IN THE INCOME TAX APPELLATE TRIBUNAL
"C" BENCH : BANGALORE

BEFORE SHRI N.V. VASUDEVAN, VICE PRESIDENT
AND SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER

| ITA No.2054/Bang/2017 |
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| Assessment year : 2014-15 |

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| The Assistant Commissioner of Income Tax,<br>Circle 2(1),<br>Hubli. | Vs. | M/s. Karnataka Vikas Grameen Bank.,<br>Head Office, Belgaum Road,<br>Dharwad.<br>**PAN: AAAAK 6324Q** |
| APPELLANT | | RESPONDENT |

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| Appellant by | : | Shri Pradeep Kumar, CIT(DR)(ITAT), Bengaluru. |
| Respondent by | : | Shri S.V. Ravishankar, Advocate |

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| Date of hearing | : | 08.09.2020 |
| Date of Pronouncement | : | 10.09.2020 |

**O R D E R**

*Per N.V. Vasudevan, Vice President*

This is an appeal by the Revenue against the order dated 3.7.2017 of Commissioner of Income-tax (Appeals), Hubli relating to the assessment year 2014-15.

2. Ground No.i raised by the Revenue by the revenue reads as follows:-

> i. On facts & circumstances of the case and in law, the learned CIT(A), Hubballi, erred in considering the assessee's claim for deduction u/s.36(1)(viia) of Rs.381,26,66,985/- as the assessee had not made any provision for bad and doubtful debts during the previous year as per the provisions contained in section 36(2)(v)

and clarification in Explanation 2 to section 36(1)(vii) by the Finance Act, 2013, w.e.f 1.4.2013.

3. The Assessee is a rural regional bank engaged in the business of banking. In the course of assessment proceedings u/s 143(3) of the Income-tax Act, 1961 (Act) for AY 2014-15, the AO noticed that the assessee had claimed deduction on account of provision for bad and doubtful debts for a sum of Rs.3,81,26,66,985/- u/s.36(1)(viia) of the Income Tax Act, 1961 (Act). The provisions of Section 36(1)(viia)(a) of the Act lays down as follows:-

> "viia) in respect of any provision for bad and doubtful debts made by –
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> (a) a scheduled bank not being a bank incorporated by or under the laws of a country outside India] or a co-operative bank other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank, an amount not exceeding seven and one-half per cent of the total income (computed before making any deduction under this clause and Chapter VI-A) and an amount not exceeding ten per cent of the aggregate average advances made by the rural branches of such bank computed in the prescribed manner;
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> Provided that a scheduled bank or a non-scheduled bank referred to in this sub-clause shall, at its option, be allowed in any of the relevant assessment years, deduction in respect of any provision made by it for any assets classified by the Reserve Bank of India as doubtful assets or loss assets in accordance with the guidelines issued by it in this behalf, for an amount not exceeding five per cent of the amount of such assets shown in the books of account of the bank on the last day of the previous year."

4. There are two deductions allowed under the aforesaid provisions viz., (i) 7.5% of the total income (computed before making any deduction under clause (viia) of Sec.36(1) of the Act towards provisions for bad and doubtful debts; (ii) 10% of the Aggregate average advances made by rural

branches of the bank computed in the manner prescribed. The Assessee claimed a sum of Rs.13,34,67,416 towards provision for bad and doubtful debts @7.5% of the total income and a sum of Rs.367,91,99,569/- towards provision for bad and doubtful debts in respect of aggregate average advances made by the Assessee's rural branches, in all an aggregate sum of Rs.381,26,66,985/-. U/S.36(2)(v) of the Act the condition for claiming deduction u/s.36(1)(viia) of the Act is that the sum claimed as deduction should be debited to the provision for bad and doubtful debts account. There is no discussion in the order of assessment as to whether the sum claimed as deduction u/s.36(1)(viia) of the Act had been debited to the provision for bad and doubtful debts account. The question that the AO ought to have analysed is as to whether the assessee can claim deduction u/s.36(1)(viia) of the Act without debiting the same to the provision for bad and doubtful debts account.

5. The AO however proceeded to discuss the provisions of Sec.36(1)(vii) and 36(2)(v) of the Act, the decision of the Hon'ble Supreme Court in the case of *Catholic Syrian Bank Ltd. Vs. CIT 343 ITR 270(SC)* and the amendment to the provisions of Sec.36(1)(vii) Explanation-1 w.e.f 1.4.2014 by the Finance Act, 2013 and finally concluded in paragraph-4.6 of his order as follows:

> "4.6 Hence it is concluded that, the assessee is therefore not eligible for any deduction u/s.36(1)(viia), as it has not made a provision for bad and doubtful debts during the year, as required in Sec.36(2)(v). Hence the total deduction claimed u/s.36(1)(viia) of Rs.381,26,66,985/- is disallowed and added back to the income returned by the Assessee."

