

**IN THE INCOME TAX APPELLATE TRIBUNAL  
VISAKHAPATNAM BENCH, VISAKHAPATNAM**

**BEFORE SHRI V. DURGA RAO, HON'BLE JUDICIAL MEMBER &  
SHRI D.S. SUNDER SINGH, HON'BLE ACCOUNTANT MEMBER**

**ITA Nos. 176 & 177/VIZ/2013  
(Asst. Year : 2008-09 & 2009-10)**

**And**

**ITA No. 517/VIZ/2014  
(Asst. Year : 2010-11)**

**And**

**ITA No. 173/VIZ/2015  
(Asst. Year : 2011-12)**

The Aryapuram Co-op. Urban Bank Ltd., Near Gokavaram Bus Stand, Rajahmundry, East Godavari District. vs. ACIT, Circle-1, Rajahmundry.

PAN No. AAATT 8099 C  
(Appellant)

(Respondent)

**ITA No. 195/VIZ/2013  
(Asst. Year : 2009-10)**

ACIT, Circle-1, Rajahmundry. vs. The Aryapuram Co-op. Urban Bank Ltd., Near Gokavaram Bus Stand, Rajahmundry, East Godavari District.

(Appellant)

PAN No. AAATT 8099 C  
(Respondent)

Assessee by : Shri G.V.N. Hari – Advocate.  
Department By : Shri Deba Kumar Sonawal – CIT DR

Date of hearing : 02/05/2018.  
Date of pronouncement : 28/05/2018.

**ORDER****PER V. DURGA RAO, JUDICIAL MEMBER**

ITA Nos. 176 & 177/VIZ/2013; ITA No. 517/VIZ/2014 & ITA No.173/VIZ/2015 filed by the assessee and ITA No. 195/VIZ/2013 filed by the Revenue are directed against the separate orders of Commissioner of Income Tax (Appeals), Visakhapatnam, dated 24/01/2013 for the Assessment Years 2008-09 & 2009-10; dated 14/07/2014 for the Assessment Year 2010-11; and also against the order of Id. CIT(A), Rajahmundry dated 27/02/2015 for the Assessment Year 2011-12. Since the issues and facts involved in all the appeals are common, heard together and disposed of by way of this consolidated order for the sake of convenience.

2. The assessee has raised the following grounds of appeal:-

- "1. *The order of the learned Commissioner of Income Tax is contrary to the facts and also the law applicable to the facts of the case.*
2. *The learned Commissioner of Income Tax (Appeals) is not justified in sustaining addition of Rs. 1,36,997/- out of disallowance of Rs. 17,71,587/- made by the assessing officer towards Bonus & Ex gratia payable.*
3. *The learned Commissioner of Income Tax (Appeals) is not justified in sustaining addition of Rs.20,76,621 out of disallowance of Rs. 27,52,916 towards Leave encashment payable.*
4. *The learned Commissioner of income tax (Appeals) is not justified in sustaining addition of its. 7763\$06 made by the assessing officer towards-interest on Share capital.*
5. *The learned Commissioner of Income Tax (Appeals) is not justified in confirming the addition of Rs. 786,356/- made by*

*the assessing officer towards disallowance of gratuity premium paid.*

6. *The Id. CIT(A) is not justified in confirming the addition of Rs. 22,96,950/- made by the Assessing Officer towards disallowance of Establishment fund.*
7. *Any other ground that may be urged at the time of appeal hearing."*

**3.** Ground Nos. 1 & 7 are general in nature, therefore, adjudication is not required on our part, same are dismissed.

**4.** Facts of the case in brief are that assessee is a cooperative society engaged in cooperative banking, filed its return of income by declaring total income of Rs. 76,17,940/-. In response to the notice issued under section 148 of the Income Tax Act, 1961 (hereinafter referred to as "Act"), the assessee also filed a revised return by disclosing total income of Rs. 1,49,08,080/-. The Assessing Officer passed an order under section 144 read with section 143(3) of the Act by making certain disallowances. On appeal, Id. CIT(A) considered and passed an order.

**5.** Before us, assessee has raised **ground No.2** relating to sustenance of addition of Rs.1,36,997/- towards **bonus & exgratia payment**. Originally, the Assessing Officer has not made any addition on this count. On appeal, Id. CIT(A) has directed the Assessing Officer to examine, whether amount of Rs. 21,00,276/- debited as bonus and ex-gratia is allowable as per law or not. The Assessing Officer has submitted a report to the Id.

CIT(A) that an amount of Rs. 19,08,584/- is debited as bonus to the staff, out of which, an amount of Rs. 17,71,587/- is paid on 03/10/2008 i.e. before filing of the return. The balance amount of Rs. 1,36,997/-, is kept in abeyance as some matter is pending (disciplinary proceedings) against employee. The Id. CIT(A) has considered the same and held that assessee admitted that the amount of Rs.19,08,584/- was debited and Rs. 17,71,587/- was paid within the stipulated time, hence, the balance amount of Rs. 1,36,997/- is not allowable in view of the provisions contained in section 43B of the Act and directed the Assessing Officer to disallow the same and add back to the total income of the assessee. We find no reason to interfere with the order of the Id. CIT(A) on this issue. Thus, this ground of appeal raised by the assessee is dismissed.

**6. Ground No.3** relating to sustenance of addition of Rs.20,76,621/- towards **leave encashment payment**. Originally, the Assessing Officer did not make any addition, however, Id.CIT(A) directed the Assessing Officer to examine whether leave encashment amount of Rs. 27,52,916/- is allowable as per explanation (f) to section 43B of the Act or not. The Assessing Officer verified the same and submitted to the Id. CIT(A) that the amount of Rs. 27,52,916/- is debited as leave encashment. The

payment of the same was not supported by any evidence and the same has been carried to the reserve account, from which payments would be made as and when the employees surrender their leave. Therefore, the same is not allowable in view of the provisions of section 43B(f) of the Act. The Id. CIT(A) asked the assessee to explain how the provisions made for leave encashment is allowable. In response, it was explained that the amount of Rs. 27,52,916/- was created towards leave encashment. As per agreement, an employee is entitled to 30 days leave encashment per year and he can accumulate leave upto 300 days at the time of his retirement, the amount of which is exempt under section 10 of the Act. Since this provision amount is created towards end liability of leave encashment, which will be paid only after retirement, the applicability of provisions to section 43B are not applicable. The assessee also relied on the decision of the Hon'ble Calcutta High Court in the case of **Exide Industries Ltd. vs. Union of India** [(292 ITR 470)(Cal.)]. The Id. CIT(A) by considering the stay granted by the Hon'ble Apex Court on the decision of the Hon'ble High Court of Calcutta, directed the Assessing Officer to disallow and add the balance amount of Rs. 20,76,621/- to the total income of the assessee.

**7.** On appeal before us, Id. counsel for the assessee has submitted that deduction made by the assessee is allowable under the provisions of section 43B of the Act.

**8.** On the other hand, Id. Departmental Representative strongly supported the orders of the authorities below.

**9.** We have heard both the parties, perused the material available on record and gone through orders of the authorities below.

**10.** In this case, the assessee has made a provision of Rs.27,52,916/- towards leave encashment and only an amount of Rs. 6,76,295/- was paid. According to the assessee, the provision made by the assessee is allowable in the light of the decision of the Hon'ble Calcutta High Court in the case of Exide Industries Ltd. (supra). On appeal, Id. CIT(A) by considering the decision of the Hon'ble Calcutta High Court and also the observations made by the Hon'ble Apex Court in the course of stay proceedings that the assessee must pay tax as if section 43B(f) is on the statute, directed the Assessing Officer to add the unutilized amount of Rs.20,76,621/- to the total income of the assessee. We find no infirmity in the order of the Id. CIT(A). Thus, this ground of appeal raised by the assessee is dismissed.

