IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "D", MUMBAI

BEFORE SHRI G.S. PANNU, ACCOUNTANT MEMBER AND
SHRI RAM LAL NEGI, JUDICIAL MEMBER

ITA NO. 6538/MUM/2016	:	**A.Y : 2011-12**
Mumbai District Central Co-op. Bank Ltd. 207, Mumbai Bank Bhavan, Dr. D.N. Road, Fort, Mumbai 400 001. (Appellant) **PAN : AAAAM3185D**	Vs.	DCIT-1(3), Mumbai (Respondent)
ITA NO. 6540/MUM/2016	:	**A.Y : 2011-12**
DCIT-1(3)(2), Mumbai (Appellant)	Vs.	Mumbai District Central Co-op. Bank Ltd. 207, Mumbai Bank Bhavan, Dr. D.N. Road, Fort, Mumbai 400 001. (Respondent) **PAN : AAAAM3185D**

Assessee by : Shri Ajay Singh
Revenue by : Shri Chaitanya Anjaria

Date of Hearing : 24/09/2018
Date of Pronouncement : 26/09/2018

O R D E R

PER G.S. PANNU, AM :

These are cross-appeals filed by the assessee and the Revenue, against the order of CIT(A)-3, Mumbai dated 31.08.2016, pertaining to the

Assessment Year 2011-12, which in turn has arisen from the order passed by the Assessing Officer dated 17.02.2014 under section 143(3) of the Income Tax Act, 1961 (in short 'the Act'). Since the cross-appeals involve certain common issues, therefore, they have been clubbed and heard together and a consolidated order is being passed for the sake of convenience and brevity.

2. The assessee before us is a co-operative bank engaged in the business of banking. For the assessment year under consideration, it filed a return of income declaring an income of Rs.2,09,80,965/-, which was subsequently revised declaring NIL income. An assessment u/s 143(3) of the Act was completed on 17.02.2014 determining the total income at Rs.10,18,26,951/- after making certain disallowances/additions which were carried in appeal before the CIT(A), who allowed part-relief. Not being satisfied with the order of CIT(A), assessee and Revenue are in appeal on respective Grounds of appeal, which we shall deal with hereinafter.

3. First, we may take-up the appeal of the Revenue wherein the Grounds of appeal read as under :-

"i. Whether, on the facts and circumstances of the case, CIT(A) is justified in deleting the disallowance of Rs, 4,25,63,473/- shown as "Deduction of Overdue Interest Reserve Provision" on the principle that interest credited of equal amount to profit and loss account is notional income / hypothetical income?

ii. Whether, on the facts and circumstances of the case, CIT(A) is justified in deleting the disallowance of Rs. 4,25,63,473/- shown as "Deduction of Overdue Interest Reserve Provision" when the assessee credited the accrued interest on Non-Performing Assets (NPA) to its profit and loss account?

iii. Whether, on the facts and circumstances of the case, CIT(A) is justified in deleting the disallowance of Rs. 4,25,63,473/- shown as "Deduction of Overdue Interest Reserve Provision" when the assessee is not a public financial institution or a scheduled bank or a State financial corporation or a State industrial investment corporation so as to claim exemption under Section 43D of the Income-tax Act, 1961 from disclosure of interest income on accrual basis as such benefit is available only to those entities which are covered by the said section?"