6. By implication, therefore the sum claimed as deduction has not been debited to the Provision for Bad and Doubt Debts Account. Even before CIT(A), the Assessee did not put forth a plea that such a debit to Provision

for Bad and Doubtful debts Account was made by the Assessee. The CIT(A) deleted the addition made by the AO by following the order of the predecessor CIT(A) in AY 2013-14.

7. At the time of hearing it was agreed by the parties that the order of CIT(A) for AY 2013-14 on which the CIT(A) placed reliance was subject matter of appeal by the Revenue before the Tribunal, Bangalore Bench in ITA No.1392/Bang/2016 and the Tribunal by its order dated 23.1.2020 allowed the ground of appeal of the Revenue holding as follows:-

> "7. Aggrieved by the order of the CIT(A), the revenue has raised ground Nos.1 & 2 before the Tribunal. At the time of hearing it was agreed by the parties that similar issue had come up for consideration before the ITAT in Assessee's own case for AY 2009-10 & 2010-11 in ITA No.673 & 674/Bang/2014 order dated 25.4.2018 and this Tribunal reversed the order of the CIT(A) and held that the deduction u/s.36(1)(viia) of the Act cannot be allowed unless the provision is created by debited to provision for bad and doubtful debts account. The following were the relevant observations of the Tribunal:-
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> > "7. We have heard the rival submissions. The learned DR submitted that as laid down by the Hon'ble Punjab and Haryana High Court in the case of State Bank of Patiala Vs. CIT 272 ITR 53 (P & H), claim for deduction u/s.36(1)(viia) of the Act cannot be greater than the amount debited to the profit and loss account as provision. Our attention was drawn to a decision of the ITAT Bangalore in the case of Syndicate Bank Vs. DCIT (2014) 150 ITD 0103 (Bangalore), wherein the Hon'ble ITAT Bangalore Bench preferred to follow the view taken by the Hon'ble Punjab & Haryana High Court in the case of State Bank of Patiala (supra) rather than the decision of the Syndicate Bank (supra) of the Bangalore Bench relied upon by the learned CIT(A) in giving relief to the Assessee on this issue. The ld. counsel for the assesses submitted that the decision of the Bangalore Bench of ITAT in the case of Syndicate Bank (Supra) should be followed by the Tribunal in preference to the decision of the Hon'ble Punjab and Haryana High Court in the case of State Bank

of Patiala (supra)and in this regard submitted that the decision of co-ordinate Bench of the Tribunal should be followed in preference to the decision of non jurisdictional High Court decision. In this regard, the ld counsel for the assessee placed reliance on the decision of the Hon'ble Karnataka High Court in the case of Patil Vijayakumar & Others Vs. Union of India 151 ITR 48 (Kar).

8. We have considered the rival submission. The provisions of Section 36(1)(viia)(a) of the Act lays down as follows:

"viia) in respect of any provision for bad and doubtful debts made by

(a) a scheduled bank not being a bank incorporated by or under the laws of a country outside India] or a co-operative bank other than a primary agricultural credit society or a primary co- operative agricultural and rural development bank, an amount not exceeding seven and one-half per cent of the total income (computed before making any deduction under this clause and Chapter VI-A) and an amount not exceeding ten per cent of the aggregate average advances made by the rural branches of such bank computed in the prescribed manner;

Provided that a scheduled bank or a non-scheduled bank referred to in this sub-clause shall, at its option, be allowed in any of the relevant assessment years, deduction in respect of any provision made by it for any assets classified by the Reserve Bank of India as doubtful assets or loss assets in accordance with the guidelines issued by it in this behalf, for an amount not exceeding five per cent of the amount of such assets shown in the books of account of the bank on the last day of the previous year."