**11. Ground No.4** relates to the sustenance of addition of Rs.77,63,806/- towards **interest on share capital**. Originally, the Assessing Officer has not made any addition, however, Id.CIT(A) directed the Assessing Officer to examine whether the amount of Rs. 77,63,806/- claimed as interest on share capital is allowable or not as per law by taking into account the latest decision of the Hon'ble ITAT on this issue. The Assessing Officer after verification, submitted a report to the Id. CIT(A) that the amount of Rs. 77,63,806/- is claimed as interest on share capital and also submitted that in the case of ***ACIT vs. Visakhapatnam Cooperative Bank Ltd.*** in ITA No.19/Vizag/2011, dated 29/08/2011, the Hon'ble ITAT, Visakhapatnam Bench has allowed such interest and further submitted that on the decision of the ITAT, department has went on appeal to the Hon'ble High Court. The Id. CIT(A) after considering the explanation given by the assessee and also the provisions of A.P. Cooperative Societies Act, has held that the order passed by the Tribunal in the case of Visakhapatnam Cooperative Bank Ltd., (supra) is not applicable on the ground that the order passed by the ITAT, Visakhapatnam Bench is based on A.P. Mutually Aided Cooperative Societies Act. The relevant portion of the order of Id. CIT(A) is extracted as under:-

"8.4.9. As contended, the appellant is governed by the provisions of AP Cooperative Societies Act and not by the AP Mutually Aided Cooperative Societies Act. The decision rendered by the Hon'ble ITAT, Visakhapatnam, in the case of Vishakhapatnam Co-op Bank Ltd. would not be applicable as it was rendered with reference to the interpretation of sec. 16 of the AP Mutually Aided Co-operative Societies Act. It is pertinent to note that sec 45 of the AP Co-operative Societies Act which deals with 'Disposal of Profit' only provide for payment of dividend and not of interest. However, Rule 36(5)(d) of the Act provided for payment of dividend or interest not less than 6% on share capital. The appellant bank had passed a resolution for payment of interest at 15%. It is seen from the resolution that the bank has decided to make payment of interest in lieu of dividends, to reduce its tax burden on account of withdrawal of deduction under section 80P of the I.T. Act by the legislature from 2007 onwards. Instead of payment of at 15% as in earlier years, interest has been paid at 15% for the subject year. It is clear that the payment has been made in lieu of dividends, and as such it amounts to application of profit and not a charge on profit. Therefore, the AO is directed to disallow the claim of Rs. 77,63,806/- and add it to the total income."

**12.** On being aggrieved, the assessee carried the matter in appeal before the Tribunal.

**13.** Ld. counsel for the assessee has submitted that the present issue is squarely covered by the decision of the coordinate bench of the tribunal in the case of **ACIT Vs. Visakhapatnam Cooperative Bank Ltd.** in ITA No. 05/Vizag/2011, dated 29/08/2011. He also relied on the order of the coordinate bench of the tribunal in the case of **Visakhapatnam Cooperative Bank Ltd. vs. ACIT** in ITA No. 444/Vizag/2012, dated 30/09/2016 and

also the decision of the ITAT, Hyderabad 'A' Bench in the case of **DCIT vs. Navabharath Co-op. Urban Bank Ltd.,** in ITA No.822/Hyderabad/2018, dated 09/10/2015.

**14.** On the other hand, Id. Departmental Representative supported the orders of the authorities below.

**15.** We have heard both the parties, perused the material available on record and gone through orders of the authorities below.

**16.** The only issue for our consideration is whether the interest on share capital paid by the assessee-bank is allowable or not. According to the Id. CIT(A), the interest payment made by the assessee bank is in lieu of dividends, as such it amounts to application of profit and not a charge on profit, therefore, it is not allowable. The same issue has been considered by the coordinate bench of the tribunal in the case of ACIT Vs. Visakhapatnam Cooperative Bank Ltd., in ITA No. 05/Vizag/2011, dated 29/08/2011, wherein it has been held that interest paid on share capital goes to reduce the interest collected by the society from its members and it would not form part of the profit. The relevant portion of the order is extracted as under:-

"5. Now, we shall take up the appeal of the assessee. The solitary issue urged in this appeal relates to the eligibility of deduction of claim made under the head "Interest on share

capital". The Learned CIT(A) has upheld the view of the Assessing Officer that the said payment is only an appropriation of profits and not a charge on profit.

6. However, according to the assessee, the said payment is not an appropriation of profit, but expenditure incurred by it in the ordinary course of business. The contentions of Learned A.R in this connection are summarized below:

(a) The assessee is a co-operative society carrying on banking business. It can lend or advance money only to its members. Accordingly the intended borrowers are required to subscribe to the share capital at a certain percentage of the loan amount. Only recently, vide circular no.UBD.BPD.(PCB). Cir.No.22/09.18.201 /2010-11 dated 15-11-2010, the Reserve Bank of India has exempted Urban Co-operative Banks fulfilling certain criteria, from the mandatory requirement of linking share capital to the borrowing norms.

(b) Thus the public subscribe to the share capital of the co-operative societies as a condition for obtaining loan, where as in the case of limited companies, the public subscribe to the equity share capital as an investment with the expectation of appreciation of share values. Further, in the case of co-operative society, a member can withdraw the share capital on ceasing to be a member and such kind of refund of share capital is not permissible in the case of limited companies. Hence there is wide variation in the purpose and characteristics of the "share capital" in the hands of co-operative societies and limited companies. In the instant case, clause 42 of the Bye-Laws of the assessee society prescribes the rules for linking share capital to the borrowers.

(c) Since the borrowers are compelled to subscribe to the share capital, the nature of their contribution is akin to making of margin money deposits and hence the interest paid on the share capital should be treated as expenditure.

(d) Section 16(1) of the A.P. Mutually aided co-operative societies Act, 1995 provides for the disposal of surplus. This section mandates for the payment of interest on share capital not exceeding the rate of interest paid by scheduled banks. Hence there is mandatory requirement for payment of interest on share capital. Clause 46 of the Bye-Laws of the assessee also provides for making the said payment.

