IN THE INCOME TAX APPELLATE TRIBUNAL
COCHIN BENCH, COCHIN

Before Shri Sanjay Arora, AM & Shri Manomohan Das, JM

ITA No.61/Coch/2023: Asst.Year:2017-2018
ITA No.62/Coch/2023: Asst.Year:2018-2019

Sivapuram Service Co-operative Bank Limited UP 21/784, Sivapuram Kariyathan Kavu PO Kozhikode-673612. [PAN: AAJAS3940H]	vs.	The Income Tax Officer Ward 2(3), Kozhikode.
(Appellant)		(Respondent)

ITA No. 1010/Coch/2022
(Assessment Year: 2014-15)

Vilavattam Service Co-op. Bank Ltd. P.O. Kurichikkara Thrissur 680028 [PAN:AAAAV9819K]	vs.	The Income Tax Officer - 2(3) Aayakar Bhavan Shakthanthampuran Nagar Thrissur - 680001
(Appellant)		(Respondent)

Appellants by:	Parvathy Ammal, CA; Shri Ajith Kaimal R., CA
Respondents by:	Smt. J.M. Jamuna Devi, Sr. D.R.

Date of Hearing : 14.9.2023		Date of Pronouncement: 13.12.2023

O R D E R

Per Sanjay Arora, AM:

This is a set of three Appeals by two different assesses directed against the orders dated 19/11/2022 & 21/11/2022 by the National Faceless Appeal Centre, Delhi ('CIT(A)'), dismissing their appeals contesting their assessments under section 143(3) of the Income Tax Act, 1961 ('the Act') for Assessment Years (AYs) 2014-15, 2017-2018 and 2018-2019. The issues arising in these appeals being common, the appeals were heard together, and are being disposed of vide a common order.

2. The basis for the denial of deduction u/s.80P to the appellant-assessees, registered as primary agricultural credit co-operative societies (PACS) under the Kerala Co-operative Societies Act, 1969 (Kerala Act), claimed in full u/s. 80P(1) r/w s. 80P(2)(a)(i) / 80P(2)(d), on its gross total income, are as under:

(a) 27.8% (AY 2017-2018) and 23.6% (AY 2018-2019) of its total advance, based on the balance sheet figures as at the relevant year-end, are for other than agricultural purposes;

(b) Loans being extended other than Class A members, i.e., who alone have voting rights; the right to surplus, etc., i.e., the real members, as opposed to Class B, C and D members, who are only nominal members;

(c) There is no specific clause in the bye-laws of the assessee-society, which does not permit admission of any other co-operative society as it's member.

(d) The paid-up share capital of the assessee-society is in excess of Rs. 1 lac, i.e., the monetary limit for it to be regarded as a primary credit society under the Kerala Act.

In addition to the above, the Revenue also claims the assessee/s to have a public character, i.e., is not a co-operative society meant for it's members only, inasmuch as they are accepting deposits from the public, satisfying thus the test of being in the business of banking as defined u/s. 5(b) of the Banking Regulation Act, 1949 (BRA), which reads as under:

'5(b) "banking" means the accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft order or otherwise.'

Reliance for the purpose is placed, *inter alia*, on *Mavilayi Service Co-operative Bank Ltd. v. CIT* [2021] 431 ITR 1 (SC); *The Citizen Co-operative Society Ltd. v. Asst. CIT* [2017] 397 ITR 1 (SC), as indeed *Pr.CIT v. Poonjar Service Co-op. Bank Ltd.* [2019] 414 ITR 67 (Ker)(FB).The only difference in the case of Vilavattam SCB Ltd. is that the ratio of agricultural advances is at a negligible 0.12%, and the claim for deduction is in entirety u/s. 80P(2)(a)(i). The matters were heard at length; the issue arising being principally legal.

3. We have heard the parties, and perused the material on record.

3.1 Both the objections (a) and (b) do not survive in view of the decision by the Hon'ble Apex Court in *Mavilayi SCB Ltd.* (supra), which also considers *The Citizen Co-operative Society Ltd.* (supra), toward which reference to paras 13, 28, 29, 31, 33 to 35 was made by Ms. Ammal, the ld. counsel for the assessee, during hearing. As regards objections (c)& (d), which find mention in the assessment orders, it is unfortunate that the same were not brought to our notice by the parties during hearing nor in fact covered in their arguments, and stand noticed by us only at the time of reading the appeal file for the purpose of dictation. The assessee (Sivapuram SCB Ltd.) has also not met the same per it's written submissions before the first appellate authority, whose order is therefore *sub silentio* in its respect, even as he upholds the findings by the AO inasmuch as the same remained uncontroverted before him. The parties were, accordingly, upon notice, heard in the matter.

