/S), Chaner Mukhi, Nariman Point, Mumbai-400021
	:	
(अपीलार्थी /Appellant)	:	(प्रत्यर्थी / Respondent)

अपीलार्थी की ओर से / Assessee by	:	Shri F V Irani
प्रत्यर्थी की ओर से/ Revenue by	:	Shri Pratap Singh

सुनवाई की तारीख /Date of Hearing	:	6.7.2017
घोषणा की तारीख /Date of Pronouncement	:	3.10.2017

आदेश / O R D E R

PER RAJESH KUMAR, A. M.:

These cross-appeals are directed against the order of ld.CIT(A), Mumbai, passed on 14-12-2012 and 15-2-2013 for the assessment years 2008-09 and 2009-10 respectively which in turn are arising out of the assessment orders framed u/s 143(3) of the Act for these these two respective years.. Since, the appeals pertain to the same assessee, for the sake of convenience, these appeals were clubbed together, heard together and are being dispose off by this common order.

2. First we shall take up the appeal filed by the assessee for the assessment year 2008-09.

3. Grounds of appeal taken by the assessee are as under :

> *1. The CIT(A) has erred in upholding the action of the AO in disallowing Rs.50,41,51,500/- u/s 14A on the basis that this represents expenses attributable o earning income on account of dividend and interest aggregating Rs.19,33,00,661/- which does not from part o the total income."*

4. The only issue raised by the assessee is against the upholding the order of AO in disallowing *Rs.50,41,51,500/-* under sectio14A of the Income Tax Act, 1961 read with rule 8D of the Income Tax Rules, 1962 as expenses attributable to the earning of the exempt income.

5. The facts in brief are that the assessee , a Schedule Bank, filed return of income on 29.9.20008 declaring a total income of Rs.819,38,47,782/-/- which was revised on 2.12.2008 declaring the same income. Thereafter the case was selected for scrutiny and the assessment was framed vide order dated 30.3.2010 passed under section 143(3) by making various additions assessing the total income of the assessee at Rs.12,46,54,02,894/- as has been mentioned in para 7 of the assessment order.

6. The AO during the course of assessment proceedings, noticed that the assessee claimed an amount of Rs.19,33,00,661/- as exempt income. The AO observed that the assessee has incurred a sum of Rs.5772.47 crores as interest pay out and it is not possible that the assessee has made the investments in tax free instrument/investments without incurring the interest cost. Accordingly, the AO came to the conclusion that the provisions of section 14A r.w.r 8D are applicable to the case of the assessee and accordingly after issuing show cause notice calculated the disallowance of Rs.49,87,83,936/-. In the appellate proceedings, the FAA after considering the arguments of the assessee dismissed the appeal upholding the order of the AO that the provisions of section 14A r.w.r 8D were applicable for the year under consideration. Aggrieved by the order of the FAA, the assessee is in appeal before this Tribunal.

7. The ld. AR submitted before the bench that the ld.CIT(A) has grossly erred in confirming the order of the assessing officer in view of the fact that the assessee's own funds and other interest free funds available were far more than the investments in the securities yielding tax free income. The ld. AR submitted that the tax free fund comprising of own funds and non interest bearing funds were Rs.15942.76 crores, whereas the investment in tax free security of Rs.746.02 crores and therefore the investments in tax free securities were out of interest free funds available with the assessee. The ld. AR in corroboration of his arguments took us through the balance sheet . The ld. AR argued that no disallowance is called for under u/s 8D(2)(ii) of the Rules. So far as the disallowance u/r 8D(2)(iii) is concerned the ld. AR submitted before the Bench that the AO has not pointed out his dissatisfaction with regard to the claim of the assessee as to how the said claim was wrong vis-à-vis the tax free income earned by the assessee which is a pre-conditions both prior to and post 1.4.2008 for application of provisions of section 14A of the Act. Once it is proved that AO has not recorded any satisfaction with the reference to the books of account of the assessee on its claim , no disallowance can be made. Alternatively, the ld.AR submitted that the disallowance at the rate of 2% of the exempt income be made in the line with the decision of the co-ordinate Bench of the Tribunal in assessee's

own case in ITA 4449/Mum/2003 and ITA No.4450/Mum/2003 For AYs 1998-99 and 1999-2000 dated 24.9.2010.

8. The ld. DR reiterated the same submissions as made before the lower authorities and also submitted that the provisions of section 14A r.w.rule 8D are effective from assessment year 2008-09 and therefore prayed that order of ld. CIT(A) should be confirmed on this issue.

