

**IN THE INCOME TAX APPELLATE TRIBUNAL
“C” BENCH : BANGALORE**

BEFORE SHRI NARENDER KUMAR CHOUDHRY, JUDICIAL MEMBER
AND
SHRI LAXMI PRASAD SAHU, ACCOUNTANT MEMBER

ITA Nos.122 & 123/Bang/2024
Assessment years : 2018-19 & 2020-21

Sri Laxminarayana Suvarna Credit Co-operative Society Ltd., 152/1, Siddapura – 581 355. Uttara Kannada. PAN : AATAS 3450L	Vs.	The Income Tax Officer, Ward 1, Sirsi.
APPELLANT		RESPONDENT

Appellant by	:	Shri Mahesh R. Uppin, Advocate
Respondent by	:	Shri Ganesh R. Ghale, Standing Counsel.

Date of hearing	:	22.02.2024
Date of Pronouncement	:	07.05.2024

ORDER

Per Laxmi Prasad Sahu, Accountant Member

These appeals are filed by the assessee against separate orders dated 19.12.2023 of the CIT(Appeals), National Faceless Appeal Centre, Delhi [NFAC], for the AYs 2018-19 & 2020-21.

2. Common issues are involved in both these appeals and the decision in ITA No.122/Bang/2023 shall apply mutatis mutandis for ITA No.123/Bang/2023.

3. The brief facts of the case for AY 2018-19 are that the assessee filed return of income declaring NIL income after claiming deduction u/s. 80P(2)(a)(i) of the Act of Rs.29,03,833 on interest income received on its investments made with Karnataka District Central Co-operative Bank (KDCC Bank) . The case was selected for scrutiny and statutory notices were issued to the assessee. The assessee filed reply. The AO noted that assessee is a credit co-operative society and mainly doing banking business and having members as follows:-

A Class members	-	628
D Class members	-	382
(Associate members)		
Nominal members	-	675

Different members have different rights and responsibilities and this violated the principle of mutuality. The assessee society was giving different types of loans like jewel loans, vehicle loans, etc. and majority of interest receipts from these kind of loans were for purposes other than agricultural purposes. The AO relying on the Supreme Court decision in Citizen Co-operative Society Ltd. [2017] 84 Taxman 114 (SC) denied deduction u/s. 80P(2)(a)(i).

4. Regarding the alternative claim of deduction u/s. 80P(2)(d) of the Act, the AO noted that interest income of Rs.29,83,833 was earned from investments with Karnataka District Central Co-operative Bank (KDCCB), even though KDCCB had skeleton of a co-operative society, its activities are at par with that of a commercial bank. Hence deduction u/s. 80P(2)(d) was also denied.

5. Aggrieved, the assessee filed appeal before the CIT(Appeals) and relying on various judgments submitted that it is eligible for deduction u/s. 80P(2)(a)(i) of the Act and alternatively claimed deduction u/s. 80P(2)(d) of the Act. The CIT(Appeals) observed that the AO's action in disallowing deduction u/s. 80P relying upon Supreme Court judgment in the case of Citizen Co-operative Society Ltd. (supra) is not correct in view of the clear cut finding in the later Apex Court judgment in the case of Mavilayi Service Co-operative Bank Ltd., 123 taxmann.com 161 (SC) that providing credit facilities to members does not necessarily mean agricultural credit alone. The assessee society in the present case is providing substantial percentage of non-agricultural loans which does not disentitle to claim deduction u/s. 80P(2)(a)(i) of the Act. Hence, in principle, the assessee is entitled to claim deduction u/s. 80P(2)(a)(i) of the Act. However, on examination of the nature of income on which deduction u/s. 80P(2)(a)(i) of the Act is claimed by the assessee, the CIT(A) noted that the interest from KDCC Bank which is a co-operative bank and noted that the assessee is not eligible for deduction. He relied on the Supreme Court judgment in the case of Totgars Co-operative Sale Society Ltd. (2010) 322 ITR 283 / 188 Taxman 282 (SC) and jurisdictional High Court judgment reported in [2017] 395 ITR 611 and observed that the Hon'ble jurisdictional High Court clearly held that interest earned from investments/bank deposits is outside the sphere of main business activity and to be categorised as "income from other sources". Since the interest income earned by the assessee from

investment in KDCC Bank is not out of business or operational income, the CIT(A) denied deduction u/s. 80P(2)(a)(i) of the Act.

6. The CIT(A) also examined the claim of deduction u/s. 80P(2)(d) on the interest income of Rs.29,03,833 earned from investment with KDCC Bank, a co-operative Bank. Relying on the judgment of Hon'ble Karnataka High Court judgment in the case of Totgars Co-operative Sale Society Ltd. [2017] 395 ITR 611 and applying the ratio decendi of Mavilayi Service Co-operative Bank Ltd., 123 taxmann.com 161 (SC), the CIT(A) observed that a co-operative bank which is working under license from RBI falls within the mischief of section 80P(4). Thus any income in the form of interest received from a co-operative bank would not be eligible for deduction u/s. 80P(2)(d) as co-operative banks functioning under license from RBI and lending and taking deposits from public are specifically excluded from the provisions of section 80P(4) and cannot be considered as a co-operative society for the purposes of section 80P. Hence the CIT(Appeals) held that the interest income earned from KDCC Bank cannot be considered as income from investment with any other co-operative society and is not eligible for deduction u/s. 80P(2)(d).