4.1 We proceed with the case of Vilavattam Service Co-op. Bank Ltd. inasmuch as the orders by the Revenue authorities in this case are much more elaborate and exhaustive. Clause 56 of it's bye-laws – referred to in their orders by both the Revenue authorities, is, as stated – and which is not rebutted at any stage, including before us, allows the assessee to accept deposits from both, members and non-members, and which can be deposited with the assessee-bank in saving, current account and Bhandara Nikshepam. The test of section 5(b) of BRA is thus satisfied, with there being a mechanism in place for withdrawal from their deposit accounts by the depositors. Now, clearly, acceptance of deposits from members and non-members (i.e., other than members), implies acceptance thereof from public at large. Sections 58 to 60 of the Kerala Act read as under, providing thus the legal basis for cl. 56 of the bye-laws:

58. *Restriction on borrowings.*-A society shall receive deposits and loans only to such extent and under such conditions as may be prescribed or as may be specified in the bye-laws.

59. *Restrictions on loans*.-(1) A society shall not make a loan to any person or a society *other than a member*:
Provided that the above restriction shall not be applicable to the Kerala State Co-operative Bank:
Provided further that, with the general or special sanction of the Registrar, a society may make loans to another society.

(2) Notwithstanding anything contained in sub-section (1), a society may make a loan to a depositor on the security of his deposit.

(3) Granting of loans to members or to non-members under sub-section (2) and recovery thereof shall be in the manner as may be specified by the Registrar.

60. *Restrictions on other transactions with non-members*.– Save as is provided in sections 58 and 59, the transactions of a society *with persons other than members* shall be subjected to such restrictions, if any, as may be prescribed. (emphasis, ours)

Section 58 mandates that acceptance of deposits and loans – which could be therefore from members and non-members, would be to such extent and on under such conditions as may be either prescribed or specified in the byelaws. Section 59 bars lending to non-members other than against their own deposits. Transactions *qua* non-members, other than that specified in ss. 58 and 59, i.e., borrowing from or lending thereto, shall, in terms of s. 60, be subject to such restrictions as may be prescribed. There is, further, no claim of any bye-law in case of Sivapuram SCB Ltd. prohibiting acceptance of deposits from non-members. Under the circumstances, there is nothing on record to draw a distinction between the two assessees before us.

4.2 Before us, it was contended that though not proscribed, there has been, on facts, no acceptance of deposits from non-members. We find this as of no moment. Firstly, any member of the public can, upon paying a small, nominal sum, become a nominal member, with no rights and privileges of a member, i.e., as to participation in the surplus; voting rights, etc., of a regular member. A person is stated to be compulsorily made a nominal, i.e., other than category A, member, prior to giving loan to him; a charge not denied, which may extend to acceptance of deposit as well. The reality of the matter cannot be ignored, and there is, thus, in effect and substance, acceptance of deposits from the public. The practice also operates to

dissolve any difference, if any, between the two assessees before us. Reference is made to *J.B. Bode & Co. Pvt. Ltd. v. CBDT* [1997] 223 ITR 271(SC) for the proposition that a matter of fact is to be viewed not from a technical stand-point, but in its substance. Secondly, whether on facts it has indeed accepted deposits from non-members, and to what extent, is irrelevant. The fact relevant and sufficient for the purpose is that it is authorized by it's governing Act and it's constitution to do so. Reference in this context be made to the decision in *Delhi Stock Exchange Association Ltd. v. CIT* [1997] 225 ITR 235 (SC). In the facts of the case, the assessee's claim for exemption of income u/s. 11 of the Act was, admitting that running a stock exchange was an object of general public utility and, thus, a charitable object by definition, rejected in the absence of any prohibition for dividend to it's shareholders and specific provision for creating funds for their benefit or for the employees or their relations. The decision by the Tribunal was upheld by the Hon'ble Courts; there being no trust and legal obligation compelling the assessee to utilize it's income only for charitable purposes, so that it was at liberty to distribute its entire profit or income by way of dividend. That is, prior to the amendment in clause (xiv) of Article 103 of it's Articles of Association in December, 1973. Whether any dividend was in fact distributed, was, as explained, not relevant, but the authority to do so, and toward which, apart from the byelaws, reference stood made to SCRA, 1956 and the letters received from the Government. There is further no restriction as to the area of operation for co-operative societies, as the assessees before us, for a society registered prior to the commencement of the amendment Act of 1999. The character of the assessees' as public bodies, undertaking banking business, is thus established. We may further advert to s. 5(cciv) of the BRA, which provides, *qua* a PACS, for, apart from it's lending profile as predominantly for agricultural and related purposes, a restriction on the admission of a co-operative society as it's member, absent in the instant case, as under:

> "56. Act to apply to co-operative societies subject to modifications.—The provisions of this Act, as in force for the time being, shall apply to, or in relation to, co-operative

societies as they apply to, or in relation to, banking companies subject to the following modifications, namely :—

(a) throughout this Act, unless the context otherwise requires,—

(i) references to a 'banking company' or 'the company' or 'such company' shall be construed as references to a co-operative bank,

(ii) references to 'commencement of this Act' shall be construed as references to commencement of the Banking Laws (Application to Co-operative Societies) Act, 1965 (23 of 1965) ;

(b) in section 2, the words and figures 'the Companies Act, 1956 (1 of 1956), and' shall be omitted;

(c) in section 5,—

(i) after clause (cc), the following clauses shall be inserted namely :—

(cci)…(cciii)

(cciv) 'primary agricultural credit society' means a co-operative society,—

(1) the primary object or principal business of which is to provide financial accommodation to its members for agricultural purposes or for purposes connected with agricultural activities (including the marketing of crops) ; and

(2) the bye-laws of which do not permit admission of any other co-operative society as a member:

Provided that this sub-clause shall not apply to the admission of a co-operative bank as a member by reason of such co-operative bank subscribing to the share capital of such co-operative society out of funds provided by the State Government for the purpose;"

The assessee-society/s is, thus, on both counts, not a PACS under BRA, which Act alone is relevant for the purpose of satisfaction or otherwise of the condition of section 80P(4). It is, therefore, eligible for being licenced by RBI, as required u/s. 22 of BRA for the conduct of business of banking in India. That is, it would not be in view of being not a PACS under BRA, excluded u/s. 3 thereof. That the assessee-society/s had not applied for licence to RBI – which could possibly be for the reason of being registered as a PACS under the Kerala Act, is another matter and, to our mind, irrelevant. That would only make the assessees as co-operative societies undertaking banking business in India, albeit without a licence from the regulatory body and, thus, illegal inasmuch as section 22 bars the same, operating thus outside the administrative control of the RBI. It would not detract from the fact of the assessee/s undertaking banking business or of being entitled to being licensed under

BRA inasmuch as it is, by definition, not a PACS there-under. Why, as argued at the instance of the Revenue in *Mavilayi SCB Ltd.* (supra) (pg. 16 of the Reports), RBI itself had issued a press release cautioning the public from dealing with societies engaged in the business of banking without licence there-from. The consequence of being unlicensed would make its income as from an illegal business, which is as much liable to tax as the income of a legal business. That is, it would not alter the nature or character of the income, which would thus continue to be eligible for the same treatment under the Act as the income of the legal business. In *Mohammed Usman v. Registrar of Co-operative Societies*, AIR 2003 (Ker) 299/[2003] 116 Company Cases 505 (Ker) /2003 (1) KLT (69), relied upon by the Revenue, discussing the provisions of BRA in detail, it was explained that a credit society doing banking activity, where it's capital exceeds Rs.1 lakh, would assume the character of a co-operative bank. We also find support from the decision in *Asst. CIT v. Quepem Urban Co-operative Credit Society Ltd*. (ITA Nos. 335-337/Pnj/2014, dated 26/11/2014), also relied upon by the Revenue. The requirement of being licensed must therefore be in context read down to being entitled to be licensed in the given facts and circumstances of the case.

4.3 The question that, however, is to be considered, is if the assessee is a 'co-operative bank'. This is as being not a PACS would not by itself imply it being a co-operative bank, which only is excluded u/s. 80P(4) from the purview of section 80P. Section 5(cci) of BRA, which Act again is only relevant in terms of section 80P(4), defining 'cooperative bank', reads as under:

"5 (cci) 'co-operative bank' means a state co-operative bank, a central co-operative bank and a primary co-operative bank;"

The first two banks are defined u/s. 5(ccvii) with reference to NABARD Act, i.e., under sections 2(d) and 2(u) thereof respectively, being the principal societies for financing other co-operative societies in the respective state and district respectively. The assessee/s clearly does not fall under either of them. It also does not qualify to

be a 'primary co-operative bank', i.e., the third category comprising a co-operative bank, defined u/s. 5(ccv), reading as under, as it admittedly does not satisfy requirement (3) of the provision:

> "5 (ccv) 'primary co-operative bank' means a co-operative society, other than a primary agricultural credit society,—
>
> (1) the primary object or principal business of which is the trans action of banking business;
>
> (2) the paid-up share capital and reserves of which are not less than one lakh of rupees; and
>
> (3) the bye-laws of which do not permit admission of any other co-operative society as a member:
>
> Provided that this sub-clause shall not apply to the admission of a co-operative bank as a member by reason of such co-operative bank subscribing to the share capital of such co-operative society out of funds provided by the State Government for the purpose;

Again, true, a co-operative bank has been explained by the Hon'ble Courts in *The Citizen Co-operative Society Ltd*. (supra) and *Mavilayi Service Co-op. Bank Ltd*. (*supra*), as a co-operative society engaged in the banking business. The same, yet, does not take the Revenue's case far. Section 80P(4) clearly excludes only a 'co-operative bank', as defined therein. Taxing statutes are to be strictly construed; more so, the exemption provisions. As such, even though qualifying to be a banking company u/s. 5(c) of the BRA inasmuch as it defines a banking company as a company which transacts the business of banking in India, reference to which must be construed as reference to a co-operative bank in view of the non-obstante provision of section 56 of BRA, yet the same Act clearly defines the term 'co-operative bank', which definition stands adopted in section 80P. As such, only where the assessee-society is a primary co-operative bank in terms of section 5(ccv), which it is not, would it qualify to be regarded as one and, thus, excluded u/s. 80P(4) from the benefit of section 80P(1). Reference in this context be made again to *The Citizens CS Ltd*. (supra); *Mavilayi SCB Ltd*. (supra);and *Kerala State Cooperative Agricultural & Rural Development Bank v. AO* [2023] 458 ITR 384 (SC). The assessee thus is not hit by the mischief of section 80P(4).

4.4 The next question before us is if the appellant-society/s indeed qualifies to be a co-operative society, the basic requirement for being eligible for exemption u/s. 80P(1). This follows as a fall-out of the assessee being, as afore-noted, not a PACS by definition (para 4.2). The assessee has to per it's charter definitely fall under any of the categories of co-operative societies to stake it's claim as one under the Kerala Act and, thus, entitled for the benefit u/s. 80P(1) by virtue of section 2(19) of the Act. We are conscious that this would raise the question as to if the AO can go behind the registration certificate granted by the Registrar of Co-operative Societies. As a reading of the decision in *Mavilayi SCB Ltd*. (supra) shows, decisions both ways were advanced before the Hon'ble Court in the matter, which did not consider it necessary to answer the same as the assessee-appellant was admittedly not a co-operative bank and, thus, not hit by section 80P(4), so that the assessee being a PACS or not was not relevant. The question, however, arises before us in the context of section 80P(1), and not 80P(4), as, if not a PACS, on what basis, one may ask, does the assessee claim to be or qualify as a co-operative society? That is, the assessee has to answer the description of a co-operative society under the Kerala Act, i.e., under which it is registered, being basic to it's claim for deduction u/s. 80P(1). The imbroglio, if one may term it as so, would not, however, detain us as the assessee is, by definition, a PACS under the Kerala Act. Section 2(oaa) thereof defines PACS as:

"2. In this Act, unless the context otherwise requires,—. . .

(f) 'Co-operative Society' or 'society' means a Co-operative society registered or deemed to be registered under this Act ; . . .

(oaa) 'Primacy Agricultural Credit Society' means a Service Co- operative Society, a Service Co-operative Bank, a Farmers Service Co- operative Bank and a Rural Bank, the principal object of which is to undertake agricultural credit activities and to provide loans and advances for agricultural purposes, the rate of interest on such loans and advances shall be the rate fixed by the Registrar and having its area of operation confined to a Village, Panchayat or a Municipality;

Provided that the restriction regarding the area of operation shall not apply to Societies or Banks in existence at the commencement of the Kerala Co-operative Societies (Amendment) Act, 1999 (1 of 2000).

> **Provided further** that if the above principal object is not fulfilled, such societies shall lose all characteristics of a Primary Agricultural Credit Society as specified in the Act, Rules and Bye-laws except the existing staff strength. . . ."

There is no reference therein, as in the case of s. 5(cciv) of BRA, to a restriction in its byelaws for admission of other cooperative societies as it's members. Reference to section 5(cciv) of BRA for the purpose of section 2(19) of the Act is mistaken. This constitutes the second flaw in the Revenue's case, the first being of the assessee, though decidedly in the business of banking, not a co-operative bank in terms of section 80P(4), to be hit thereby.