4. As a perusal of the aforestated Grounds of appeal reveal, the solitary issue raised by the Revenue arises from the action of CIT(A) in allowing the claim of the assessee for deduction of Rs.4,25,63,473/- representing Provision for overdue interest. Pertinently, the relevant facts are that assessee being a co-operative bank identified certain loans and advances which were Non-Performing Assets (NPAs) as per the Income Recognition and Asset Classification Norms issued by the Reserve Bank of India (RBI) from time to time. On such NPAs, interest was not being received by the bank within the stipulated period from the borrowers, although such interest was credited to the Profit & Loss Account. The assessee created a corresponding Provision which was debited to the Profit & Loss Account, which was disallowed on the ground that it was a mere Provision. The CIT(A), however, allowed the claim of the assessee by noticing that under the mercantile system of accounting though the interest on NPAs/sticky loans was credited to the Profit & Loss Account, but such interest was not actually received by the assessee. The CIT(A) took note of the fact that assessee had credited the interest on NPAs in the Profit & Loss Account, but the same was correspondingly debited under the head 'Overdue Interest Provision' account and claimed as a deduction by debiting the aforesaid Provision in the Profit & Loss Account. The CIT(A) noticed that if such debit made to the Profit & Loss Account was disallowed, it would amount to taxing

interest receivable on NPAs without there being any certainty of its receipt. The operative part of the order of CIT(A) in this regard reads as under :-

> *"10.9 In the banking business, a peculiar feature is on interest accrual which is to be taken as income of the bank in the Mercantile System of Accounting. It has two components, one is interest received on Good Loans and another as interest receivable on Non Performing Assets (NPA)/Sticky Loans. The general practice in giving the accounting treatment under the mercantile accounting system is that the interest on (NPA)/Sticky Loans is to be credited in the P&L A/c. Since this interest is not actually received by the bank and the same amount was to be debited under the head "Overdue Interest Reserve Account" to neutralize the actual income of the bank. In the Balance Sheet, the (NPA)/Sticky Loans are shown in the asset side, as well as the "Overdue Interest Reserve Account" is shown under the liability side of the Balance Sheet. During the course of assessment, the AO did not allow amount under head "Overdue Interest Reserve Account" debited to P&L A/c and added back to the income of the appellant. In the result, the interest receivable on NPA/Sticky Loans are taxed without being received during the previous year or uncertain future conditions.*
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> *10.10 On the other hand, if the bank directly taken the NPA/Sticky Loans amount or take the overdue interest reserve in the liability side of the Balance Sheet without taking these two entries in the P&L A/c, then the AO taken a different view to add back the amount under the head "Overdue Interest Reserve Account" and initiated penalty proceedings u/s 271(1)(c) of the IT Act for concealment of income receivable as being taken under the mercantile system of accounting. This situation is disputed by almost all the banks and the same leads to a long litigation between the banks and the department.*
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> *10.11 The issue has come up before the ITAT, Pune Bench in the case of M/s Solapur District Central Co-op. Bank Ltd. vs ACIT, Circle 2, in which the Hon'ble ITAT Pune Bench held that the NPA interest income has to be recognized only on realization and the interest income shown under the head "Overdue Interest Reserve Account" is to be allowed as the same was*

debited to neutralize the effect of interest on NPAs credited to the P&L A/c. The issue was taken up by the department before the Hon'ble Bombay High Court Aurangabad Bench, on similar issues in case of different assessees, but the Hon'ble High Court has not admitted the appeal of the department and hence the matter settled. In view of the above findings of the Hon'ble BombayHigh Court Aurangabad Bench, the interest on NPA/Sticky advances debited under the head overdue interest reserve account need to be allowed.

10.12 In the present case, the appellate bank has credited the gross amount of interest on credit side of the Profit & Loss Account including interest on NPA Loans of Rs.4,25,63,473/- and simultaneously shown on the debit side of the Profit & Loss Account under the head "Overdue Interest Reserve Account", being the amount of interest on NPAs. In other words, instead of neteting of the interest the two amounts have been shown separately one on the credit side and other on the debit side. The net effect of the said presentation is the same. Therefore, the claim of the appellant in respect of amount of Rs.4,25,63,473/- under the head "Overdue Interest Reserve Account" is not a reserve created out of its real income but is a notional income which bank claims of deduction from the recorded Interest Income for an equivalent amount of such 'Notional/Hypothetical Income'. In view of the same, Ground No. 4 is allowed."

Against such a decision, Revenue is in appeal before us.