7. The CIT(Appeals) therefore rejected assessee's claim of deduction u/s 80P(2)(a)(i) or 80P(2)(d) of the Act. Against this, the assessee is in appeal before the ITAT.

8. The Id. AR reiterated the submissions made before the lower authorities and submitted that the assessee is a co-operative society and

carrying on business of providing credit facilities to its members. The assessee received interest income out of its investments with KDCC Bank which is a co-operative society registered under the Karnataka Co-operative Societies Act, 1959 (KCS Act) and accordingly deduction u/s. 80P(2)(a)(i) of the Act should be allowed. Alternatively, he submitted that interest earned by the assessee is attributable to credit business of assessee society and it is liable to be deducted from the total income as per section 80P(2)(a)(i) of the Act. The assessee was required to invest certain amounts as per section 58 of KCS Act and Rule 28 of the KCS Rules and bound to maintain fluid resources by way of statutory deposits. Therefore interest should be treated as operational income. He alternatively claimed deduction u/s. 80P(2)(d). He further submitted that if deduction u/s. 80P(2)(a)(i) or section 80P(2)(d) of the Act is not allowed, then the assessee is eligible for cost of funds as per section 57(iii) of the Act. He submitted that the revenue authorities have taxed the entire interest income without giving any benefit of cost of funds to the assessee. He relied on the following judgments:-

- (i) The Vavveru Co-operative Rural Bank Ltd., WP No.12727 & 12767/2016 (Hyderabad High Court)
- (ii) Raythara Sahakari Sangha Ltd. in ITA No.685/Bang/2023 dated 14.12.2023 (ITAT Bang.)
- (iii) PCIT v. Guru Nithyananda Credit Co-op. Society, ITA No.804/2017 (Karnataka High Court)
- (iv) Machina Service Co-operative Society Ltd., ITA Nos 124 & 125/Bang/2024 dated 22.2.2024 (ITAT Bang.)

9. The Ld.DR relied on the order of the Ld.CIT(A) and he submitted that the interest income received by the assessee is not to be considered as a business income since the Hon'ble Jurisdictional High Court of Karnataka has settled this issue in the case of Totgars' Co-operative Sales Society Ltd. reported in (2017) 395 ITR 611 (Karnataka) dated 16.06.2017. He also submitted that the Hon'ble Gujarat High Court in Katlary Kariyana Merchant Sahkari Sarafi Mandali Ltd. reported in (2022) 140 taxmann.com 602 (Gujarat) dated 04.01.2022 on similar facts had decided the issue in favour of the revenue.

10. He also submitted that the status of the payer of interest also should be seen whether it is co-operative bank or co-operative society. He relied on the judgment of Hon'ble Apex Court in case of Kerala State Co-operative Agricultural and Rural Development Bank Ltd. (KSCARDB) vs. Assessing Officer, reported in (2023) 154 taxmann.com 305 (Supreme Court). He further submitted that the interest received from Co-operative bank is also not eligible for deduction u/s 80P(2)(d) of the Act because it was received from the co-operative bank as noted by the ld. CIT (A) at para No. 6.11 which is carrying business of banking. He further submitted that the assessee society has violated the principle of mutuality therefore deduction u/s 80P(2)(a)(i) cannot be granted, relying on the judgement of Hon'ble Apex Court in the case of Citizen Co-operative Society Ltd. as relied by the lower authorities. The assessee has violated the provisions of Karnataka Cooperative Society (amendment) Act 2014, the number of

associate members under clause (a) in any co-operative society except employees co-operative society shall not exceed fifteen percent of the total regular membership.

11. He further submitted that in the case of Kerala State Co-operative Agricultural and Rural Development Bank Ltd. KSCARDB vs. The Assessing Officer, Trivandrum & Ors. (2023) 154 taxmann.com 305 the Hon'ble Supreme Court has clearly held that if the payer bank holds licence from RBI for carrying out banking business, then the interest received from such bank is not eligible for deduction u/s. 80P(2)(d), though the co-operative bank may be primarily formed as co-operative society and that the activity of the entity should be seen.

12. Considering the rival submissions, we note that here the issue is that whether the assessee is eligible to claim of deduction u/s. 80P(2)(a)(i) or 80P(2)(d) on the interest income earned on its investments amount made with District co-operative banks. The AO has discussed the issue and noted that the assessee has violated the principle of mutuality relying on the judgement of Hon'ble Apex Court in the case of Citizen Co-operative Society Ltd. noted supra and violation of Karnataka Co-operative Society (Amendment) Act 2014 and denied the deduction claimed u/s 80P(2)(a)(i) of the Act. The Ld.CIT(A) has not accepted the claim of the assessee by relying on the judgment of Hon'ble Karnataka High Court in case of Totgars' Co-operative Sales Society Ltd. (supra) and Hon'ble Apex Court in the

