

**IN THE INCOME TAX APPELLATE TRIBUNAL
“SMC’ BENCH: BANGALORE**

BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER

ITA No.588/Bang/2022
Assessment Year: 2017-18

Kanak Pattin Sahakari Sangha Niyamit, Bilagi, Dist. Bagalkot Behind Bus Stand, Bilagi Karnataka 587 116 PAN NO : AABAK9999E	Vs.	ITO Ward(1) Bagalkot
APPELLANT		RESPONDENT

Appellant by	:	Shri V. Sridhar, A.R.
Respondent by	:	Shri Ganesh R. Gale, Standing Counsel for Department

Date of Hearing	:	28.12.2022
Date of Pronouncement	:	28.12.2022

O R D E R

PER CHANDRA POOJARI, ACCOUNTANT MEMBER:

This appeal by the assessee is directed against the order of CIT(A), NFAC, Delhi dated 30.05.2022 for the AY 2017-18. The grounds of appeal raised by the assessee are reproduced as under:

1. The Ld. Commissioner of Income Tax (Appeals) erred in law as well as on facts in rejecting the genuine claim of the appellant in respect of deduction u/s 80P(2)(a)(i) to the extent of Rs.31,36,705.00 as claimed by the appellant. The appellant prays for grant of the deduction as claimed.

2. The Ld. Commissioner of Income Tax (Appeals) erred in law as well as on facts in applying the Judgment of Hon. Supreme Court of India in the

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case of Citizen Co —Operative Society, Hyderabad. As the facts of Citizen society & the assessee society is totally different.

3. Each of the above grounds is without prejudice to one another and the appellants crave leave to add, delete, amend or otherwise modify or withdraw one or more of the above grounds either before or at the time of hearing of this appeal.

2. Facts of the case are that the assessee is a co-operative society and assessed to tax under Income Tax Officer W-1, Bagalkot. The assessee is registered under Karnataka Co-operative Societies Act, 1959. The assessee society engaged in the business of accepting the deposits from members and providing credit facilities to its members. The income of assessee co-op. society is eligible for deduction under the specific provisions of Section 80P(2)(a)(i) of the Income-tax Act, 1961 [the Act' for short]. However, the learned Assessing officer has for the reasons stated in his order denied this specific deduction. The Assessee has submitted that the decision of Hon. Supreme Court of India in the case of Citizen Co-operative society, Hyderabad is not applicable since the facts of this case and assessee society's case is totally different. The ld AR also submitted in his written submissions that the Banking Regulation Act does not apply to it, that there is no control or supervision by the RBI & Negotiable Instruments Act do not apply to it and that the co-op. Society cannot designate itself as bank and it can only deal with its members of society only. The learned A.O. has rejected all the submissions made by the assessee to defend the claim of this specific deduction. He has further gone on to treat the assessee co-op society is carrying on banking business, which is contrary to facts & law. Having come to the wrong conclusion the assessee society does a banking business, the learned A.O has wrongly taxed the

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income denying the specific deduction U/S 80P(2)(a)(i) of the Income Tax Act, 1961. Aggrieved by the aforesaid order of the A.O., the assessee went in appeal before the Id. CIT(A). The Id. CIT(A), NFAC, Delhi confirmed the order of the AO by observing as under:

6.3 *I have perused the assessment order, submission of the appellant and the judgement of Hon'ble Supreme Court in the case of Citizen Co-op Credit Society Ltd v. ACIT C-9(1), Hyderabad in Civil appeal No.10245 of 2017 (Arising out of SLP (C) No.20044 of 2015) dated 8.08.2017,*

6.4. *Hon'ble Supreme Court in the case of Citizen Co-op Credit Society Ltd v. ACIT C-9(1)(supra) has held as under:*