9. In the case of *Syndicate Bank (supra) 78 ITD 103 (Bang.)*, the Bangalore Bench of ITAT took the view that irrespective of the debit to the profit and loss account on account of provision for bad and doubtful debts (PBDD), an Assessee is entitled to 10 percent of the AARA as deduction u/s.36(1)(viia) of the Act. The relevant observations of the Tribunal in the aforesaid decision was as follows:

> "20. The learned CIT has also acted under the misconception that deduction under cl. (viia) is related to the actual amount of provision made by the assessee for bad and doubtful debts. The true meaning of the clause, as indicated earlier, is that once a provision for bad and doubtful debts is made by a scheduled bank having rural branches, the assessee is entitled to a deduction which is quantified not with respect to the amount provided for in the accounts, but with respect to a certain percentage of the total income and also a certain percentage of the aggregate average advances made by the rural branches of the bank. In other words, this is a specific deduction given by the statute irrespective of the quantum provided by the assessee in its accounts towards provision for bad and doubtful debts."

10. However the Bangalore Bench of ITAT in the case of Syndicate Bank (supra) 150 ITD 103 (Bang.) noticed that the ITAT Bangalore Bench in the case of *Canara Bank* in ITA No.58/Bang/2004 dated 9.6.2006 considered in the case of Canara Bank in ITA No.58/Bang/2004 dated 9.6.2006 considered the decision of the ITAT in the case of *Syndicate Bank* 78 ITD 103(Bang) and the decision of the Hon'ble Punjab and Haryana High Court in the case of *State Bank of Patiala* (supra) and held that the decision rendered by the Hon'ble High Court has to be followed. The above decision though of a non jurisdiction High Court was followed as the said decision of the Hon'ble High Court was rendered after the decision in the case of *Syndicate Bank 78 ITD 103 (Bang.)*. The Tribunal held that Judicial discipline demands that the Tribunal should follow the later decision which has considered both the decisions on the issue. The Tribunal following the said decision held deduction on account of Provision for Bad and Doubtful Debts u/s.36(1)(viia) of the Act has to be allowed only to the extent such provision is actually debited in the Profit & Loss Account by the Assessee for the relevant previous year. We therefore respectfully following the decision of the Tribunal in the case of Canara Bank (supra), allow Gr.No.2 to 4 raised by the Revenue and hold that the disallowance made by the AO

> was proper and the Assessee is entitled to deduction only to the extent PBDD is debited to the P & L A/c. Thus Gr.No.2 to 4 3 raised by the revenue are allowed."

> 8. Respectfully following the decision of the Tribunal in Assessee's own case we hold that the AO was justified in disallowing the claim for deduction on account of provisions for bad and doubtful debts u/s.36(1)(viia) of the Act as admittedly the Assessee did not debit its profit and loss account any sum towards provision for bad and doubtful debts. We therefore restore the order of the AO and allow Gr.No.1 & 2 raised by the revenue."

8. In view of the aforesaid decision of the Tribunal, we hold that the AO was justified in disallowing the claim for deduction on account of provisions for bad and doubtful debts u/s.36(1)(viia) of the Act as admittedly the Assessee did not debit its profit and loss account any sum towards provision for bad and doubtful debts. We therefore restore the order of the AO and allow Gr.No.1 raised by the revenue.

9. As far as Grd.No.ii raised by the revenue is concerned, the same reads as follows:-

> "On the facts and in the circumstances of the case, the ld. CIT(Appeals), Hubballi, erred in deleting the addition made on account of 'Disallowance of excess deduction claimed u/s. 36(1)(viii)' of Rs.6,97,63,000/-, as the AO has calculated the eligible advances as per Annual Report. The AO has adopted the figure of profit after tax and reduced Other Incomes while computing the deductions. As such, the addition made by the AO of Rs.6,97,63,000/- on account of excess claim of deduction u/s. 36(1)(viii) of the I.T. Act, may be restored."

10. The issue in Grd.No.ii is with regard to the quantum of deduction to be allowed u/s.36(1)(viii) of the Act. The relevant provisions of Sec.36(1)(viii) reads as follows:-

"(viii) in respect of any special reserve created and maintained by a specified entity, **an amount not exceeding twenty per cent of the profits derived from eligible business computed under the head "Profits and gains of business or profession"** (before making any deduction under this clause) carried to such reserve account:

**Provided** that where the aggregate of the amounts carried to such reserve account from time to time exceeds twice the amount of the paid up share capital and of the general reserves of the specified entity, no allowance under this clause shall be made in respect of such excess.

