IN THE INCOME TAX APPELLATE TRIBUNAL

"B" BENCH : BANGALORE

BEFORE SHRI ARUN KUMAR GARODIA, ACCOUNTANT MEMBER AND

SHRI LALIET KUMAR, JUDICIAL MEMBER

ITA Nos. 2830 & 2831/Bang/2018
Assessment Years : 2015-16 & 2014-15

The Income-Tax Officer, Ward – 1, Chitradurga.	vs.	M/s. G.M. Souharda Pattina Sahakari Niyamitha, Bheemasamudra Post, Chitradurga. **PAN: AAAJG1543N**
APPELLANT		RESPONDENT

Appellant by	:	Shri R.N. Siddappaji, Addl. CIT (DR)
Respondent by	:	Shri S. Ramasubramanian, CA
Date of hearing	:	12.03.2019
Date of Pronouncement	:	22.03.2019

O R D E R

Per Shri A.K. Garodia, Accountant Member

Both these appeals are filed by the revenue and the same are directed against two separate orders of ld. CIT(A), Davangere both dated 30.07.2018 for Assessment Years 2014-15 and 2015-16. Both these appeals were heard together and are being disposed of by way of this common order for the sake of convenience.

2. The grounds raised by the revenue for Assessment Year 2014-15 in ITA No. 2831/Bang/2018 are as under.

> "*1. The order of the Commissioner of Income Tax(Appeals), Davangere, is opposed to the law and not on the facts and circumstances of the case.*
>
> *2. The CIT (Appeal) has not considered the fact that in order to be eligible for deduction U/s 57, it is necessary to establish that the expenditure was incurred wholly and exclusively for the purpose of earning the corresponding income.*
>
> *3. The CIT (Appeal) has erred in not considering the fact that direct nexus between the expenditure allowed and income earned is not established.*
>
> *4. For these and other grounds that may be urged upon, the order of the CIT(A) may be reversed and that assessment order be restored.*

5. The appellant craves leave to add, alter, amend or delete any other grounds on or before hearing of the appeal."

3. Similarly the grounds raised by the revenue for Assessment Year 2015-16 in ITA No. 2830/Bang/2018 are as under.

"*1. The order of the Commissioner of Income Tax(Appeals), Davangere, is opposed to the law and not on the facts and circumstances of the case.*

2. The CIT (Appeal) has not considered the fact that in order to be eligible for deduction U/s 57, it is necessary to establish that the expenditure was incurred wholly and exclusively for the purpose of earning the corresponding income.

3. The CIT (Appeal) has erred in not considering the fact that direct nexus between the expenditure allowed and income earned is not established. •

4. For these and other grounds that may be urged upon, the order of the CIT(A) may be reversed and that assessment order be restored.

5. The appellant craves leave to add, alter, amend or delete any other grounds on or before hearing of the appeal."

4. It was submitted by ld. DR of the revenue that as per Para 3 of the assessment order for Assessment Year 2014-15, it is noted by AO that assessee is in receipt of interest income of Rs. 71,96,872/- from the investments made with various banks and the AO brought this amount to tax by holding that this interest income is not allowable u/s. 80P(2)(d) of IT Act. He further pointed out that against this assessment order, the assessee preferred an appeal before CIT(A) and as per the first order of CIT(A) passed by him on 28.09.2017, it was held by CIT(A) that this income is liable for assessment as income under the head "Other Sources" u/s. 56 and is to be calculated as per the provisions of the Act. He also pointed out that this was the direction given by CIT(A) to AO that he should compute interest income earned on deposits from co-operative banks as well as scheduled banks after allowing deduction u/s. 57 of IT Act. Thereafter he drawn our attention to the order giving effect to the CIT(A) order passed by AO on 29.11.2017. He pointed out that in this appeal effective order, the

AO has held that 2% on total administrative expenditure incurred is allowed as expenditure incurred for earning brought to tax as income from other sources and in this manner, he allowed deduction of Rs. 7,20,366/-. Regarding interest expenditure incurred by the assessee of Rs. 2,84,94,075/-, it was held by the AO that the assessee society has not incurred cost of funds to earn this interest income of Rs. 71,96,872/-. He further submitted that against this order of the AO giving effect to the order of CIT(A), the assessee preferred an appeal before CIT(A) and as per the impugned order of CIT(A) dated 30.07.2018, it was held by CIT(A) that the entire addition made by the AO is deleted. He submitted that for deleting the entire addition made by the AO, ld. CIT(A) has considered the working given by the assessee before him in respect of apportionment of interest expenditure and administrative expenses. His first objection was this that there was violation of Income Tax Rules, 1962 because CIT(A) has not obtained remand report from AO regarding this fresh evidence filed. His second objection was this that when the entire expenditure and administrative expenses are debited to P&L account, no expenses is left to be allowed separately against interest income brought to tax by the AO under the head “Income from Other Sources”. In reply, the ld. AR of assessee supported the order of CIT(A). He submitted that the balance sheet of the assessee for Assessment Year 2014-15 is available on page no. 5 of the paper book and as per the same, it can be seen that in the liability side, there is deposits and other accounts of Rs. 38,14,40,168/- and on the asset side of balance sheet is Money at call & short notice of Rs. 12,60,10,000/- and Loans and Advances of Rs. 2,520 Lakhs. He pointed out that on page no. 4 of the paper book is profit and loss account and as per the same, there is debit of Rs. 2,84,94,075.79. He submitted that this expenditure is incurred on deposit of Rs. 38,14,40,168.11 and this deposit amount is used for both purposes i.e. for making deposit in bank as well as giving loans to members. He submitted that if the interest income from banks is taxed under the head Income from other sources then, interest expenditure has to be apportioned between both interest incomes i.e. interest on loans of Rs. 305.34 Lakhs received from members and interest

on FD with banks of Rs. 71,96,872/-. Both sides agreed that the facts in Assessment Year 2015-16 are identical to facts for Assessment Year 2014-15 and hence, the decision of Assessment Year 2014-15 can be followed in Assessment Year 2015-16 also.