5. Before us, the ld. DR has defended the decision of the Assessing Officer by placing reliance thereon and reiterating the Grounds of appeal raised. So however, it is quite clear that the reasoning made out by the CIT(A) has not been controverted by the ld. DR on the basis of any credible material which would require any interference in the order of CIT(A).

6. Apart therefrom, the learned representative for the assessee pointed out that the Hon'ble Bombay High Court in the case of *CIT vs M/s. Deogiri Nagari Sahakari Bank Ltd. & Ors., 379 ITR 24 (Bom.),* has considered an identical situation and held that in the case of a co-operative bank, the prudential norms issued by the RBI are applicable and interest on sticky advances identified in terms of such prudential norms is not taxable on mere mercantile basis. The Hon'ble Karnataka High Court in the case of *CIT(A) vs Bijapur District Central, [2018] 93 taxmann.com 211 (Karnataka)* also upheld the proposition that a co-operative bank was not required to pay tax on interest income on NPAs without such interest being actually received or being credited by the assessee in the Profit & Loss Account of the concerned year. In the instant case, assessee credited the relevant interest on NPAs in the Profit & Loss Account and at the same time debited it in the Profit & Loss Account by way of a Provision. The Revenue contends that since a Provision is not an allowable deduction, such amount was liable to be added back. An identical situation has been dealt with by the Pune Bench of the Tribunal in the case of *Solapur District Central Co-op. Bank Ltd. vs ACIT, [2015] 152 ITD 335*. In the said decision, our coordinate Bench noted that what has to prevail is the proposition of law as understood and not merely the presentation in the Annual Financial Statements. It is a trite law that only a part of presentation in the Annual Financial Statements is not conclusive to infer that certain income has accrued *de hors* the entire set of entries made in the financial statements. It is relevant to note that non-taxability of interest income of NPAs is required to be adjudicated having regard to the relevant legal position and not on the basis of mere presentation in the financial statements. In any case, the net effect of the presentation made by the assessee in its financial statements is that the interest income on NPAs is

not being offered to tax without the same being actually received, a proposition which is upheld by the Hon'ble Bombay High Court in the case of *M/s. Deogiri Nagari Sahakari Bank Ltd. (supra)* as well as the Hon'ble Karnataka High Court in the case of *Bijapur District Central (supra).* In fact, the Hon'ble Supreme Court vide its judgment in the case of *CIT vs Jamnagar District Co-operative Bank Ltd., [2018] 94 taxmann.com 300 (SC)* dismissed a SLP arising from the judgment of Hon'ble Gujarat High Court. In the said case, in a similar matter, it was held by the Hon'ble High Court that in case of a co-operative bank, interest on NPAs, which was irrecoverable, was not to be taxed on accrual basis looking to the guidelines of RBI. In our considered opinion, having regard to the aforesaid discussion, we find no error on the part of the CIT(A) in allowing the claim of the assessee and deleting the addition of Rs.4,25,63,473/- made by the Assessing Officer. In the result, appeal of the Revenue is dismissed.

7. Now, we may take-up the appeal of the assessee wherein the only issue is with regard to an addition of Rs.7,37,22,955/- made by the Assessing Officer. The Grounds raised by the assessee in its appeal read as under :-

"1. Deletion of disallowance confirmed by CIT(A) regarding claim of deduction of 'Overdue Interest' which was taxed in earlier year(s) on accrual basis, by way of 'add back' in tax computation by the appellant.

1. The learned AO has erred [and the CIT(A) has erred in confirming] the disallowance of deduction/non taxability, claimed by the appellant for Rs.7,37,22,955 on account of recovery of 'Overdue Interest' of earlier years by

a. Ignoring the Assessment Orders of earlier AYs wherein the said amounts have been offered to tax by disallowing/adding back the debits to the P&L account of the appellant.

b. Ignoring the fact that once the income has been taxed in the earlier years, the same income cannot be taxed again."