Explanation.—In this clause,—

(*a*) "specified entity" means,—

(*i*) a financial corporation specified in section 4A of the Companies Act, 1956 (1 of 1956)[71];

(*ii*) a financial corporation which is a public sector company;

(*iii*) a banking company;

(*iv*) a co-operative bank other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank;

(*v*) a housing finance company; and

(*vi*) any other financial corporation including a public company;

(*b*) "eligible business" means,—

[72][(i) in respect of the specified entity referred to in sub-clause (i) or sub-clause (ii) or sub-clause (iii) or sub-clause (iv) of clause (a), the business of providing long-term finance for—

(*A*) industrial or agricultural development;

(*B*) development of infrastructure facility in India; or

(*C*) development of housing in India;]

(*ii*) in respect of the specified entity referred to in sub-clause (v) of clause (a), the business of providing long-term finance for the construction or purchase of houses in India for residential purposes; and

(*iii*) in respect of the specified entity referred to in sub-clause (vi) of clause (a), the business of providing long-term finance for development of infrastructure facility in India;

(*c*) "banking company" means a company to which the Banking Regulation Act, 1949 (10 of 1949) applies and includes any bank or banking institution referred to in section 51 of that Act;

(*d*) "co-operative bank", "primary agricultural credit society" and "primary co-operative agricultural and rural development bank" shall have the meanings respectively assigned to them in the Explanation to sub-section (4) of section 80P;

(*e*) "housing finance company" means a public company formed or registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes;

(*f*) [73]"public company" shall have the meaning assigned to it in section 3 of the Companies Act, 1956 (1 of 1956);

(*g*) "infrastructure facility" means—

(*i*) an infrastructure facility as defined in the Explanation to clause (i) of sub-section (4) of section 80-IA, or any other public facility of a similar nature as may be notified[74] by the Board in this behalf in the Official Gazette and which fulfils the conditions as may be prescribed[75];

(*ii*) an undertaking referred to in clause (ii) or clause (iii) or clause (iv) or clause (vi) of sub-section (4) of section 80-IA; and

(*iii*) an undertaking referred to in sub-section (10) of section 80-IB;

(*h*) "long-term finance" [75a] means any loan or advance where the terms under which moneys are loaned or advanced provide for repayment along with interest thereof during a period of not less than five years;

11. There is no dispute that the Assessee was an eligible entity and that to the extent of 20% of the profits derived from the eligible business, the Assessee was entitled to claim deduction u/s.36(1)(viii) of the Act. The dispute is with regard to manner of computation of eligible deduction u/s.36(1)(viii) of the Act. The computation done by the Assessee and that done by the AO was as follows:-

"The appellant has computed the deduction as under:

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| Total income as per return of income before deduction u/s 36(i)(viia) | Rs.177.96 crores |
| Add: Deduction created and claimed and Eligible under u/s 36(i)(viii) | Rs. 11.52 crores |
| Total income from business eligible for deduction | Rs.**184.48 crores** |
| Total advance as on 31.03.2014 (before provision for NPA) | Rs.6481.52 crores |

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|---|---|
| Eligible advances as on 31.03.2014 as per list enclosed | Rs. 2123.29 crores |
| % of eligible advance to total advance | 32.76% |
| Total income as worked out above (20.00% of Rs. 189.48 crores) | Rs. 37.90 crores |
| Profit from eligible business, at 32.76% of above | Rs.12.41 crores |
| Reserve created and deduction claimed | Rs.11.52 crores |

12. But the learned assessing officer worked out the deduction u/s 36(i)(viii) of the Act in the following manner and allowed the claim of the appellant to extent of Rs. 4,54,37,000 :-

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| Total Advances made | | Rs. 6481,52,00,000/- |
| Eligible Advance | | Rs. 2123,29,00,000/- |
| % of Eligible advances over Total Advances | | 32.76% |
| Income considered for deduction u/s 36(1)(viii) | | |
| Gross Income | | Rs. 1033,03,34,000/- |
| Less Other income | | Rs. 70,67,86,000/- |
| Total income | | Rs. 962,35,48,000/- |
| Less expenses | | Rs. 893,00,59,000/- |
| Net Profit | | Rs. 69,34,89,000/- |
| 32.76% of Net Profit | | Rs. 22,71,86,000/- |
| 20% of Rs. 22,71,86,000/- | | Rs. 4,54,37,000/- |

13. It was the plea of the Assessee before CIT(A) that the AO has erred in restricting the deduction under section 36(i)(viii) of the Act to Rs. 4,54,37,000.00 against deduction of Rs. 11,52,00,000.00 claimed by the appellant. The AO disallowed the claim of the assessee to the extent of Rs. 6,97,63,000.00 by working out the deduction by him as per his own method which is not as per provisions of Income Tax Act, 1961 and as per method of calculation of deduction u/s 36(i)(viii) of Act worked out by the Hon'ble Karnataka High Court in the case of *Karnataka State Financial Corporation Vs. CIT (1988) 174 ITR 206*).