"25) So far so good. However, it is significant to point out that the main reason for disentitling the appellant from getting the deduction provided under Section 80P of the Act is not sub-section (4) thereof. What has been noticed by the Assessing Officer. after discussing in detail the activities of the appellant, is that the activities of the appellant are in violations of the provisions of the MACSA under which it is formed. It is pointed out by the Assessing Officer that the assessee is catering to two distinct categories of people. The first category is that of resident members or ordinary members. There may not be any difficulty as far as this category is concerned. However, the assessee had carved out another category of 'nominal members'. These are those members who are making deposits with the assessee for the purpose of obtaining loans, etc. and, in fact, they are not members in real sense. Most of the business of the appellant was with this second category of persons who have been giving deposits which are kept in Fixed Deposits with a motive to earn maximum returns. A portion of these deposits is utilised to advance gold loans, etc. to the members of the first category. It is found, as a matter of fact, that the depositors and borrowers are quite distinct. In reality, such activity of the appellant is that of finance business and cannot be termed as cooperative society. It is also found that the appellant is engaged in the activity of granting loans to general public as well. All this is done without any approval from the Registrar of the Societies. With indulgence in such kind of activity by the appellant, it is remarked by the Assessing Officer that the activity of the appellant is in violation of the Co-operative Societies Act. Moreover, it is a co-operative credit society which is not entitled to deduction under Section 80P(2)(a)(i) of the Act,

26) It is in this background, a specific finding is also rendered that the principle of mutuality is missing in the instant case. Though there is a detailed discussion in this behalf in the order of the Assessing Officer,

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our purpose would be served by taking note of the following portion of the discussion:

'As various courts have observed that the following three conditions must exist before an activity could be brought under the concept of mutuality: that no person can earn from him;

that there a profit motivation:

and that there is no sharing of profit.

It is noticed that the fund invested with bank which are not member of association welfare fund, and the interest has been earned on such investment for example, ING Mutual Fund [as said by the MD vide his statement dated 20.12.2010]. [Though the bank formed the third party vis-a-vis the assessee entitled between contributor and recipient is lost in such case. The other ingredients of mutuality are also found to be missing as discussed in further paragraphs].

In the present case both the parties to the transaction are the contributors towards surplus, however. there are no participators in the surpluses. There is no common consent of whatsoever for participators as their identity is not established. Hence, the' assessee fails to satisfy the test of mutuality at the time of making the payments the number in referred as members may not be the member of the society as such the AOP body by the society is not covered by concept of mutuality at all."

27) These are the findings of fact which have remained unshaken till the stage of the High Court. Once we keep the aforesaid aspects in mind, the conclusion is obvious, namely, the appellant cannot be treated as a co-operative society meant only for its members and providing credit facilities to its members. We are afraid such a society cannot claim the benefit of Section SOP of the Act."

6.5 *In the present case, the AO has discussed the issue in detail at Para 5-7 (Page 2-3) of the order observing that the appellant is dealing with non members termed as 'nominal and associate members' and claimed to have admitted the same as per the provisions of the Karnataka Co-op Societies Act, 1959.*

6.6 *Analysing the details in regard to 'Regular Members' and 'Nominal & Associate Members', the AO has established that the no. of the associate members are more than the regular members. It was therefore evident that the appellant has been accepting deposits and earning interest income from nominal and associate members as well. As per the provisions, the appellant cannot admit members in whatever name called except regular members authorized by the provisions of Co-op Societies Act. However, it was found that the appellant is accepting deposits and also giving loans to second category of members viz nominal members termed as associate members.*

6.7 As regards the contention that it has admitted general public as associate members as per the provisions of Karnataka Co-op Societies Act, it is seen that the limit of 15% of total members prescribed under the Karnataka Co-op Societies Act, 1959, for other than regular members, has also exceeded since 15% comes to 574 whereas, it has admitted total number of associate members at 2038.

6.8 Above facts establish that the appellant is carrying out its activities of financing to 'associate and nominal members' who are not regular members. The associate members are not entitled to any share in the assets or profits of the appellant and do not have the right to participate or right to vote. The nominal members are not eligible to be elected as director or an office bearer of the society. Thus, it is established that the appellant is carrying out its business in violation of provisions and rules under the Karnataka Co-op Societies Act.

6.9 Facts in the present case is identical to the case of Citizen Co - Op. Credit Society Ltd., Vs ACTT C-((1), Hyderabad. (supra) and in view of the same, relying respectfully on the decision of Hon'ble Supreme Court decision (supra), it is held that the deduction under section 80P(2)(a)(i) is not admissible in respect of income earned from 'nominal members and associate member' and therefore, the disallowance of deduction of Rs. 31,36,705/ u/s 80(P) (2)(a)(i) is confirmed. Grounds of appeal No. 2 to 7 are **DISMISSED.**”

3. After hearing both the parties, in my opinion, similar issue was considered by the Tribunal in the case of Ravindra Multipurpose Co-operative Society Ltd. Vs. ITO in ITA No.1262/Bang/2019 dated 31.8.2021 wherein held as under:-