9. We have carefully considered the submissions of rival parties and perused the orders of lower authorities. The undisputed facts of the case are the assessee's own interest free funds comprising its own funds and other interest free funds availed with the assessee were far more than the investment made in securities which yielded tax free exempt income. Moreover, the perusal of the AO's order reveals that the AO has not recorded any satisfaction with regard to the claim of the assessee of exempt income without attributing any the expenses relating thereto with reference to the books of accounts which is a pre-condition for invoking the provisions of the section 14A r.w.r 8D as has been decided by the Hon'ble Apex Court in the case of 'Godrej & Boyce Manufacturing Co. Ltd. V/s DCIT (2017) 81 taxmann.com 111(SC), wherein it has been held that the AO has to record the satisfaction that the assessee has incurred any expenditure in relation of the earning of earning income after examining the records and books of accounts maintained by the assessee and thus the AO has to be record his satisfaction

with regard to the correctness of the claim of the assessee otherwise the provisions of section 14A can not be applied. We find merit in the plea of the ld.AR that in absence of any satisfaction recorded by the AO no disallowance could be made u/r 14A r.w.rule 8D. However, to maintain the consistency with the decision of the co-ordinate bench of the Tribunal, we think it fit and reasonable which has been an alternative prayer by the counsel during the course of hearing that the disallowance of 2% be made as has been made by the Tribunal in the assessment year 1998-99 and 1999-2000. **The operative part of ITA No 4449/Mum/2003 AY 1998-99 is reproduced as under (para 5):-**

> *"5. Before us, Ld Counsel for the assessee demonstrated that assessee has sufficient funds and therefore, no disallowance is called for on account of interest vide Rule 8D(2)(ii) of IT Rules, 1962. In this regard, he relied on various decisions including that of the judgment of the Hon"ble jurisdictional High Court in the case of Reliance Utilities & Power Ltd [2009] 313 ITR 340, with which we agree. Regarding the disallowance out of administrative expenses, Ld Counsel for the assessee submitted that disallowance of a reasonable percentage of the exempt income is an accepted method of quantifying the disallowance of expenses for the AYs prior to AY 2008-2009, the year of amendment to Rule 8D of IT Rules, 1962. In this regard, Ld Counsel for the assessee filed decisions of the Tribunal in the cases of DCIT vs. HDFC Bank Ltd in ITA Nos. 4529/M/2005 and others, dated 29.6.2011 and order of the Tribunal in the case of Bank of India vs. ACIT in ITA No.1498/Mum/2011 for the AY 2001-2002, dated 9.4.2014 and submitted that disallowance @ 1% of the exempt income in the case of Banks is accepted as a „reasonable basis". Further, he also referred to the decision of the Tribunal in the case of M/s. Godrej Agrovet Ltd vs. ACIT in ITA No.1629/Mum/2009, dated 17.9.2010, which was subsequently ratified by the Hon"ble jurisdictional High Court in the same case. This case is relevant for the proposition that the*

disallowance of 2% of the exempt income is found reasonable by the Hon"ble High Court."

Accordingly, we set aside the order of the ld.CIT(A) and direct the AO to make addition to the 2% of the exempt income. This ground of appeal is partly allowed.

ITA No.1561/Mum/2013

Grounds of appeal taken by the revenue are as under :

> *"On the facts and in the circumstances of the case and in law, the learned C!T(A) has erred in allowing relief to the assessee to the extent impugned in the grounds enumerated below: .*
>
> *1. The order of the C!T(A) is opposed to law and facts of the case.*
>
> *2. "On the facts and in the circumstances of the case and in law, the Ld. CIT(A) has failed to appreciate that as per the provision to section 36(1)(vii), bad debts is allowed to be written off to the extent of the amounts in excess over the credit balance in provision account".*
>
> *3. "On the facts and in the circumstances of the case and in law, the Ld. C!T(A) has failed to appreciate that the assessee is following Mercantile System of accounting and, therefore, interest accrued should have been offered for taxation"*