True, we are conscious that a society registered as a PACS stands to loose all it's characteristics, i.e., other than existing staff strength, on failing to fulfill, as in the instant case, it's principal object, i.e., providing credit through it's members primarily for agricultural and allied purposes, it yet continues to be, in terms of the said Act, a cooperative society, defined u/s. 2(f) thereof as a society registered or deemed to be registered under the said Act. And on which there can be no quarrel, particularly in view of s. 8 of the said Act, stating the registration certificate to be a conclusive evidence of it's registration, which is, further, on the basis of declared objects (s.7). The appellant-societies, thus, despite loosing all the characteristics of a PACS in view of their activities subsequent to registration, yet continue to be primary agricultural cooperative societies under the Kerala Act. This is again principally for the reason that taxing statutes, and more so the exemption provisions, are to be strictly read. It would be a different matter, we may add, where the benefit u/s. 80P(1), which in the instant case is u/s. 80P(2)(a)(i), was for agricultural credit. As explained in *Mavilayi SCB Ltd*. (supra) itself, referring to *Udaipur Sahakari Upbhokta Thok Bhandar v. CIT* [2009] 315 ITR 21 (SC), the burden to prove it's claim for exemption is on the assessee, who is, therefore, to show of it being entitled to the benefit of s. 80P(2)(a)(i). And, that the AO cannot be considered as going behind the registration certificate when he examines the satisfaction or otherwise of s. 80P(2)(a)(i).

4.5 The next question before us is; the assessee/s having been found to be in the business of banking, the satisfaction of condition of section 80-P(2)(a)(i). Carrying on the said business is as much an eligible activity thereunder as is the provision of credit to it's members; both being regarded as eligible activities, i.e., at par. As explained in *Mavilayi SCB Ltd*. (supra), s. 80P(4) is in the nature of a *proviso*, which cannot be read to cut down the plain language of the main enactment. The assessee/s is accordingly entitled to exemption on it's entire income from banking business, and without any adjustment with regard to the provision of credit to non-members, if any.

In Sum

5. The Revenue's case was of the assessees, claiming to be primary cooperative societies under the Kerala Act, undertaking the business of banking and, thus, cooperative banks, ineligible for exemption u/s. 80P u/s. 80P(4). Taxing statutes are to be strictly construed; more so, exemption provisions, with the burden to prove it's claims being on the assessee. This, coupled with the mandate that the statute is to be read in a manner so as to effectuate it's object, rather than defeat it, led us to examine the obtaining facts in light of the law as explained by the Hon'ble higher courts. The object of s. 80P(4), as explained by the Apex Court in *Mavilayi SCB Ltd*. (supra), is not the financing of agriculture *per se*, as understood by the Hon'ble jurisdictional High Court in *Poonjar SCB Ltd*. (supra), but the exclusion of the 'cooperative banks' from the purview of the beneficial provision of s. 80P.

The appellants are, despite the extent of their agricultural financing, found to be engaged in the business of banking, albeit unlicensed, and which is one of the two eligible activities u/s. 80P(2)(a)(i). On the basis of their activities and bye-laws, mutually consistent, they are further found to be a 'cooperative society' in terms of s. 2(19) of the Act, operating in pursuance of their bye-laws, consistent with the Kerala Act. And, two, not a 'cooperative bank' in terms of s. 80P(4) of the Act. The assessees' are, accordingly, entitled to deduction in full u/s. 80P(1) r/w s.

80P(2)(a)(i) in respect of income of their banking business, unimpacted by it being of an unlicensed business.

As regards the claim for deduction u/s. 80P(2)(d), i.e., in the case of Sivapuram Co-operative Society Ltd. (supra), no argument in this regard was made before us, as indeed before the Revenue authorities and, accordingly, their orders are *sans* any findings in the matter. The assessee's relevant ground speaks of interest on investment with co-operative bank. The same, to the extent not covered as a part of banking business, would stand to be exempt u/s. 80P(2)(d) in view of the decision in *Pr. CIT v. Perroorkada SCB Ltd*. [2022] 442 ITR 141 (Ker). The same is accordingly admitted and allowed to that extent.

We decide accordingly.

6. In the result, assessees appeals are allowed.

Order pronounced on December 13, 2023 under Rule 34 of The Income Tax (Appellate Tribunal) Rules, 1963

Sd/-	Sd/-
(Manomohan Das)	(Sanjay Arora)
Judicial Member	Accountant Member

Cochin; Dated: December 13, 2023
Devadas G*

Copy to:
1. The Appellant.
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4. The Sr. DR, ITAT, Cochin.
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Assistant Registrar
ITAT, Cochin