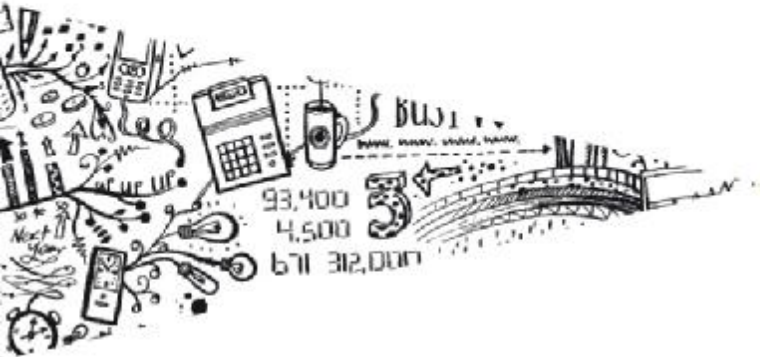


20 October 2011

EY Tax Alert

CBDT circular on withholding guidelines for banks on interest on Court deposits



Executive summary

This Tax Alert summarizes a recent Circular No. 08/2011 [F. No. 275/30/2011-IT(B)] dated 14 October 2011 (Circular) issued by the Central Board of Direct Taxes (CBDT) outlining the tax withholding procedure to be adopted in respect of interest on deposit with banks held in pursuant to the Supreme Court/High Court/any other Court or Tribunal (Court) during the pendency of litigation of claim/compensation.

The Circular provides guidelines to the effect that tax withholding on interest accruing on such deposits is to be made in the name of the litigant/s (depositor/s) to whom the Court has directed to deposit the amount. Consequently, tax withholding certificate is to be issued in the name of such depositor. With a view to ensure implementation of tax withholding requirements, the depositor/s are required to submit prescribed declaration to the Court which, in turn, would pass the information to the concerned bank. The Circular also provides certain illustrations for guidance in the matter, apart from enlisting the circumstances where the procedure of the Circular is not applicable.

Background

- ▶ The Indian Tax Laws (ITL) require tax withholding on interest paid by banks on deposits if the aggregate of the amount of such interest credited or paid to the account of the payee during the financial year exceeds the specified amount.

- ▶ In the course of the proceedings before the Court, the depositor/s are, at times, directed by the Court to make deposit of a certain amount with banks, either directly or through the Court. Such deposits (usually time deposits) are kept in banks in the names of Registrar/Prothonotary and Senior Master or any other name as per the Court's order. Under such circumstances, issues were raised about the tax withholding on interest periodically accruing on such deposits and about the person(s) who would be entitled to credit of the taxes so withheld.
- ▶ One of the banks in India, UCO Bank^[1] had filed a writ petition before the Delhi High Court challenging the show cause notice issued by the Tax Authority for recovery of taxes for alleged default by the Bank in not withholding tax on interest on the Court deposits. Considering the complexity of the issue, the two-judge division Bench of the High Court referred the matter to a three-judge Larger Bench. At the hearing before the Larger Bench, Tax Authority represented that the matter is already being looked into by the CBDT and there is a possibility that some kind of solution can be arrived at. The Larger Bench, by its order dated 15 July 2011, directed the CBDT to take a decision on the issue within three months from the date of receipt of its order.
- ▶ Accordingly, the CBDT has issued a circular to address the difficulties in the implementation of tax withholding provisions of the ITL under such situations.

^[1] W.P(C) 2972/2011, Source: www.delhihighcourt.nic.in

General guidelines

- ▶ The Circular is applicable to cases where, pursuant to the Court's direction, one or more than one depositor/s make deposit with banks, directly or through the Court.
- ▶ The Circular requires that tax is to be withheld in the name of the person who makes the deposit.
- ▶ With a view to facilitate the administration of tax withholding, the depositor/s are required to submit a prescribed declaration with the Court at the time of making deposit of the amount ordered by the Court. The Registrar/Prothonotary and Senior Master or any person authorized by the Court is required to pass these information to the concerned bank for ensuring that tax withholding is made by the bank in the name of the depositor/s.
- ▶ The bank is to issue withholding certificate in the name of such depositor/s. In case of deposits by more than one person, withholding on interest is to be made on a proportionate basis i.e., in proportion to the share in deposit. Accordingly, the bank is required to issue withholding certificates in favor of depositors.

Illustrations in the Circular

The Circular provides following illustrative instances for the guidance as to in whose name withholding to be effected and who is entitled to tax credit.

Nature of litigation proceedings	Depositor	Name in which deposit may be held	In whose name withholding is to be effected?
Compensation awarded by Motor Accident Claims Tribunal	Insurance company	In such name as directed by the Court	Insurance Company
Land compensation litigation	Land Acquisition Authority	Not specified	The concerned acquisition authority, if it is an entity liable to tax on its income. No withholding if acquisition is by the Central or State Government
Adjudication of financial dispute	Depositors	Depositors in the name of the Court officer	Depositors

Exclusions from the applicability of the Circular

The Circular excludes the following situations from its scope:

- ▶ Any deposit with a taxpayer dealt by the Court, in the capacity of being an administrator or receiver or any other authority of similar nature, or
- ▶ Any deposit that has arisen due to an attachment made by the Court, or
- ▶ The cases of 'representative assessee', as mentioned under the ITL.

Comments

The issue about the applicability of tax withholding in respect of interest on bank deposits made pursuant to the Court order is a vexed issue. The difficulty arises as the deposit is often in the name of the Registrar or Prothonotary or Court officer. Also, it remains unclear as to who may be eventually entitled to get the benefit of the deposit and interest thereon. The guidance provided in the Circular can assist banks in the matter of discharge of their tax withholding obligation.

While the Circular provides guidance to the payer under the specified circumstances, the issue about the person who is eligible to claim credit in respect of such withholding and the year in which such person may claim benefit of withholding will need to be decided in accordance with the applicable provisions of the ITL as also the applicable judicial rulings.

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