10. In this appeal only two grounds have been raised by the revenue. In the grounds of appeal no.1, the issue is regarding the deletion of addition of Rs.289,19,80,059 by CIT(A) as made by the AO u/s 36(1)(vii) of the Act towards bad debts written off. During the year, the assessee claimed bad debts in the books of accounts of Rs.329,86,21,622/- comprising of Rs.289,19,80,059 regarding non-rural branches and Rs.40,66,41,563/-

towards bad debts pertaining to rural branches. According to the AO, the bad debts were to be allowed to the extent of excess of total bad debts written off during the year over the opening credit balances in the provisions for bad and doubtful u/s 36(1)(viia) of the Act of rural advances covered by proviso to section 36(1)(vii) as determined by the assessment order framed u/s 143(3) of the Act for AY 2007-08 which worked out to Rs. 3,26,91,517/-. Thus, the bad debts to the tune of Rs.285,92,88,542 were disallowed and added to the total income of the assessee which was arrived at by reduction of Rs. 3,26,91,517/- from the bad debts written off qua non rural branches i.e 289,19,80,059/-. The assessee preferred an appeal before the ld. CIT(A) who allowed the appeal of the assessee after considering the decision of the Hon'ble Supreme Court in the case of Catholic Syrian Bank (2012) 343 ITR 270 (SC) by observing and holding as under :

> *"4.1 Therefore, in view of the decision of Hon'ble Supreme Court as reproduced above, which has also been followed by Hon'ble ITAT in assessee's own case for A.Y. 96-97 in ITA No. 7677/M/2010 vide order dated 7/11112, assessee is allowed deduction on account of bad debts written off u/s. 36(1)(vii) independent of its claim and balance available for the purpose of section 36(1)(viia). There is no provision for bad debts available or claimed against the urban branches, whereas, Rs.289, 19,80,059/- the bad debts written off claimed pertains to urban branches only as claimed by the assessee. Hence, the entire claim of the assessee for bad debts written off Rs.289,19,80,059/- is allowed u/s. 36(1) (vii), it includes the amount of Rs.3,26,91,517/- which has already been allowed by the A.O. and, therefore, the balance disallowance of claim of bad debts Rs.285,92,88,542/- is also allowed. This ground of appeal o the assessee is allowed."*

11. Before us the ld. AR pointed out at the outset that the issue raised in this ground stands covered by the decision of the co-ordinate Bench of the Tribunal in assessee's own case for the assessment years 1989-90 to 1992-93 and 1994-95 to 1999-2000 and therefore following the order of coordinate benches , the order of First Appellate Authority should be upheld by dismissing the appeal of the revenue on this issue.

12. The ld. DR strongly objected to the contentions of the assessee by relying on the order of AO and requested that order the ld.CIT(A) be set aside and that of AO be upheld..

13. We have heard the rival contentions and perused the material placed before us including the orders relied upon by the parties and impugned orders. We find from the record the co-ordinate Bench of the Tribunal that an identical issue has been decided in assessee's case in the earlier years by following the decision of the Hon'ble Supreme Court in (2012) 343 ITR 270 (SC). For the sake of convenience, we reproduce the operative part of the judgement as under:

> *"41. To conclude, we hold that the provisions of Sections 36(1)(vii) and 36(1)(viia) of the Act are distinct and independent items of deduction and operate in their respective fields. The bad debts written off in debts, other than those for which the provision is made under clause (viia), will be covered under the main part of Section 36(1)(vii), while the proviso will operate in cases under clause (viia) to limit deduction to the extent of difference between the debt or part thereof written off in the previous year and credit balance in the provision for bad and doubtful debts account made under clause (viia). The proviso to Section 36(1)(vii) will relate to cases covered*

under Section 36(1)(viia) and has to be read with Section 36(2)(v) of the Act.Thus, the proviso would not permit benefit of double deduction, operating with reference to rural loans while under Section 36(1)(vii), the assessee would be entitled to general deduction upon an account having become bad debt and being written off as irrecoverable in the accounts of the assessee for the previous year. This, obviously, would be subject to satisfaction of the requirements contemplated under Section 36(2).

42. Consequently, while answering the question in favour of the assessee, we allow the appeals of the assessees and dismiss the appeals preferred by the Revenue. Further, we direct that all matters be remanded to the assessing officer for computation in accordance with law, in light of the law enunciated in this judgment.

I have gone through the judgment of my esteemed brother Swatanter Kumar, J. and I agree with the conclusions contained therein. However, I would like to give my own reasons.