14. The CIT(A) allowed the claim of the Assessee observing as follows:-

> "20. Ground of appeal No.5 Disallowance u/s. 36(1)(viii) Rs.6,97,63,000/-:
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> The AO in the assessment order has worked out the deduction to be allowed u/s. 36(I)(viii) of the Act. As against the claim made of Rs.11,52,00,000/- the AO has allowed Rs.45,43,7000/- u/s. 36(1)(viii) thereby disallowing the claim to the extent of Rs.6,97,63,000/- as excess. In the order, he has given the working but has not given any reasons as to why he is not considering the assessee's calculation of deduction u/s. 36(1)(viii). The AO has agreed with assessee's calculation of total advances made of Rs.64,81,52,00,000r- and eligible advance of Rs.21,23,29,00,00/- and percentage of eligible advances at 32.75%. but while arriving at the total income he has taken the figure at Rs.962,35,48,000/- and deducted expenses of Rs.89,30,00,59,000/- and net profit at Rs.69,34,89,000/- whereas the assessee arrived at the total income at Rs.37.90 cr and profit from eligible business at 32.76% i.e. Rs.12.41 cr and deduction claimed u/s. 26(I)(viii) at Rs.11.52 cr against Rs.4,54,37,000/- arrived at by the AO.
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> 21. The AO should have elaborated and given his conclusive findings as to how he has arrived at the deduction to be allowed u/s. 36(I)(viii) at Rs.4,54,37,000/- as against Rs.11,52,00,000/-.

> 22. The assessee, in the argument, states that, the method of calculation of deduction u/s.36(1)(viii) by the AO is neither as per section 36(1)(viii) nor as per the decision of Hon'ble High Court of Karnataka i.e. the jurisdictional High Court in the case of Karnataka State Finance Corporation Vs. CIT (1988) 174 ITR 206. The Karnataka High Court in this case has given the definition of total income based on section 2(45) of the Act. Total income as per section 2(45) means the total amount of income referred to in section 5 computed in the manner laid down in this Act. The only exception which has to be made u/s. 36(1)(viii) is that, the total income for the purpose of this section must be the one "computed before making any deduction under chapter-VIA. The assessee has calculated the deduction u/s. 36(1)(viii) based on the above decision which has been worked out by the AO in the case of Karnataka High Court.
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> 23. In the very same case i.e. the assessee, my predecessor the CIT (Appeals), Hubli for the AY 2008-09 has accepted the working made by the assessee about the deduction u/s. 36(1)(viii) to be made.
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> 24. Since the AO for the present AY has not given his reasons as to why he is not agreeing with the assessee's calculation of deduction to be given u/s. 36(1)(viii) , and the assessee has given its working based on the decision of the jurisdictional High Court and also other decisions, and my predecessor CIT(A) Hubli has accepted the said calculation for the assessment year 2008-09 in the very same case, it is held that, the assessee's working of deduction u/s. 36(1)(viii) of Rs.11.52cr is found to be in order and not Rs.4,54,37,000/-. In the result the disallowance made of Rs.6,97,63,000/- is hereby deleted."

15. Aggrieved by the order of the CIT(A), the Revenue has raised Grd.No.ii before the Tribunal. We have heard the rival submissions. A perusal of the CIT(A) order shows that the relief allowed by the CIT(A) to the assessee is based on the decision of the Karnataka High Court in the case of *Karnataka State Finance Corporation (supra)*. The CIT(A) has not given a factual finding as to how the deduction claimed by the Assessee is in accordance with the statutory provisions. We are of the view that since

no finding has been given by the CIT(A) as to the basis on which the relief was given by the CIT(A), we deem it fit and proper to set aside the order of the CIT(A) and remand to the AO for fresh consideration the question of proper deduction to be allowed u/s 36(1)((viii) of the Act. The AO will consider the contentions put forth by the assessee and decide the issue afresh affording opportunity being heard to the assessee.

16. In the result, appeal by the revenue is allowed for statistical purposes.

Pronounced in the open court on this 10th day of September, 2020.

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| Sd/- | Sd/- |
| ( CHANDRA POOJARI )<br>ACCOUNTANT MEMBER | ( N V VASUDEVAN )<br>VICE PRESIDENT |

Bangalore,
Dated, the 10th September, 2020.

*/Desai S Murthy /*

Copy to:

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

By order

Assistant Registrar
ITAT, Bangalore.