(e) The Government of Andhra Pradesh has issued Guidelines for framing Bye-Laws of a Co-operative society, in which the object behind payment of interest on share capital is explained as under:

"Nonetheless, it should be our endeavour to protect our members' share capital from inflation, and if possible, to pay

*an interest on it equal to the maximum rate that commercial banks pay on fixed deposits. In early years, however, we may be able to pay only a nominal rate of interest, if any"*

*Thus the object of payment of interest on share capital is only to keep the monetary value of the share capital in tact for the share holders, which is similar to the objective of keeping money in deposits with the bank. Hence such a payment is expenditure in the hands of the co-operative society.*

*(f) The Income tax Act permits deduction of interest paid to the partners in the case of partnership firms, however, subject to the conditions prescribed under section 40(b) of the Act. The partners are akin to the members in the case of "Co-operative societies". Further u/s 40(ba) of the Act, the interest paid to the members of an "Association of Person" is not allowed as deduction. However the "Co-operative societies" are specifically exempted from the definition of "Association of Persons" in section 40(ba), meaning thereby the Income tax Act does not debar deduction of payment of interest to the members of a co-operative society.*

*(g) The interest expenditure is allowed under section 36(1)(iii) of the Act . The said section states that the amount of interest paid in respect of capital borrowed for the purposes of the business or profession shall be allowed as deduction while computing the income from business. The Hon'ble Supreme Court in the case of Munjal Sales Corporation Vs. CIT (2008)(298 ITR 298) has observed that section 40(b)(iv), which allows payment of interest to partners, have to be read along with section 36(1)(iii) of the Act. Hence both section 36(1)(iii) and section 40(b)(iv) of the Act go together.*

*(h) The term "Capital borrowed" signifies that there is a liability to repay the capital so borrowed. In the case of Pepsu Road Transport Corporation Vs. CIT (1981)(130 ITR 18)(P&H), the share capital provided by the Central and State Government was not treated as "borrowed capital" only for the reason that there was no obligation to refund the capital so provided. However, in the case of co-operative societies, there is a liability to repay the share capital when the concerned member ceases to be a member. Hence "Share capital" in the hands of co-operative societies should be treated as "Borrowed Capital".*

*(i) In the case of Jamshedpur Motor Accessories Stores Vs. CIT (1974)(95 ITR 664), the Hon'ble Patna High Court has held that the payment of share of profit to the financiers in lieu of interest is not uncommon and hence, if such a payment was made on the ground of commercial expediency, the same is allowable as deduction.*

(j) In the case of *CIT Vs. T.T.D Co-operative Stores Ltd., (1998)(232 ITR 109)(A.P)*, the rebate to be given to its members was ascertained only at the end of the year at the time of making up of accounts. The revenue treated the said payment as appropriation of profit. However, the Hon'ble Andhra Pradesh High Court has held that the rebate so given is not part of profit at all but it goes to reduce the price of the goods sold by the co-operative society. Accordingly the rebate so given was allowed as a deduction. The same principles apply in the instant case also.

(k) The assessee has claimed the "interest on share capital" as expenditure in its profit and loss account, i.e. it is not shown as appropriation of profit.

(l) The interest so paid to the share holders is taxable in their respective hands. If the said payment is disallowed in the hands of the assessee, it would lead to double taxation.

7. The contentions of Learned D.R are summarized below:

(a) Under the Income tax Act, the payments made towards trading liabilities and which are "Charge on Profits" are only allowed as deduction.

(b) In the instant case, the interest is paid on "share capital". The said payment partake the character of "Dividend", which is an appropriation of profit.

(c) The Partnership firms and Association of Persons are not legal entities. Under the Act, the payment of interest on capital is not allowed as a deduction except for the partnership firms.

(d) For the purpose of computing income under the Income tax Act, the provisions of the Income tax Act alone should be considered, i.e. the provisions of any other law are not required to be considered.

(e) The payment of interest on capital is prescribed u/s 16(1) of the A.P. Mutually aided Co-operative Societies Act, 1995 under the head "Disposal of Surplus", i.e. the said payment is only an appropriation of profit and not a charge on profit.

(f) The double taxation is not new to the Income tax Act. Under the old scheme of taxation of Partnership firms, the income of the firm was subjected to tax both in the hands of the firm as well as in the hands of the partners.

(g) There is no provision under the Income tax Act to allow deduction of payment of "Interest on share capital". Even under

the Co-operative Act referred (Supra), such payment is permitted while deciding the manner of disposal of "surplus" only.

(h) The criteria of "repayment of share capital" alone cannot be taken support to categorise the impugned payment as "Interest on borrowed capital". Except in the hands of Limited Companies, the capital can be repaid in other forms of business organizations like Individuals, Partnership firms, Association of persons etc. Even in the case of Limited companies, they are permitted to purchase their own shares.

(i) The books of account maintained by the assessee either as per Co-operative Act or as per the guidelines of Reserve Bank of India does not decide the nature of payment. A payment can be allowed as expenditure only if it is a charge on profit or it was incurred to earn the income.

(j) The decision of Hon'ble Supreme Court in the case of Munjal Sales Corporation is concerned with the scope of provisions of sec.40(b)(iv) of the Act. The decision of Hon'ble P & H High court in the case of Pepsu Road Transport Corporation, the assessee there in was not a Co-operative society.

8. In the rejoinder, the Learned A.R submitted the disallowance provided u/s 40(ba) of the Act for interest paid to the members of Association of Persons does not apply to a co-operative society. He further submitted the term "Capital borrowed" used in sec. 36(1)(iii) of the Act should be given wide meaning.

9. We have heard the rival contentions and carefully perused the record. The dispute between the parties revolves around a narrow compass. The claim of the assessee is that the amount paid towards interest on capital is a charge on profit and hence allowable as deduction while computing the income of the assessee. However, the view of the department is that the it is merely an appropriation of profit, since the said payment itself is decided only at the time when the decision on the manner of disposal of "surplus" of the year is taken, i.e., the said payment is decided only after the end of the financial year, that too after deciding the net profit of the year. It is interesting to note that both the parties have taken support of section 16(1) of the A.P. Mutually Aided Co-operative Societies Act, 1995, which reads as under:

"16. Disposal of Surplus:- (1) In any year a Co-operative Society shall allocate towards a deficit cover funds, deferred payment to members as patronage rebate in proportion to their use of the Co-operative Societies services and payment on share capital of interest not exceeding the rate of interest paid by scheduled banks, such percentage of the surplus arising from its business

*transactions in the previous year, as may be approved by the general body."*

*The case of the assessee is that it is mandatory to pay interest on share capital as the word "Shall" is used in the above said section and hence the impugned payment is a charge on profit. On the contrary, the view of the department is that the term "Surplus" is defined to mean the net excess of income over expenditure and hence the disposal of surplus signifies only "Appropriation of Profit".*

10. *However, in our view, the impugned issue needs to be analysed in a different angle. In this connection, we feel it pertinent to discuss about the decision of Hon'ble Jurisdictional Andhra Pradesh High Court in the case of CIT Vs. T.T.D Co-operative Stores Ltd, referred supra. The facts of the said case and the decision rendered by the Hon'ble Court are, in our view, relevant for resolving the issue before us. The assessee in the above said case is also a co-operative society engaged in the business of purchasing provisions and other goods which are sold mostly to the members of society. At the end of the year, after ascertaining the profits, the society declared rebate to its members. The assessee claimed the amount of rebate so distributed as a deduction in computing the income, but the said claim was disallowed by the revenue by holding that the rebate is nothing but an appropriation of its profit. The Tribunal, however, held that the rebate was to be related to the sale price of goods, which should be considered as a provisional price and the rebate is related to the said provisional price. Accordingly it was that the amount of rebate should be allowed as a deduction in appropriating trading profits and not as expenditure incurred. This was so held for assessment years 1980-81 and 1981-82. However, for the assessment year 1982-83, the ITO allowed the deduction of rebate only to the extent of profits of business. This was confirmed by the Tribunal. On these facts, the High court proceeded to answer the following two questions:-*

*(a) Whether, on the facts and in the circumstances of the case, the Tribunal was correct in holding that the payment of rebate to its members was an expenditure wholly and exclusively incurred for the purpose of its business?*

*(b) Whether, on the facts and circumstances of the case, the Tribunal was correct in holding that the appropriation of profits to members under sec. 45 of the Co-operative Societies Act in the name of rebate was not distribution of profits to the members?*

10.1 The Hon'ble Court approved the observations of the Tribunal that the scheme of rebate is that the price at which the goods were sold to the members was taken as a provisional price. When the rebate is given at the end of the year, the provisional price is reduced and the amount received by the society (sales amount) is itself taken at a reduced figure. The Court explained that the deduction goes to the trading account where the figure for sales will be reduced by the amount of rebate given. It is not a case where this deduction on business expenditure is made after ascertaining the gross profit.