4.1. We have considered the rival submissions of both sides in the light of records placed before us.

4.2. The issue that arises for consideration is:

(i) whether the authorities below were justified in denying the claim of the assessee for reduction u/s 80P(2)(a)(i) of the Act. (Grounds 2-4, Additional Ground no.1)

(ii) whether, interest income earned by assessee is eligible for deduction u/s 80P(2)(d) of the Act, whereas the deduction is one claimed u/s 80P(2)(a)(i) of the Act. (Additional ground 2)

5. Ground No.1 is general in nature and therefore do not require any adjudication.

6. Grounds 2-4 & Additional Ground No.1:

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In respect of associate/nominal members, Hon'ble Supreme Court in the case of Mavilayi Service Cooperative Bank Ltd. v. CIT (2021) 123 [taxmann.com](https://www.taxmann.com) 161 (SC) has held that the expression "Members" is not defined in the Income-tax Act. Hence, it is necessary to construe the expression "Members" in section 80P(2)(a)(i) of the Act in the light of definition of that expression as contained in the concerned co-operative societies Act. In view of this, the facts are to be examined in the light of principles laid down by the Hon'ble Supreme Court in Mavilayi Service Cooperative Bank Ltd. (supra). Accordingly, we remit this issue of deduction u/s.80P(2)(a)(i) of the Act to the file of Ld.AO to examine the same de novo in the light of the above judgment. Needless to say that proper opportunity of being heard is to be granted to assessee in accordance with law

Accordingly grounds 2-4 and Additional Ground No.1 stands allowed for statistical purposes.

7. Additional Ground 2 is in respect of interest from investment in Co-operative banks, nationalised banks.

7.1 This issue has been decided by coordinate bench of this Tribunal in case of Potters Cottage Industrial Co-Operative Society Ltd., for assessment years 2015-16 in ITA No 1257 & 1258/Bang/2019 by order dated 30-08-2019. This Tribunal observed and decided as under:

"We note that the Ld.AO denied deduction under section 80P(2)(d) of the Act, as well in respect of interest income received by assessee from deposits kept with banks for the years under consideration. The Ld.AO assessed the interest income received from bank deposits under the head income from other sources.

The Ld.Counsel placed reliance on the decision of Hon'ble Karnataka High Court in keep case of Totgars co-operative sale society Ltd. vs ITO reported in (2015) 58 [Taxmann.com](https://www.taxmann.com) 35.

We have perused plethora of decisions on this issue by Hon'ble Karnataka High Court and the ratio laid down by Hon'ble Supreme Court. Hon'ble Supreme Court in the case of the Totgars Co-operative Sale Society Ltd. Vs. ITO reported in 322 ITR 283 held that, Income from utilisation of surplus funds was taxable under the head income from other sources, and therefore not eligible for deduction u/s 80P.

Hon'ble Karnataka High Court in case of Tumkur Merchants Souharda Credit Cooperative Ltd. vs. ITO reported in 230 Taxman 309, dealt with an issue where deduction u/s.80P(2)(a)(i) of the Act was claimed on interest from the deposits made in a nationalized bank which was used for providing credit facilities to its members. The Assessee therein claimed that the said interest amount is attributable to the credit facility provided by the assessee and forms part of profits and gains of business. Hon'ble Karnataka High Court after considering the decision by Hon'ble Supreme Court in case of Totgars(supra) held that, since the word income is qualified by the expression "attributable" to the business of