5. We have considered the rival submissions. We find that as per the P&L account for Assessment Year 2014-15 available on page no. 4 of the paper book, the total income is of Rs. 73,22,944.07/- and as per the computation of income available on page no. 3 of the paper book, after making some additions and deductions, gross total income was worked out at Rs. 73,68,938/- and deduction was claimed by the assessee u/s. 80P of the same amount and in this manner, the net income has been computed at Nil. As per the assessment order, the AO has made addition of Rs. 71,96,872/- in respect of interest income from banks by holding that this interest income is not allowable for deduction u/s. 80P(2)(d) of IT Act. There is one more addition made by the AO, but the same is not in dispute before us. In our considered opinion, for the purpose of allowing deduction u/s. 80P, only net income has to be considered and not gross income and therefore, if there is any disallowance in respect of any income then if there is any disallowance which is considered by the AO as not allowable for deduction u/s. 80P(2)(d) then the net amount of such income should be considered for making disallowance and not the gross amount of such income. In the present case, this is seen that the assessee is having mixed funds in the form of share capital, reserves and deposits from members and this mixed fund was utilized for making investment with banks and giving loan to members. If the AO is able to establish direct nexus between deposit with banks and assessee's own interest free funds, then there may be a case for adjusting entire interest expenditure against the interest income earned by the assessee on loans to members and as a consequence, no deduction will be allowable in such situation on account of interest expenditure against interest income from banks. Similarly, if the assessee can establish direct nexus between interest bearing borrowed funds and investment with bank, then entire amount of interest expenditure has to be allowed as deduction

from interest income from banks to the extent the assessee is able to establish the nexus. In the present case, neither the AO nor the assessee has established any direct nexus. In such a situation, in our considered opinion, this should be held that proportionate interest expenditure should be considered as allowable u/s. 57(iii) of IT Act. This view of us is in line with Rule 8D inserted for the purpose of making disallowance u/s. 14A of IT Act. In this view of the matter, we find no infirmity in the order of CIT(A) as per which he has directed to delete the entire disallowance made by the AO because he has noted that as per the proportionate working for administrative expenses, cost of funds of is Rs. 97,98,828/- . This amount of cost of funds has been worked out on this basis that total interest paid of Rs. 2,84,94,076/- is in respect of total sources of funds of Rs. 40,69,06,727/- it includes capital of Rs. 71,98,199/-, reserves of Rs. 1,82,68,360/- and borrowings of Rs. 38,14,40,168/- as per the working of CIT(A) on page no. 11 of its order. The sum worked out is at 7% of such total sources of funds. This was one of the submission of ld. DR of revenue that in the working of rate of interest attributable to sources of funds, amount of capital and reserves should not be included because admittedly no interest is payable on capital. This logic appears to be reasonable and correct but it is not going to help the revenue because in that case, the rate of interest of Rs. 2,84,94,076/- attributable to only borrowings of Rs. 38,14,40,168/- will work out to 7.47% in place of 7% noted by the CIT(A). The proportionate cost of funds for arriving interest income from banks in respect of year ended as on 31.03.2014 will work out to an amount in excess of the amount worked out by applying the rate of 7%. This is bound to be more than the entire such interest income from banks of Rs. 74,38,988/-. Hence we find no infirmity in the order of CIT(A) on this issue.

6. Regarding this argument of ld. DR of revenue that there is violation of Rule 46A of IT Rules, 1962. We would like to observe that there is no such ground raised by revenue in its appeal in both years and moreover, it is noted by CIT(A) in last Para on page no. 10 of his order that during the course of appellate proceedings, details of expenditure incurred by the

appellant was obtained which is reproduced below for the sake of ready reference. In our considered opinion, as per this observation of ld. CIT(A), it comes out that such details were obtained by CIT (A) from the assessee, This is covered u/s. 250 (4) of IT Act and Rule 46A is not applicable in that situation because 46A is applicable in situation where the assessee wants to file or produce certain additional evidence before CIT(A). In the present case, in view of this observation of CIT (A) that these details are obtained by him from the assessee, it cannot be said that the assessee produced these details before CIT (A). In our considered opinion, these details were called for by the CIT (A) from the assessee as per its observation on page no. 10 of the order and hence, in our considered opinion, Rule 46A is not applicable in the facts of present case.

7. In the result, both the appeals filed by the revenue are dismissed.

Order pronounced in the open court on the date mentioned on the caption page.

Sd/-	Sd/-
(LALIET KUMAR)	(ARUN KUMAR GARODIA)
Judicial Member	Accountant Member

Bangalore,
Dated, the 22nd March, 2019.
/MS/

Copy to:

1. Appellant	4. CIT(A)
2. Respondent	5. DR, ITAT, Bangalore
3. CIT	6. Guard file

By order

Assistant Registrar,
Income Tax Appellate Tribunal,
Bangalore.