10.2 With regard to the question whether the said payment of rebate is appropriation of profit, the High Court observed as under:

"The only objection is that this rebate is given at the end of the year after ascertaining the profit made during the year. That can be an occasion to find out whether the society has a surplus out of which a rebate could be given to the loyal customers. But even if the ascertainment is at the time of making up of the accounts, the actual rebate is related back to the date of sales and the sales figure is reduced in trading account. This is the view taken in *Armour Co-operative Marketing Society Vs. CIT (1987)(167 ITR 565)(AP)*."

10.3 The High court also took note of the following decisions of Hon'ble Supreme Court, which were referred to by the Tribunal and also the counsel for the assessee.

- (a) *Poona Electricity Supply Co. Ltd Vs. CIT (1965)(57 ITR 521)*
- (b) *Associated Power Co. Ltd Vs. CIT (1996) (218 ITR 195)*

We extract below the observations made by the Hon'ble Supreme Court in this regard:

"The Tribunal also referred to the decision of the Supreme Court in *Poona Electric Supply Co. Ltd.'s case (supra)* in support of their view. In that case, the Electricity Act provided for creating a reserve for the customers, in case the profit is more than the reasonable rate admissible for paying charges to the customers. The Supreme Court pointed out that if the rebate is given, it goes to reduce the price and, therefore, it is a case of the assessee receiving less amount as a profit."

10.4 However, in the case of *T.T.D. Co-operative Stores Ltd., supra*, the counsel for the revenue sought to distinguish the case of *Poona Electric Supply Co. Ltd, (supra)*, by stating that there is no such statutory direction to grant rebate in the case of *T.T.D. Co-*

*operative Stores Ltd. However, the High Court rejected the said contention of the revenue by observing as under:*

*"...but we are of the opinion that there is a clear decision to give rebate to those members of the society who have done large business as an incentive for the purpose of encouraging the co-operative movement and that the rebate is not to be given if there is a loss. Even in the recent decision in Associated Power Co. Ltd. Vs. CIT (supra), the Supreme Court has reiterated the view after quoting the following passage from Poona Electric Supply Co. Ltd's case (supra):-*

*"Under s. 10(1) of the IT Act, tax shall be payable by an assessee under the head "Profits and gains of business" in respect of profits and gains of any business carried on by him. The said profits and gains are not profits regulated by any statute, but profits in a business computed on business principles. They are business profits and not statutory profits. They are real profits and not notional profits. The real profit of a businessman under s. 10(1) of the IT Act cannot obviously include the amounts returned by him by way of rebate to the consumers under statutory compulsion. It is as if he received only from the consumers the original amount minus the amount he returned to them. In substance, there cannot be any difference between a business man collecting from his constituents a sum of Rs.Y in addition to Rs.X by mistake and returning Rs.Y to them and another businessman collecting Rs. X alone. The amount returned is not a part of the profits at all."*

*At the end the High Court observed as under:*

*"After considering various judgments, this Court was led to observe that the income tax was a tax on the real income, i.e. the profit arrived at on commercial principles subject to the provisions of the IT Act. The real profit could be ascertained only by making the permissible deductions. There was a clear cut distinction between deductions made for ascertaining the profits and distribution made out of profits. In a given case, whether the outgoing fell in one or the other of the heads was a question of fact to be found on the relevant circumstances, having regard to the business principles. Another distinction that had to be borne in mind was that between the real profits and the statutory profits, that is, between the commercial profits and the statutory profits, the latter were statutorily fixed for a specified purpose. The Supreme Court emphasized the fact that the amount returned is not a part of profit at all. We, therefore, answer the questions in the affirmative and against the Revenue."*

11. Now we shall turn to the facts prevailing in the instant case. The assessee is a co-operative society governed by "A.P. Mutually Aided Co-operative Societies Act, 1995. It carries on the business of banking, which involves mainly accepting deposits and other sources of funds and deploys them in advancing loans and

*advances. The assessee, being a co-operative society, is entitled to lend or advance money only to its members, i.e., any person who intends to borrow money from the assessee has to necessarily become a member of the assessee society. Clause 42 of Bye Laws of the assessee society prescribes the condition for "Linking Share holding with Loan/Limits and the said clause reads as under:*

**"42. LINKING SHAREHOLDING WITH LOAN/LIMITS:**

- a) *A borrower should hold share capital at least 5 percent of his borrowings, if such borrowing is on an unsecured basic i.e. in the form of clean overdrafts, loan against one or two personal sureties and purchase/discount of clean bills and cheques.*
- b) *A borrower against tangible securities should hold share of the Bank to the extent of 2.50percent of his borrowings from the Bank except Gold loan borrowers.*
- c) *In the case of loans for small scale industrial units the linking of share capital might be fixed initially at one percent of the borrowings, to be raised in the course of next two years to 2.5percent.*
- d) *The share linking prescribed in the clause shall not however, apply to the loans granted to nominal member against pledge of gold jewels and silverware.*
- e) *Loans may however, be granted to non-members on the security of their deposits with the Bank".*

12. *The Co-operative societies in the province of Andhra Pradesh were initially governed by "The Andhra Pradesh Co-operative Societies act, 1964". Subsequently, the Andhra Pradesh State Government brought in a new Act named "The Andhra Pradesh Mutually Aided Co-operative Societies Act, 1995 to bring all the mutually aided co-operative societies under the new Act. The Statement of objects and reasons given for the new Act reads as under:*

*"An Act to provide for the voluntary formation of Co-operative Societies reliant business enterprises, based on thrift, self-help and mutual aid and owned, managed and controlled by members for their economic and social betterment and for the matter connected therewith or incidental thereto.*

*.....*

*Over the years, however, increased State participation in the financing and management of co-operatives has led to an unfortunate situation where co-operatives themselves, by and large, have started to perceive themselves not as member-controlled, member-sensitive business, guided by the universally accepted principles of co-operation, but as channels for*

*Government subsidies and largesse. Sound and sustainable co-operative business, accountability, responsibility and self-reliance have taken a back seat.*

....

*On the other hand, the Government recognizes that there are some Co-operatives which may have some Government funds but are not dependent upon such funds or on Government assistance in other forms for their survival. These co-operatives need to be given greater autonomy and encouraged to pursue to legitimate interests of their members in an effective, self-reliant, responsible, accountable and democratic manner. The Government also recognizes that enabling legislation is required if ordinary people who expect to benefit from the co-operative form of business, without being dependent on Government resources, are to voluntarily promote and effectively develop services for themselves through their own Co-operative societies."*

*Thus it can be seen that the Object and reasons for bringing in a new legislation clearly recognizes and further gives stress to the necessity of developing co-operative societies as a member-controlled, member-sensitive business institution with the aim of achieving economic and social betterment of its members.*

13. *The Andhra Pradesh Government has issued guide lines for framing Bye-laws of a Co-operative society. In clause 30 of the said guide line, under the head "Interest on Share Capital", the Government has brought out the distinguishing features of "Share Capital" belonging to a limited company and a co-operative society in the following lines:*

### **30. Interest on Share Capital**

*"In other forms of business, people invest with the hope that their investment will earn them the maximum possible returns. However, in a cooperative, members invest in order that they can set up services which they are in need of, from the provision of which, they can get significant financial benefit. That is, they expect to benefit, not from direct return on the investment, but from the services provided by the cooperative, as a result of the investment.*