The question for our consideration is - whether on the facts and circumstances of the case, the assessee(s) is eligible for deduction of the bad and doubtful debts actually written off in view of Section 36(1)(vii) which limits the deduction allowable under the proviso to the excess over the credit balance made under clause (viia) of Section 36(1) of Income Tax Act, 1961 ("ITA"

for short)

2. Under Section 36(1)(vii) of the ITA 1961, the tax payer carrying on business is entitled to a deduction, in the computation of taxable profits, of the amount of any debt which is established to have become a bad debt during the previous year, subject to certain conditions. However, a mere provision for bad and doubtful debt(s) is not allowed as a deduction in the computation of taxable profits. In order to promote rural banking and in order to assist the scheduled commercial banks in making adequate provisions from their current profits to provide for risks in relation to their rural advances, the Finance Act, inserted clause (viia) in sub-section (1) of Section 36 to provide for a deduction, in the computation of taxable profits of all scheduled commercial banks, in respect of provisions made by them for bad and doubtful debt(s) relating to advances made by their rural branches. The deduction is limited to a specified percentage of the aggregate average

advances made by the rural branches computed in the manner prescribed by the IT Rules, 1962.Thus, the provisions of clause (viia) of Section 36(1) relating to the deduction on account of the provision for bad and doubtful debt(s) is distinct and independent of the provisions of Section 36(1)(vii) relating to allowance of the bad debt(s). In other words, the scheduled commercial banks would continue to get the full benefit of the write off of the irrecoverable debt(s) under Section 36(1)(vii) in addition to the benefit of deduction for the provision made for bad and doubtful debt(s) under Section 36(1)(viia). A reading of the Circulars issued by CBDT indicates that normally a deduction for bad debt(s) can be allowed only if the debt is written off in the books as bad debt(s). No deduction is allowable in respect of a mere provision for bad and doubtful debt(s). But in the case of rural advances, a deduction would be allowed even in respect of a mere provision without insisting on an actual write off.However, this may result in double allowance in the sense that in respect of same rural advance the bank may get allowance on the basis of clause (viia) and also on the basis of actual write off under clause (vii). This situation is taken care of by the proviso to clause (vii) which limits the allowance on the basis of the actual write off to the excess, if any, of the write off over the amount standing to the credit of the account created under clause (viia). However, the Revenue disputes the position that the proviso to clause (vii) refers only to rural advances. It says that there are no such words in the proviso which indicates that the proviso apply only to rural advances. We find no merit in the objection raised by the Revenue.Firstly, CBDT itself has recognized the position that a bank would be entitled to both the deduction, one under clause (vii) on the basis of actual write off and another, on the basis of clause (viia) in respect of a mere provision. Further, to prevent double deduction, the proviso to clause (vii) was inserted which says that in respect of bad debt(s) arising out of rural advances, the deduction on account of actual write off would be limited to the excess of the amount written off over the amount of the provision allowed under clause (viia). Thus, the proviso to clause (vii) stood introduced in order to protect the Revenue. It would be meaningless to invoke the said proviso where there is no threat of double deduction. In case of rural advances, which are covered by the provisions of clause (viia), there would be no such double deduction. The proviso limits its application to the case of a bank to which clause (viia) applies. Clause (viia) applies only to rural advances. This has been explained by the Circulars issued by CBDT. Thus, the proviso indicates that it is limited in its application to bad debt(s) arising out of rural advances of a bank. It follows that if the

amount of bad debt(s) actually written off in the accounts of the bank represents only debt(s) arising out of urban advances, the allowance thereof in the assessment is not affected, controlled or limited in any way by the proviso to clause (vii).

3. Accordingly, the above question is answered in the affirmative, i.e., in favour of the assessee(s). For the above reasons, I agree that the appeals filed by the assessees stand allowed and the appeals filed by the Revenue stand dismissed with no order as to costs."

We, respectfully following the decision of the co-ordinate bench of the Tribunal uphold the order of the ld.CIT(A) and dismiss the ground taken by the revenue.

14. The issue raised in grounds of appeal no.3 is against the decision of the ld.CIT(A) that the interest accrued at the year end on the securitiesqua broken period is not taxable as against the addition made by the AO on the ground that the interest accrued up to the year end has to be taxed according to the mercantile system of accounting whether or not it is fall due.

15. The facts of the case are that the assessee held the securities on which the interest was accrued on fixed days normally twice in an year on which the interest due dates were different from the year end and therefore, the interest after due date till the year end was accounted on the accrual system of accounting but not offered to tax. The AO was of the view that the interest has to be taxed on the basis of accrual irrespective of date of payment as the same accrues on day to day basis and therefore rejected the

contention of the assessee that the interest falling after due date till year end is not taxable. Accordingly added an amount of Rs.86,21,931/-. Aggrieved, assessee preferred appeal before the ld.CIT(A), who after considering the submissions and on perusal of the record allowed the appeal of the assessee on this ground by observing that the the assessee has no right to receive the interest and therefore the same is not taxable.