case of Citizens Co-operative Society Ltd. noted supra and denied deduction u/s 80P(2)(a)(i) and 80P(2)(d). During the course of hearing, the Ld.AR of the assessee relied on the Circular No. 18/2015 dated 02.11.2015 and submitted that as per the provisions of the Karnataka Co-operative Societies Act, the assessee is required to maintain SLR from the deposits received from the members and has to invest 100% from the general reserve and 25% from the deposits collected from members. Accordingly, assessee has invested in the fixed deposits. As per the circular, the income received from the investments should be treated as business income u/s. 28 and assessee is eligible to make a claim of deduction u/s. 80P(2)(a)(i) as business income. Further, the assessee submitted that the investments were made in co-operative banks which are co-operative society. Therefore the interest received on such investments are to be allowed for deduction u/s. 80P(2)(d). In support of his argument, the assessee relied on the judgements noted supra. We note from plain reading of Circular No. 18/2015 dated 02.11.2015 it is applicable to those co-operative societies / co-operative banks in which the Banking Regulation Act, 1949 applies. During the course of hearing the assessee was asked to submit the requirement of SLR as per Karnataka Cooperative Societies Act and the quantum and period for calculating SLR, the assessee was unable to give reply. Rule 23 of the Karnataka Co-operative Societies Rules states that reserve fund belongs to the society and is intended to meet the unforeseen losses. Further if the cooperative society wants to invest reserve fund or any portion thereof

for any other purpose as prescribed under section 58 (a) to (d) of the Karnataka Co-operative Societies Act permission is to be taken from , the Registrar of Co-operative Societies. Therefore the argument of the assessee that it is operational income is rejected. Even the maintainability of SLR requirement from out of internal fund/external funds invested in KDCC Bank and interest earned thereon will not change the character of the nature of income and it is not attributable to the business of the assessee. The issue regarding the word “attributable” has been discussed elaborately by the Hon’ble Apex Court in the case of M/s Totgars Co-operative Sales Society (2010) reported in [2010] 188 Taxman 282 (SC) where it is held by the Hon’ble Supreme Court that the deduction u/s 80P is available only to the income which is attributable to the business operation. Since the interest income received by the appellant is not attributable to the main business of the appellant i.e. not operational income, accordingly the interest received by the assessee on investment made with KDCC Bank is not eligible for deduction u/s. 80P(2)(a)(i) of the Act.

13. Regarding section 80P(2)(d) of the Act, we note from the submissions of the Id. AR that the assessee has invested in KDCC Bank and earned interest thereon and deduction should be allowed u/s 80P(2)(d). Section 80P(2)(d) describes that if the assessee has derived interest/dividend from its investments with any other co-operative society, then the assessee is eligible for claim of deduction on such interest/dividend derived. In the judgment of Hon’ble Apex Court in the case of Kerala State Co-operative Agricultural and Rural

Development Bank Ltd. (KSCARDB) vs. Assessing Officer, (2023) reported in 154 taxmann.com 305 (Supreme Court) it has been discussed in detail the definition of co-operative banks and co-operative society. If the payer bank falls under the definition of co-operative bank in the light of the judgment of Hon'ble Apex Court then the assessee is not eligible to get deduction u/s. 80P(2)(d) on such interest income derived from KDCC Bank. We note that the assessee has received interest from KDCC Bank is a schedule bank which is governed by the Banking Regulation Act of 1949 as observed by the Id. CIT (A) at Para No. 6.11 of his order and this finding has not been denied by the Id. AR of the assessee, accordingly we hold that the assessee is not eligible for deduction u/s 80P(2)(d) on such interest income also.

14. We further note that the assessee has received interest from KDCC Bank on its investments. The revenue authorities have considered the entire interest as income from other sources u/s. 56 and no expenses u/s. 57(iii) has been allowed to the assessee for earning of such income. While calculating the income, the net income should be considered as taxable income after reducing the expenditure incurred towards earning of such income. Therefore relying on the judgment of Hon'ble Jurisdictional High Court in case of Totgars' Co-operative Sales Society Ltd. vs ITO Sirsi, reported in (2015) 58 taxmann.com 35 (Karnataka), the assessee is eligible for claim of its cost of funds on the interest income received from bank. Reliance is also placed on the judgment of Co-ordinate Bench of the Tribunal in

case of The West Coast Paper Mill Employees Souharda Credit Co-op. Ltd. Accordingly, the assessee is directed to provide the details of cost of funds before the assessing officer. Therefore for allowing cost of funds, we are remitting this issue to the assessing officer for determining the cost of funds for earning interest income.

15. In the result, both the appeals are partly allowed for statistical purpose. A common order passed shall be kept in the respective case files

Order pronounced in the open court on this 7th day of May, 2024, as per Rule 34 of the Income Tax (Appellate Tribunal) Rule 1963.

Sd/-
(NARENDER KUMAR CHOUDHRY)
JUDICIAL MEMBER

Sd/-
(LAXMI PRASAD SAHU)
ACCOUNTANT MEMBER

Bangalore,
Dated, the 07th May, 2024.

/Desai S Murthy/

Copy to:

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

By order

Assistant Registrar
ITAT, Bangalore.