*Nonetheless, it should be our endavour to protect our members' share capital, from inflation, and, if possible, to pay an interest on it equal to the maximum rate that commercial banks pay on fixed deposits. In early years, however, we may be able to pay only a nominal rate of interest, if any.*

*Section 16 of the Act itself does not permit us to give more interest than the banks and, therefore, we may want to include in our bye-laws that each year our general body will decide how much interest to give on share capital, such, however, that it does*

*not exceed the maximum interest payable by scheduled banks, on fixed deposits”.*

*Thus it is brought out clearly that the objective of subscribing to the share capital of a co-operative society is only to avail its services which the members themselves set up at the time when they are in need of so that they can get significant financial benefit. It is also stated in the guide line that section 14 of the new Act does not permit the Co-operative societies to raise share capital from Government or other non-members.*

*14. Another distinguishing feature in the case of co-operative societies is that the share capital collected by a co-operative society from a person shall be refunded to him on his ceasing to be a member. This kind of refund of share capital is not permitted under the Companies Act. A share holder of a limited company has to transfer or sell the shares to any other person in order to realize his investment. Only recently, the Limited companies are permitted to purchase their own shares and such purchase cannot be equated to refund of share capital. In our view, the Co-operative Societies are permitted to refund the share capital in tune with its objective of providing services to its members only. In case of co-operative societies carrying on banking business, this provision enables it to lend or advance money only to its members.*

*15. From the foregoing discussions, it becomes clear that the mutually aided Co-operative Societies exist solely for the mutual benefit of its members. In the instant case, the assessee herein is required to lend or advance money only to its members, the object of which is that the benefits arising out of the business should be shared by the members only inter se.*

*16. In this back ground, if we look at the impugned issue, i.e. the interest paid on share capital, the ratio laid down by Hon'ble jurisdictional A.P. High Court in the case of CIT Vs. T.T.D. Co-operative Stores Ltd, (Supra), by following the Supreme Court's decisions referred (Supra), squarely apply to the facts of the instant issue. In the case of T.T.D. Co-operative Stores Ltd., (Supra), the members were sold goods at a particular rate and at the time of finalizing the accounts, a rebate was given to the members as a special incentive for increasing societies business. The claim of the revenue that the said rebate is only appropriation of profit was rejected by the Hon'ble High Court. The amount of rebate was treated as a reduction in the sales figure on the reasoning that*

- (a) *the initial sales amount is considered as provisional price for the goods sold.*
- (b) *the rebate determined at the end of the year after ascertaining the profit made during the year is taken as the occasion to find out whether the society has a surplus out of which a rebate could be given to the loyal customers.*
- (c) *The said payment is backed by a clear decision to give rebate.*
- (d) *the actual rebate relate back to the date of sales and the sales figure is reduced in the trading account, even if the ascertainment of rebate is at the time of making up of the accounts.*
- (e) *the net profit is ascertained only after allowing the rebate, which goes to reduce the price at which members purchased the goods from the society, i.e. it is not a case where this deduction on business expenditure is made after ascertaining the gross profit.*
- (f) *There is distinction between the "real profits" and the "statutory profits", that is between the commercial profits and the statutory profits, the latter were statutorily fixed for a specified purpose. The income tax was a tax on the real income, i.e. the profit arrived at on commercial principles subject to the provisions of the IT Act.*

17. *In the instant case, the business of the assessee society is banking business, wherein the "cash" forms the working commodity. The business of banking, inter alia, consists of taking deposits and advancing loan. In the instant case there is no dispute with regard to the fact that the loans are advanced only to the members and the borrower has to necessarily subscribe to the share capital of the assessee society in order to avail the loan facility.*

18. *The Hon'ble Supreme Court has explained the concept of "reduction of sales price" vis-à-vis the rebate by giving an example and the same was extracted by us in paragraph 10.4 (Supra). We are of the view that the concept so explained by Hon'ble Supreme Court equally applies in the instant case also. We shall explain the same by giving an example. Suppose, a person, say Mr. X, approaches the assessee society for availing a loan of say, Rs.1,00,000/-. Let us assume that he is required to purchase shares worth Rs.5,000/- from the share capital of the assessee society. In that case, Mr. X will pay Rs.5,000/- to the assessee society and the assessee society will give a loan of Rs.1,00,000/- to Mr. X. In effect, Mr.X would receive a net amount of Rs.95,000/- only from the assessee society. Similarly, the net amount which goes out of the coffers of the assessee society is also `95,000/- only. However, the assessee society would charge*

*interest at applicable rate on the loan amount of Rs.1,00,000/-, even though the net amount received by Mr.X is only Rs.95,000/-, i.e., that the assessee society is collecting interest, not only on Rs.95,000/-,being net cash out flow from its coffers, but also on the amount of Rs.5,000/- given by Mr. X as Share capital. At the end of the year, the assessee society may determine the amount of interest payable on the share capital out of the surplus. In the above said example, the assessee society would pay interest on the amount of Rs.5,000/- given as share capital. In that case, as per the ratio of the Hon'ble Supreme Court and the Andhra Pradesh High Court in the cases cited in para 10 and para 10.3 (Supra), the interest so paid on the share capital actually goes to reduce the amount of interest that was collected initially by the assessee society from Mr. X.*

*19. As stated earlier, it was held in those cases that the income tax is to be levied on the "real income", i.e. the profit arrived at on commercial principles subject to the provisions of the Income tax Act. Accordingly it was held that the rebate given to the members is not a part of profit at all. In the instant case also, it has to be held that the amount paid by the assessee as "interest on share capital", in the instant year, goes to reduce the gross interest collected by it from its members and it would not form part of profit at all. We order accordingly."*

**17.** In the above referred to case, the coordinate bench of the tribunal has given a specific finding that the assessee is a cooperative society, governed by the A.P. Mutually Aided Cooperative Societies Act, 1995. The above judgment has been followed again in the case of assessee itself in ITA No. 449 & 450/Vizag/2012 dated 30/09/2016. The relevant portion of the order is extracted as under:-

*"22. We have heard both the parties, perused the materials available on record and gone through the orders of the authorities below. In this case, the assessee has debited an amount of Rs.1,57,53,620/- towards interest on share capital. It was submitted that as per the section 16 of the A.P. Mutually Aided*

*Cooperative Societies Act, 1995, it is an allowable expenditure. The A.O. has not accepted the explanation of the assessee and he has observed that the assessee has to allocate the interest on share capital only upon determination of the surplus arising from the business i.e. net profit. This is nothing but appropriation of profits but not an expenditure incurred for carrying on the business. The Ld. CIT(A) by following the decision of the coordinate bench of the Tribunal in assessee's own case for the assessment year 2007-08 in ITA No.5/Vizag/2011 & 19/Vizag/2011 for A.Y. 2007-08 vide order dated 29.8.2011 has directed the A.O. to delete the addition made by him. It is submitted across the bar that the very same issue in the assessee's own case is pending before the Hon'ble High Court. In view of the above, by following the coordinate bench of the Tribunal, in view of the doctrine of precedent, we dismiss this ground of appeal raised by the Department."*