16. The ld. AR, at the outset, submitted before us that the issue involved in this ground stands covered in favour of the assessee and against the revenue by the decision of jurisdictional High Court in the case of Director of Income tax (int.Tax. V/s Credit Suisse First Boston (Cyprus) Ltd 2012 23 taxmann.clm 424 (Bom)(supra). Therefore, the ld. AR prayed that in view of the decision of the hon'ble jurisdictional High Court, the issue be decided in assessee's favour.

17. The ld. DR strongly opposed the submissions of the assessee by relying on the order of AO.

18. We have carefully considered the contentions of the rival parties and perused the material placed before us including the impugned orders. We find that in the instant case, the issue is with regard to the taxability of the interest relating to the broken period after due date of interest till the close of accounting year. Acceding to the assessee the same is not taxable as the assessee has no right to receive the said interest though accrued on day to

day basis. The ld.CIT(A) allowed the appeal of the assessee on the same reasoning. We have perused the decision of he Hon'ble Jurisidicitonal High Court in the case of Director of Income tax (int.Tax. V/s Credit Suisse First Boston (Cyprus)ltd (supra) and find that the identical issue has been decided by holding that the said interest is not liable to tax qua the broken period. The relevant para of the judgment is reproduced below:

> ***"18.*** *In CIT v. Canara Bank [1992] 195 ITR 66/61 Taxman 79 another Division Bench of the Karnataka High Court followed the above judgments. The High Court construed the last sentence quoted above from the judgment of the Supreme Court emphasised by us as under :-*
>
> > *"The last sentence conveys the idea that actually the income fructifies to the assessee only when the securities yield the interest and only in such a situation Section 18 is attracted and that the securities do not yield any income during the broken period of any year."*
>
> *We are in respectful agreement with this interpretation of the judgment of the Supreme Court. It logically follows from the fact that the Supreme Court upheld the judgment of the High Court in Vijaya Bank Ltd. (supra).*
>
> ***19.*** *The right to receive interest on the Government securities vested in the respondent only on the due date mentioned in the securities. Consequently, interest accrued on the securities only on the due dates and cannot be said to have accrued to the respondent on any date other than the date stipulated therein. The contention that interest accrues for broken periods between two consecutive dates stipulated in the agreement/instrument for payment of interest is without any basis in law.*
>
> *If the respondent held the security upto 31st March, 2001 and sold the same thereafter, but before the date on which interest was payable as stipulated in the security, interest cannot be said to have accrued to the respondent.*
>
> *It is not disputed that in respect of the securities held by the respondent on 31st March, 2001, the due date for payment of interest thereon had not arrived on 31st March, 2001 and that the respondent sold some of such securities prior to the next due date for payment of interest. It is only the holder of the security on such date to whom interest can be said*

to have accrued. In any event interest did not accrue to the respondent on 31st March, 2001, as admittedly interest was not payable on that date as per the terms of the said securities.

20. *The appellate authorities, therefore, rightly deleted the addition of Rs.1,21,57,517/- by the Assessing Officer as interest income."*

We, therefore, respectfully following the ratio laid down by the hon'ble jurisdictional High Court, dismiss the ground raise by the revenue. Resultantly, the appeal of the revenue is dismissed.

ITA No.3438/Mum/2013 (By revenue) and ITA No.3649/Mum/2013 (by assessee)

19. The grounds of appeal taken in these appeals by the respective parties are identical to that of ITA Nos.1561/Mum/2013 and 1525/Mum/2013. Since we have decided the issues in assessee's favour in the above mentioned appeals, the decision taken therein would , mutatis mutandis, apply to these cases as well. Accordingly, these appeals are decided as mentioned above.

20. In the result, the appeals of the assessee are allowed and that of revenue are dismissed.

Order pronounced in the open court on 3rd Oct, 2017.

Sd	sd
(JOGINDER SINGH)	**(RAJESH KUMAR)**
Judicial Member	**Accountant Member**

मुंबई Mumbai; दिनांक Dated :3.10.2017

Sr.PS:SRL:

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent
3. आयकर आयुक्त(अपील) / The CIT(A)
4. आयकर आयुक्त / CIT – concerned
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, मुंबई / DR, ITAT, Mumbai
6. गार्ड फाईल / Guard File

आदेशानुसार/ BY ORDER,

उप/सहायक पंजीकार (Dy./Asstt. Registrar)

आयकर अपीलीय अधिकरण, मुंबई **/ ITAT, Mumbai**