**IN THE INCOME TAX APPELLATE TRIBUNAL**
**"SMC - A" BENCH : BANGALORE**

**BEFORE SHRI GEORGE GEORGE K, VICE PRESIDENT**

| ITA No.419/Bang/2023 |
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| Assessment Year : 2017-18 |

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| M/s. Belur Urban Co-operative Bank Ltd.,<br>1, Old Post Office Road,<br>Belur, Hassan – 573 115.<br>**PAN : AAAAB 7546 D** | Vs. | ITO,<br>Ward –2,<br>Belur Road,<br>Hassan. |
| APPELLANT | | RESPONDENT |

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| Assessee by | : | Shri. Mahesh R. Uppin, Advocate |
| Revenue by | : | Shri. Ganesh R Ghale, Advocate, Standing Counsel for Revenue. |

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| Date of hearing | : | 21.11.2023 |
| Date of Pronouncement | : | 22.11.2023 |

## O R D E R

This appeal at the instance of the assessee is directed against CIT(A)'s order dated 27.03.2023, passed under section 250 of the Income Tax Act, 1961 (hereinafter called 'the Act'). The relevant Assessment Year is 2017-18.

2. Brief facts of the case are as follows:

Assessee is a co-operative society registered under the Karnataka Co-operative Societies Act, 1959. For the Assessment Year 2017-18, return of income was filed on 31.01.2017 declaring loss of Rs.5,43,167/-. The return was selected for scrutiny and notice under section 143(2) of the Act was issued on 24.09.2018. During the course of assessment proceedings, the AO got reconciled the interest income and interest expenses on accrual basis and assessment was completed under section 143(3) of the Act on 12.12.2019 by determining the total

income of Rs.31,17,724/-. The AO made an addition of Rs.36,60,891/- on account of difference in interest income on accrual basis.

3. Aggrieved by the Assessment Order, assessee filed appeal before the First Appellate Authority (FAA). Assessee contended before the FAA that it had not accounted the interest receivable. It was submitted that it is in consonance with Rule 22 of the Karnataka Co-operative Societies Rules, 1960. Further, the assessee relied on the judgment of the Hon'ble jurisdictional High Court in the case of CIT Vs. Urban Co-operative Bank Ltd., in ITA No.471/2013 (judgment dated 30.06.2014). The CIT(A), however, distinguished the case law relied on by the assessee and held that interest is recoverable (though not credited in the P & L account) since the state government had assured the reimbursement of interest. Further, the CIT(A) held that assessee cannot be allowed to have hybrid system of accounting and interest income has to be assessed on accrual basis. The CIT(A) also noted at para 9.7 of the impugned order that assessee did not press the ground relating to the taxability of interest income only in the year of receipt as per the provisions of section 145B(3) of the Act. Thus, the appeal of assessee was dismissed by the CIT(A).

4. Aggrieved by the order of the CIT(A), assessee has filed the present appeal before the Tribunal raising the following grounds:

1. *Does the addition made for Interest Receivable on Loans amounting to Rs. 36,60,891/-in the impugned Order is sustainable even when the said interest was not realized and hence not taken to profit as the same relates to Non-Performing Assets;*

2. *Whether the accounting of interest by the appellant in consonance with the governing statute, viz: Rule 22 of Karnataka Co-op. Societies Rules, 1960*

*(involving cash basis as well as mercantile basis) being consistently followed be disputed to make addition;*

3. *The additions made in the impugned order run contrary to the judgement of* ***Dy. CIT vs. Parikh Petro Chemical Agencies (P) Ltd. [2002] 81 ITD 18 (Mum.-Trib.)***

4. *In the absence of income computation/ disclosure standards notified by the Central Govt. for appellant society in accordance with Sec. 145(2) of the Act, the addition made in the impugned order is in violation of Sec. 145(3) of the Act and hence liable to be deleted.*

5. *The addition made is also opposed to the decision of jurisdictional Hon. High Court of Karnataka in ITA: 471/2013 in CIT & anr. vs. Urban Co-operative Bank Ltd. Shikaripura.*

6. *The appellant craves leave to add, delete, to amend, modify and /or to alter any of the foregoing grounds and also urge such other grounds at the time of hearing.*

5. The learned AR submitted that there was a mistake in submission before the lower authorities. It was stated that the state government has not stood as a guarantor for the reimbursement of interest which is not recovered in respect of loans which has become Non-Performing Assets (NPAs). In this context, the learned AR relied on the judgment of the Hon'ble jurisdictional High Court in the case of CIT Vs. Urban Co-operative Bank Ltd., (supra). The learned AR further submitted that some of the interests were recovered and duly offered to tax in the year of receipts. It was submitted that in the interest of justice and equity, the matter needs to be examined afresh by the AO.

6. The learned Standing Counsel supported the orders of the AO and CIT(A).

7. I have heard the rival submissions and perused the material on record. It is the claim of the learned AR that the assessee had computed income in consonance

with Rule 22 of Karnataka Co-operative Societies Rules, 1960 which reads as under:

> *"22. Manner of determining net profits under sub-section (1) of Section 57 and rate at which dividend may be paid by Co-operative Societies.—(1) In determining net profits from which not less than 25 per cent are to be taken to the reserve fund under sub-section (2) of Section 57, the following procedure shall be adopted.—*
>
> > *(a) All interest accrued due, but not actually realised shall be deducted from the gross profits for the year, before the net profits are arrived at. So much of the accrued interest that has been so deducted from the profits :of the year, as are actually recovered during the subsequent year, may be added to the profits of the subsequent year. The Registrar may, in special cases and after due enquiry, permit a society to treat interest accrued due for a period not exceeding one year as profits; but, if the amount so permitted to be treated as profits is not actually recovered during the subsequent year, it shall be deducted from the profits of such subsequent year before the net profits of that year are arrived at;"*

8. However, it is to be noted that section 145 of the Act does not permit the assessee to follow the hybrid system of accounting. In other words, if the interest income has accrued, the same is to be brought to tax in the year of accrual though it is received in the subsequent year. Further, question is whether there is a right to receive / accrual in the relevant Assessment Year. It is the case of the assessee before the Tribunal that principal amount itself has not been recovered much less the interest on the same. Consequently, the interest on these NPAs is never accounted for since there is no right to receive the same in the relevant year. In the interest of justice and equity, I am of the view that the matter requires reconsideration at the level of the AO. Assessee shall provide the necessary proof to show that interest which is not accounted for in the books of accounts is on the NPAs which is not recoverable. Assessee is also directed to furnish necessary material to prove when interest income was received subsequently, the same was

offered to tax in the year of receipt. To examine these aspects, the matter is restored to the files of the AO. It is ordered accordingly.

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

*Pronounced in the open court on the date mentioned on the caption page.*

**Sd/-**

**(GEORGE GEORGE K)**
**Vice President**

Bangalore.
Dated: 22.11.2023.
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| 1. | Appellants | 2. | Respondent |
| 3. | DRP | 4. | CIT |
| 5. | CIT(A) | 6. | DR,ITAT, Bangalore. |
| 7. | Guard file | | |

By order

Assistant Registrar,
ITAT, Bangalore.