**18.** A similar issue has been considered by the ITAT, Hyderabad 'A' Bench in the case of Navabharath Co-op. Urban Bank Ltd., (supra) wherein the Tribunal has held that in the case of cooperative society, there is a liability to repay the share capital to its members concern once become a member. Therefore, the share capital in the hands of the cooperative society is to be treated as a borrowed capital. A similar issue was considered by the coordinate bench of the tribunal in the case of Visakhapatnam Cooperative Bank Ltd., (supra) wherein it has been held that interest paid on share capital goes to reduce the gross interest paid by the assessee from its members and it would not form part of profit. Respectfully following the above decision of the coordinate bench of the tribunal in the case of Visakhapatnam

Cooperative Bank Ltd., (supra) as also the decision of ITAT, Hyderabad 'A' Bench in the case of Navabharath Co-op. Urban Bank Ltd., (supra), we hold that interest paid on share capital goes to reduce the interest collected by the society from its members, would not form part of the profit. By considering the facts of the present case and also by following the decision of the coordinate bench of the tribunal in the case of Visakhapatnam Cooperative Bank Ltd., in ITA No. 05/Vizag/2011, dated 29/08/2011 & ITA Nos. 449 & 450/Vizag/2012 dated 30/09/2016; and also the decision of ITAT, Hyderabad 'A' Bench in the case of Navabharath Co-op. Urban Bank Ltd (supra), this ground of appeal raised by assessee is allowed.

**19. Ground No.5** relating to confirmation of disallowance of Rs.7,86,356/- made towards **gratuity premium payment**. Originally, this amount was not offered for taxation. Subsequently, by filing a revised computation under protest, gratuity amount was offered for taxation. On appeal it was submitted before the Id. CIT(A) that this amount is already paid to the employees and therefore it cannot be subject to tax. However, Id. CIT(A) has not accepted the explanation given by the assessee on the ground that the assessee himself filed a revised

return of income and offered this amount to tax and dismissed the ground raised by the assessee.

**20.** On appeal before us, Id. counsel for the assessee has submitted that the amount of Rs. 7,86,356/- is in respect of gratuity payment, which has already been paid to the employees and therefore it cannot be taxed and submitted that the issue may be remitted back to the file of the Assessing Officer for fresh consideration in accordance with law.

**21.** On the other hand, Id. Departmental Representative strongly supported the orders of the authorities below.

**22.** We have heard both the parties, perused the material available on record and gone through orders of the authorities below.

**23.** From the facts available on record, we find that the assessee has made the payment of Rs. 7,80,565/- in respect of gratuity. In the original return of income, this amount was not offered for taxation. When the department asked, as to why this amount was not offered for taxation, the assessee in his revised computation of income, the same is offered for taxation with a protest. The case of the department is that for the payment of gratuity, the assessee has to take an approval from the Commissioner, there is no approval has been taken, therefore directed the assessee to

offer gratuity payment for taxation. The case of the assessee is that the amount which has already been paid and is a genuine payment, the payment is not doubted, therefore it cannot be disallowed. By taking into consideration of the facts of the case, we are of the opinion that this issue has not been properly examined neither by the Assessing Officer nor by the Id. CIT(A), who simply rejected the claim of the assessee. We therefore are of the opinion that this issue has to be remanded back to the file of the Assessing Officer for fresh consideration in accordance with law. Accordingly, we set aside the order passed by the Id. CIT(A) and remit the issue back to the Assessing Officer for fresh consideration.

**24. Ground No.6** relating to the confirmation of disallowance of Rs. 22,96,950/- made towards **Establishment fund**. The assessee had debited an amount of Rs. 22,96,950/- to the profit & loss account towards payment to establishment fund. The Id. CIT(A) directed the Assessing Officer to examine and report the same. The Assessing Officer reported the Id. CIT(A) that the above amount is debited to establishment fund and no explanation was offered by the assessee, and submitted that same may be considered for disallowance. The Id. CIT(A) after considering the report of the Assessing Officer, asked the assessee, to explain why

the amount debited to the profit & loss account should not be disallowed and added to the total income. It was submitted before the Id. CIT(A) that the bank created establishment fund is to meet unforeseen expenditure that may arise in future to staff salaries, VRS, gratuity etc. The bank created this fund to the extent of Rs. 80.00 lakhs (F.Y. 2004-05 Rs. 40.00 lakhs + F.Y. 2005-06 Rs. 40.00 lakhs). As per section 116C(1) of the Cooperative Societies Act, the bank shall not pay exceeding 30% of gross profit or 2% of working capital, whichever is less towards pay and allowances. It was further submitted that during the year, the bank had paid salaries of Rs. 2,37,07,648/- by debiting Rs. 2,14,10,698/- to staff salaries and allowance account and balance amount from establishment fund. The establishment fund was recouped by the difference amount of Rs. 22,96,950/- from profit & loss account. It was further submitted that the General Body authorized the excess payment of Rs. 22,96,950/- from the establishment fund and submitted that the payment made from the establishment fund to the salaries of employees is allowable expenditure under section 37(1) of the Act. The Id. CIT(A) considered the explanation given by the assessee and by following the decision of the Hon'ble Jurisdictional High Court in the case of **A. Subramanyam Naidu & others vs. Government of Andhra**

**Pradesh** reported in 2005 (5) ALD 682, held that section 116C(1) of the AP Cooperative Societies Act is mandatory in nature and society cannot violate this mandatory requirement on the plea that it has to fulfil certain obligations under the Minimum Wages Act or the Industrial Disputes Act, disallowed the amount of Rs.22,96,950/- and added to the total income of the assessee. For the sake of convenience, the relevant portion of the Id.CIT(A)'s order is extracted as under:-

*"8.5.5 I have considered the submissions made. It is evident that the payment of salaries and allowances beyond the limit prescribed by the statute in Sec. 116C has been made from the Establishment Fund, and the Establishment Fund has been recouped for this excess amount paid from the profit and loss account. The issue is whether such payment made into the Establishment Fund would be an allowable deduction. It is pertinent to note that there is a statutory bar that a society cannot incur expenditure exceeding 30% of gross pay or 2% of working capital. In the case of A. Subramanyam Naidu and others v Govt of A.P. 2005, (5) ALD 682, the Andhra Pradesh High Court has held that sec.116C(1) of the AP co-operative societies Act is mandatory in nature. In that judgment, the Honourable High Court has observed that the society cannot violate mandatory requirement on the plea that it has to fulfill certain obligations under the Minimum Wages Act or the Industrial Disputes Act. The fulfillment of the statutory requirement under sec.116C of the Act is mandatory and is in the interest of the society which would enable the Society to meet its requirements under other legislations."*

**25.** On appeal, Id. counsel for the assessee has submitted that excess creation of establishment fund neither violated nor it is

prohibited by law. The expenditure incurred by the assessee is a genuine expenditure and therefore, the same has to be allowed.

**26.** On the other hand, Id. Departmental Representative strongly supported the orders of the authorities below.

**27.** We have heard both the parties, perused the material available on record and gone through orders of the authorities below.

**28.** In this case, Id. CIT(A) gave a categorical finding that the assessee by creating establishment fund, violated section 116C of the A.P. Cooperative Societies Act, which is mandatory in nature. The Hon'ble Jurisdictional High Court in the case of A.Subramanyam Naidu & others (supra) has considered and held that the society cannot violate the mandatory requirement on the plea that it has to fulfil certain obligations under the Minimum Wages Act or the Industrial Disputes Act. The fulfilment of the statutory requirement under section 116C of the Act is mandatory and is in the interest of the society which would enable the society to meet its requirements under other legislations. The Id. CIT(A) by following the same, directed the Assessing Officer to disallow the amount of Rs. 22,96,950/- and add the same to the total income of the assessee. We find no reason to interfere with the

order of the Id. CIT(A). Thus, this ground of appeal raised by the assessee is dismissed.