8. Factually speaking, the amount in question represented recovery of interest on assets which were classified as NPAs in the earlier period. Before the Assessing Officer, assessee pointed out that such recovery of overdue interest was not taxable in this year since the same has been previously offered to tax in the respective years. The Assessing Officer has noted the submissions of the assessee, as reflected by para 4.1 of his order. However, the Assessing Officer rejected the plea of the assessee and added the same to the returned income. In this context, the learned representative for the assessee referred to the discussion made by the CIT(A) in paras 7.4 and 7.5 of his order and pointed out that the addition has been unfairly sustained inasmuch as such amount of income has already been offered to tax in the earlier years. At the time of hearing, it has been explained that unlike the instant year, in the past years, whenever assessee was crediting the interest on NPAs in the Profit & Loss Account, corresponding debit made in the Profit & Loss Account by way of 'Provision of NPA Interest' was being disallowed while computing the final taxable income. It is only in this year that assessee has staked claim for deduction of such Provision, which is an issue in the cross-appeal of the assessee, that has been dealt with by us in the earlier paras. The learned representative pointed out that in this view of the matter, since the impugned recoveries made on account of interest on NPAs of Rs.7,37,22,955/- represent amounts which have been otherwise offered to tax in the past years, the same cannot be now taxed again. Our attention has been drawn to the relevant details and it has been stated by the learned representative that the assessee would be satisfied if the aforesaid short

plea is verified by the Assessing Officer and thereafter assessee be allowed appropriate relief. In this context, reference has been made to para 7.4 of the order of CIT(A) and pointed out that the observation made therein is indeed contrary to the fact-position, as the details furnished by the assessee support its assertion.

9. On the other hand, the ld. DR appearing for the Revenue has not controverted the factual matrix and did not oppose the plea of the assessee for remanding the matter back to the file of the Assessing Officer for proper verification and allowing of consequential relief, if any.

10. We have carefully considered the rival submissions. A perusal of the assessment order reveals that when assessee was show-caused on this point, it filed written submissions dated 13.01.2014, whose contents have been reproduced by the Assessing Officer in para 4.1 of his order. In these submissions, assessee asserted that the impugned sum was interest recovered on loans and advances which have been classified as NPAs in the earlier financial years. It has also been asserted that in the earlier financial years, the corresponding Provision for overdue interest on such NPA accounts was not considered as tax deductible, meaning thereby that such amounts were offered to tax in those respective assessment years without such amounts having been actually received. The claim of the assessee is that such amounts have been actually recovered in this year and thus cannot be taxed again. Be that as it may, the short plea of the assessee before us is that such assertion of the assessee be verified on the basis of the material on record and thereafter, appropriate relief be allowed. We find the plea of the assessee to be quite germane to decide the controversy, and since it

involves appreciation of factual affairs, we deem it fit and proper to restore the matter back to the file of the Assessing Officer who shall verify the assertions of the assessee and thereafter exclude the impugned sum from the computation of income if he is satisfied that such amount has already been offered to tax in the earlier years on accrual basis. Needless to mention, the Assessing Officer shall allow the assessee a reasonable opportunity of being heard before passing an order afresh on this aspect, as per law. In the result, appeal of the assessee is treated as allowed for statistical purposes.

11. Resultantly, whereas the appeal of the Revenue stands dismissed, that of the assessee is allowed for statistical purposes.

Order pronounced in the open court on 26th September, 2018.

Sd/-	Sd/-
(RAM LAL NEGI)	(G.S. PANNU)
JUDICIAL MEMBER	ACCOUNTANT MEMBER

Mumbai, Date : 26th September, 2018

Copy to :

1) The Appellant
2) The Respondent
3) The CIT(A) concerned
4) The CIT concerned
5) The D.R, "D" Bench, Mumbai
6) Guard file

By Order

Dy./Asstt. Registrar
I.T.A.T, Mumbai