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Banking, is used in Sec.80P(2)(a)(i) of the Act, it has to receive a wider meaning and should be interpreted as covering receipts from sources other than the actual conduct of business. Hon'ble Karnataka Court held that a Cooperative Society that is carrying on with the business of providing credit facilities to its members, earns profits and gains of business by providing credit facilities to its members. The interest income so derived or the capital, if not immediately required to be lent to the members, cannot be kept idle. If they deposit this amount in bank so as to earn interest, the said interest income is attributable to the profits and gains of the business of providing credit facilities to its members only. The society is not carrying on any separate business for earning such interest income. The income so derived is the amount of profits and gains of business attributable to the activity of carrying on the business of banking or providing credit facilities to its members by a co-operative society and is liable to be deducted from the gross total income under Section 80P of the Act. Hon'ble Karnataka Court distinguished the facts in the decision of the Hon'ble Supreme Court in the case of Totgars (supra) by observing that Hon'ble Supreme Court was dealing with a case where the assessee-cooperative society, apart from providing credit facilities to the members, was also in the business of marketing of agricultural produce grown by its members. The sale consideration received from marketing agricultural produce of its members was retained in many cases. The said retained amount which was payable to its members from whom produce was bought, was invested in a short-term deposit/security. Such an amount which was retained by the assessee-Society was a liability and it was shown in the balance sheet on the liability side. Therefore, to that extent, such interest income cannot be said to be attributable either to the activity mentioned in section 80P(2)(a)(i) of the or under Section 80P(2)(a)(iii) of the Act. Therefore, in the facts of Totgars (supra), Hon'ble Supreme Court held the assessing officer was right in taxing the interest income indicated above under Section 56 of the Act. The Court also observed that even the Hon'ble Supreme Court made it clear that, they are confining the said judgment to the facts of that case.

Similar view taken in case of Guttigedarara Credit Co-operative Society Ltd. vs. ITO reported in [2015] 377 ITR 464 by Hon'ble Karnataka High Court. In a subsequent decision of Pr.CIT And Anrs vs. Totgars Co-Operative Sale Society reported in 392 ITR 74 in the context of deduction u/s.80P(2)(d) of the Act, it was held by Hon'ble Karnataka high Court that deduction in respect of any income by way of interest or dividends derived by the co-operative society from its investments with any other co-operative society, the whole of such income is available under sec.80P(2)(d) of the Act. Hon'ble Karnataka high Court held that decision by Hon'ble Supreme Court in case of Totgars (supra), was not on the deduction claimed u/s.80P(2)(d) of the Act, but was rendered in respect of deduction claimed under Section 80P(2)(a)(i) of the Act. Hon'ble Karnataka High Court in the case of Pr.CIT Anr. vs. Totgars Co-Operative Sale Society reported in 395 ITR 611 took a different view and held that interest income earned on deposits whether with any other bank will be in the nature of income from other sources and not income from business and therefore the deduction u/s.80P(2)(d) of the Act cannot be allowed to the

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Assessee. The Hon'ble Court followed decision of Hon'ble Gujarat High Court in the case of SBI Vs. CIT reported in 389 ITR 578, wherein Hon'ble Gujarat High Court dissented from the view taken by the Hon'ble Karnataka High Court in the case of Tumkur Merchants case (supra). It can thus be seen that the ratio laid down by the Hon'ble Karnataka High Court in the case of Totagars Cooperative Sales Society in 395 ITR 611 is that, in light of the principles enunciated by Hon'ble Supreme Court in Totgars Co-operative Sale Society (supra), in case of a society engaged in providing credit facilities to its members, income from investments made in banks does not fall within any of the categories mentioned in section 80P(2)(a) of the Act. Thus interest earned from investments made in any bank, not being a co-operative society, is not deductible under section 80P(2)(d) of the Act. However, section 80P(2)(d) of the Act specifically exempts interest earned from funds invested in co-operative societies. Therefore, to the extent of the interest earned from investments made by assessee with any co-operative society, a co-operative society is entitled to deduction of the whole of such income under section 80P(2)(d) of the Act. This needs to be verified by the Ld.AO.

On the basis of above discussions, and in the interest of Justice we remand this issue back to the Ld.AO to verify the interest earned from investments made in co-operative societies that is eligible for deduction under section 80P(2)(d) of the Act.”

11.2 Respectfully following the above view, we direct the Ld.AO to verify the interest earned on investment earned from co-operative societies and to consider the claim of assessee in accordance with law under section 80p(2)(d) of the Act.

Accordingly these grounds raised by assessee stands allowed for statistical purposes.

Accordingly, the appeals filed by assessee for assessment years under consideration stands allowed for statistical purposes.

In the result, the appeal of the assessee is allowed for statistical purposes.”

4. In view of the above order of the Tribunal, taking a consistent view, the issue in dispute before me is remitted to the file of AO for fresh consideration on similar line. Ordered accordingly.

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5. In the result, the appeal filed by the assessee is partly allowed for statistical purposes.

Order pronounced in the open court on 28th Dec, 2022

Sd/-
(Chandra Poojari)
Accountant Member

Bangalore,
Dated 28th Dec, 2022.
VG/SPS

Copy to:

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

By order

Asst. Registrar,
ITAT, Bangalore.