**ITA No.177/VIZ/2013**

**29.** Grounds No. 1 & 8 are general in nature, no adjudication is required, therefore, same are dismissed.

**30.** Ground No.2 relating to Bonus & Exgratia payment, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.2. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is dismissed. ||

**31.** Ground No.3 relating to leave encashment payment, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.3. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is dismissed.

**32.** Ground No.4 relating to interest on share capital, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.4. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is allowed.

**33.** Ground No.5 relating to gratuity premium payment, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.5. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is allowed for statistical purposes.

**34.** Ground No.6 relating to establishment fund, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.6. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is dismissed.

**35.** Ground No.7 relating to disallowance of addition of Rs.11,10,000/-. The Assessing Officer has not made any addition in the assessment order, however, the Id. CIT(A) directed the Assessing Officer to examine whether the amount of Rs.11,10,000/- debited as investment depreciation reserve is allowable as per law or not. The Assessing Officer after verification, submitted a report to the Id. CIT(A), wherein he has stated that the amount of Rs. 11,10,000/- is debited as investment depreciation reserve and also stated that this amount represents the difference between face value of the investment and purchase price of the investment and the same is not allowable. The Id. CIT(A) by considering the remand report submitted by the Assessing Officer, asked the assessee to explain how this claim is allowable. It was submitted before the Id. CIT(A) that as per RBI guidelines, provision is required to be made for depreciation on investments held under available for sale or held for trading category. Accordingly, the bank has debited Rs.11,10,000/- towards depreciation for reduction in market price

on investments, therefore, same is allowable. The Id. CIT(A) has considered all the details, in his order at paragraph Nos. 11.5.3 & 11.5.4 and finally held as under:-

*"The total appreciation comes to Rs.15,02,928/- and the depreciation comes to Rs. 11,45,215/-; the net depreciation can be taken to be NIL. Thus, the net position is one of appreciation and not depreciation. Further, it is noted that the scrip APSDL 2014 @ 5.60% maturing on 23/04/2014 was not valued as per the regulation. As the net position is found to positive, this aspect does not need further verification. In view of the above factual position, the claim of depreciation of investment of Rs. 11,10,000/- is not allowable. Accordingly, the AO is directed to make the disallowance of Rs. 11,10,000/- and add it to the total income. This issue is accordingly disposed off."*

We find no infirmity in the order passed by the Id. CIT(A).

Thus, this ground of appeal raised by the assessee is dismissed.

#### **ITA No. 517/VIZ/2014**

**36.** Ground Nos. 1, 2, 3 & 9 are general in nature, no adjudication is required, therefore, same are dismissed.

**37.** Ground No.4 relating to establishment fund, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.6. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is dismissed.

**38.** Ground No.5 relating to interest on share capital, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.4. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is allowed.

**39.** Ground No.6 relating to leave encashment, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.3. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is dismissed.

**40.** Ground No.7 relating to gratuity premium payment, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.5. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is allowed for statistical purposes.

**41.** Ground No.8 relating to disallowance of contingency fund. The Assessing Officer has noted that the assessee had debited an amount of Rs. 5.00 lakhs towards contingency liability, the details of which were not furnished for verification. As the amount was towards provision and as no details were furnished, the Assessing Officer made the impugned disallowance. Even before the Id.CIT(A), no details were filed, even before us also, no details are filed. Therefore, we find no infirmity in the order passed by the Id.CIT(A). Thus, this ground of appeal raised by the assessee is dismissed.

**ITA No. 173/VIZ/2015**

**42.** Ground Nos. 1 & 6 are general in nature, no adjudication is required and therefore same are dismissed.

**43.** Ground No.2 relating to interest on share capital, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.4. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is allowed.

**44.** Ground No.3 relating to disallowance of provision for leave encashment, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.3. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is dismissed.

**45.** Ground No.4 relating to gratuity premium payment, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.5. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is allowed for statistical purposes.

**46.** Ground No.5 relating to establishment fund, is a similar ground raised in ITA No. 176/VIZ/2013 as ground No.6. In view of our decision in the above referred to appeal, this ground of appeal raised by the assessee is dismissed.

**ITA No.195/VIZ/2013**

**47.** Grounds No. 1 & 8 are general in nature, no adjudication is required and therefore same are dismissed.

**48. Ground Nos. 2 & 3** are relating to **violation of Rule 46A** of the IT Rules, 1962. We find that Id. CIT(A) after calling remand report and examined each and every issue independently, passed

the order, therefore, there is no violation of Rule 46A. Thus, these grounds of appeals raised by the Revenue are dismissed.

**49.** Ground No. 4 relating to sustenance of addition of unsecured loans under section 68 of the Act. The Assessing Officer has added savings bank, special savings bank, short term deposits and various categories of deposits including opening balances as unsecured loans and addition was made under section 68 of the Act. Before Id. CIT(A), it was submitted that assessee has accepted various deposits as per KYC norms and also guidelines of the Reserve Bank of India and the same are regularly submitted under section 285BA of the Act, therefore, the Assessing Officer is not justified in invoking the provisions of section 68 of the Act. The Id. CIT(A) after considering the explanation of the assessee, directed the Assessing Officer to verify the complete details of fresh deposits received during the year and submit the factual report. The Assessing Officer after verifying the details, submitted a report to the Id. CIT(A), which is as follows:-

*"3. The assessee has furnished information regarding various types of deposits accepted and held. In this regard, it is found from the record that the total deposits under the heads term deposits, savings bank, special savings bank, current, recurring deposits and others, held by the bank as on 31/03/2009 is Rs. 131,25,89,511/-. The same has shown me a random sample of deposit application.*

*3.1. Since the assessee-bank did not comply with the show cause letter dated 21/10/2011 and notice under section 142(1) of*

*the same date, the addition of Rs. 131,25,89,511/- was deemed as unsecured loans as shown by the assessee –bank against col. No. 2(b)(ii) of Part-A-BS of the ITR-5, which was electronically uploaded.”*

**50.** The Id. CIT(A) after considering the remand report and also considering the details filed by the assessee, deleted the addition made by the Assessing Officer by observing as under:-

*"7.8 I have carefully considered the details and submissions made by the appellant on this issue. It is evident that the amount of Rs.131,25,89,511/- represent the closing balance of all the deposits held by the bank as on 31-03-2009. It is pertinent to note that these include opening balance, deposits made into savings account, renewed deposits and other deposits. The appellant reduced the application forms taken from depositors for the deposits made into savings account, renewed deposits and other deposits. The appellant produced the application forms taken from depositors for the deposits made. They were perused and found to be obtained in the normal course of the banking business. The statements filed before RBI in forms OSS-1, (quarterly return), Form No.9 (Monthly return), and form I (Maintenance of CRR and SLR ratio) were submitted on requisition, by its letter dated 16-1-2012, The deposits collected were periodically reported in these forms and the bank has maintained its SLR and CRR with reference to the deposits held by it. All this documentation clearly indicates that the amount represents deposits which were collected in the normal banking business and cannot be characterized as unsecured loan. The AO appears to have proceeded on the impression that these represent unsecured loan, probably for the reason that these were shown as unsecured loan by the assessee-bank against col.No.2(1b)(ii) of Part-A-BS of the ITR-5, which was electronically uploaded. The erroneous impression could not have been dispelled as the assessment was completed under sec. 144 of the I.T.Act. The details of depositors submitted in the CD were also test checked with the application forms, and no discrepancy was noticed. The AO had also not reported any discrepancy in his remand report. The RSI Inspection report also show adherence to the KYC norms.”*

**51.** On appeal before us, Id. Departmental Representative is not able to point out any error in the order of the Id. CIT(A). The Id.CIT(A) after examining all the details and also remand report and also fresh deposits received during the year, deleted the addition made by the Assessing Officer. We find no infirmity in the order passed by the Id. CIT(A). Thus, this ground of appeal raised by the Revenue is dismissed.

**52.** Ground Nos. 5 & 6 relate to addition of Rs. 60,66,867/-. In the assessment order, the Assessing Officer has disallowed an amount of Rs. 60,66,867/- being 50% of the expenses claimed in the profit & loss account on *ad hoc* basis. On appeal before the Id.CIT(A), it was submitted that the entire expenses are fully vouched and are relating to business of the assessee. The Assessing Officer without examining the details simply disallowed the expenses on *ad hoc* basis which is not permissible under the law. The Id. CIT(A) directed the Assessing Officer to examine the details of the expenses and submit the report. The Assessing Officer after examining the details submitted a remand report, which is as follows:-

*"Since the assessee bank did not comply with the show cause letter dated 21/12/2011 and notice under section 142(1) of the same date, the addition of Rs. 60,66,867/- was made by disallowing 50% of the other expenses shown by the assessee -*

bank at Col. No. 36 of Part A- P & L a/c of ITR-Vs. Which was electronically uploaded.

The assessee bank furnished the details of other expenses amounting to Rs,98,65,416/- as per Annexure IV enclosed to the letter filed in this office on 22-2-2012. While the claim of expenditure is Rs.1,21,33,731/-, details are only provided for Rs.98,65,418/- leaving a balance of Rs.22,68,313/-. In the absence of any evidence for the same, this amount of Rs.22,68,313/- needs to be disallowed."

**53.** The Id. CIT(A) called the assessee to explain in respect of disallowance suggested by the Assessing Officer to the extent of Rs. 22,68,313/-. The assessee submitted all the details before the Id. CIT(A) in respect of the expenditure incurred. The Id. CIT(A) after considering the explanation given by the assessee and also considering all the details available on record, deleted the addition made by the Assessing Officer. The relevant portion of the order of Id. CIT(A) is extracted as under:-

"With reference to point no.6, the detailed break up of other expenses of Rs.1,21,33,731/- shown in the return of income is given below. Out of the total operating expenses of Rs.98,65,418/- the expenditure towards hospitality, conference, conveyance telephone, travelling and fringe benefit tax included in rent, taxes and lighting aggregating 20,17,382/-, the balance figure of operating expenses of Rs.78,48,035/- is shown under head other expenses in the e filed return of income. If this break up is taken into consideration there is no difference at all as alleged by the Assistant commissioner in his report.

Operating expenses	78,48,035
Investment Amortization	3,75,695
Special Reserve	9,00,000
Computerization fund	18,90,000
Investment Depreciation reserve	11,10,000
Reserve for shares	1,00,001
Total	1,21,33,731

10.4 The appellant has produced the ledger extract containing the break up for the operating expenses amounting to Rs.98,65,418/-. This has been verified by the A.O. as seen from his remand report. The AR pointed out that these expenses are categorized into two amounts [Rs.78,48,035+FBT Rs.1,16,517/-, and Rs.19,00,685/-]. The ARs also submitted that the AO deducted the amount of Rs.19,00,685/- from other expenses of Rs.42,85,696/- to arrive at the amount of Rs.22,53,313/-. Hence, the Appellant was asked to substantiate the allowability of the other expenses amounting to Rs.42,85,696/-. The ARs submitted that the expenses relating to Special Reserve of Rs.9,00,000/-, computerization fund of Rs.18,90,000/- and Reserve for Share of Rs.10,001/- has been added back, and in support of which the revised statement of income filed was produced. The allowability of the expenses relating to investment amortization, and investment depreciation reserve is discussed in the forthcoming paras. Therefore, in the light of the above factual position, the -ad hoc disallowance of 50% of the other expenses is not justified. Accordingly the addition of Rs. 60,66,867/- is deleted."

**54.** Ld. Departmental Representative has not pointed out any error in the order passed by the Id. CIT(A). The Id. CIT(A) after careful consideration of all the details, passed the order. We find no infirmity in the order passed by the Id. CIT(A). Thus, this ground raised by the Revenue is dismissed.

**55.** Ground No.7 relates to sustenance of addition of Rs.62,12,660/- towards sundry creditors. The Assessing Officer disallowed sundry creditors to the tune of Rs. 23,79,60,181/- by invoking the provisions of section 68 of the Act. The Id. CIT(A) directed the Assessing Officer to examine the details and asked him to submit remand report. The Assessing Officer has submitted the remand report, which is reproduced as under:-

"4. Since the assessee-bank did not comply with the show cause letter dated 21-10-2011 and notice under sec. 142(1) of the same date, the addition of Rs.23,79,60,181/- was deemed as sundry creditors as shown by the assessee-bank against current liabilities at Col.No.i(A) under current assets, loans and advances of the ITR-5, which was electronically uploaded.

4.1. The assessee bank has furnished the details of such inter-branch contra entries and details of due by items for Rs.3,07,12,370/- and contra entries between head office and branch offices for Rs. 20,68,77,819.25. Thus, there is a difference of Rs. 3,69,992/-, for which no explanation was offered. Hence, this may be considered for addition as unexplained sundry."

**56.** The Id. CIT(A) by considering the remand report submitted by the Assessing Officer and also examining all the details, deleted the addition made by the Assessing Officer by observing as under:-

"The appellant submitted that the sum of Rs. 3,70,000/- represent contra entries for the inward/outward bill collection. The ledger extracts namely schedule 7 and 10 of the balance sheet were also submitted de letter dated 22-8-2012 and 16-12-2013. I have verified the same and found them to be contra entries and revenue neutral. In -the light of the submissions made by the Assessee and the remand report of the Assessing officer, I am of the view that the addition of Rs. 23,79,60,181/- is not sustainable in law. Accordingly, the same is deleted. As a result, the appeal is allowed on this ground."

**57.** Ld. Departmental Representative has not pointed out any error in the order of the Id. CIT(A). The Id. CIT(A) after careful consideration of all the details, passed the order. We find no infirmity in the order passed by the Id. CIT(A). Thus, this ground of appeal raised by the revenue is dismissed.

**58.** In the result, all the appeals filed by the assessee are partly allowed for statistical purposes; and the appeal filed by the Revenue is dismissed.

Order Pronounced in open Court on this 28<sup>th</sup> day of May, 2018.

Sd/-  
**(D.S. SUNDER SINGH)**  
Accountant Member

sd/-  
**(V. DURGA RAO)**  
Judicial Member

**Dated : 28<sup>th</sup> May, 2018.**

*vr/-*

Copy to:

1. The Assessee – The Aryapuram Co-op. Urban Bank Ltd., Near Gokavaram Bus Stand, Rajahmundry, East Godavari District.
2. The Revenue – ACIT, Circle-1, Rajahmundry.
3. The CIT, Rajahmundry.
4. The CIT(A), Visakhapatnam & Rajahmundry.
5. The D.R., Visakhapatnam.
6. Guard file.

By order

Easy & Speedy  
Justice

(VUKKEM RAMBABU)  
Sr. Private Secretary,  
ITAT, Visakhapatnam.