

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

BEFORE SHRI LAXMI PRASAD SAHU, ACCOUNTANT MEMBER
AND
SHRI KESHAV DUBEY, JUDICIAL MEMBER

ITA No.947/Bang/2024
Assessment year : 2017-18

Primary Agricultural Credit Co-operative Society Ltd., Temple Road, Nittur, Tumkur – 572 223. PAN : AAAAF 1047R	Vs.	The Income Tax Officer, Ward 1 & TPS, Tumkur.
APPELLANT		RESPONDENT

Appellant by	:	Shri Deepak Gunashekar, CA
Respondent by	:	Shri Ganesh R. Ghale, Standing Counsel.

Date of hearing	:	19.06.2024
Date of Pronouncement	:	03.07.2024

ORDER

Per Laxmi Prasad Sahu, Accountant Member

This appeal is filed by the assessee against the order dated 21.03.2024 of the CIT(Appeals), National Faceless Appeal Centre, Delhi [NFAC], for the AY 2017-18 not allowing deduction u/s. 80P(2)(a)(i)/ 80P(2)(d) and/or expenditure towards earning of interest income u/s 57 of the Act on the interest income on its investments.

2. Briefly stated the facts are that the assessee has filed return of income on 24.10.2017 declaring total income at Nil after claiming

deduction u/s. 80P(2)(a)(i) on the gross total income to the extent of Rs.21,25,403. The case was selected for scrutiny and statutory notices were issued to the assessee. The assessee filed the documents and the AO observed that the function of a society is mainly based on the principle of mutuality wherein, each and every member does have equal and identical rights and participation in the business of the society. It was held by various judicial authorities that such a society only can be considered for deduction u/s 80P(2)(a)(i) of the Act on the income earned from business. In the instant case , the assessee is carrying the main business of providing credit facilities to its members. The assessee society is having two category of members namely regular/normal members and nominal members. All these members are providing and utilizing the facilities provided by the Society. However, nominal members do not have the same right and facilities as that of regular/normal members accordingly the assessee society has violated the principal of mutuality and relying on the judgement of the Hon'ble Apex Court in case of Citizen Co-operative Society Ltd. (2017) 88 taxmann.com 279(SC) issued notice proposing to disallow deduction u/s. 80P(2).

3. In response the assessee submitted that the society is providing credit facilities to its members and not engaged in banking business. Business is carried out exclusively with members. Definition of member is not given in Income Tax Act and hence section 2(f) of KCS Act will prevail which includes nominal and associate member. Therefore the judgment of Citizen Co-op. Society Ltd. (supra) is not

applicable to assessee. The assessee also submitted vide its letter dated 06.08.2019 filed on 07.08.2019 stating that “The interest on deposits made with co-operative banks and scheduled banks. The interest income is the part of the business of the society in providing credit facilities to its members whenever the surplus accrued we have made deposits in the banks and it is attributable to our main business of the society, hence your assessee is eligible for deduction u/s. 80P(2)(a) of the Income Tax Act.” and relied on some judgements.

4. The AO held that principle of mutuality is missing in assessee's case as held by the Hon'ble Apex Court in the case of Citizen Co-operative Society Ltd. (supra) . The AO therefore denied deduction u/s. 80P(2)(a)(i). The AO further noted that the assessee has received interest of Rs.13,33,517/- on its investments with Co-operative Banks and Scheduled Banks and the entitlement of deduction was examined in the line of the condition stipulated in section 80P(2)(d), which allows deduction in respect of interest earned on deposits by the society but in this case it was noted that the deposits were made in the Co-operative Bank and Scheduled Bank but not with the Co-operative Society, therefore the deduction u/s 80P(2)(d) of the Act on interest received on its investments cannot be granted and the entire income were treated as income from other sources.

5. Aggrieved from the above order, the assessee filed appeal before the CIT(Appeals). The CIT(Appeals) relying on the decision of Citizen Co-operative Society Ltd. (supra) and Karnataka High Court

judgment in the case of Totgars Co-op. Sale Society denied the deduction under section 80P(2)(a)(i) and 80P(2)(d) of the Act.

6. Against the order of the CIT(Appeals), the assessee is in appeal before the ITAT.

7. The Id. AR reiterated submissions made before the lower authorities and submitted that assessee is eligible for deduction u/s 80P(2)(a)(i) as per judgment of Hon'ble Apex Court in Mavilayi Service Co-op. Bank Ltd. [2021] 123 taxmann.com 1 (SC) wherein it is held that primary agricultural credit societies are entitled to the benefit of deduction u/s. 80P(2)(a)(i) of the Act on interest income earned from lending to members including nominal members. He submitted that interest income received on assessee's investments to another co-operative society are also eligible for deduction u/s. 80P(2)(d) because the co-operative banks are primarily co-operative societies as specified in section 80P(2)(d). He further submitted that the Id. CIT(A) has not considered the judgment in the case of Tumkur Grain Merchants Souharda Credit Co-op. Ltd. reported in 55 taxmann.com 447 and the ITAT decision in Totgars Co-operative Sale Society in ITA No.376 to 379/Bang/2023 wherein interest income earned from investment in co-operative bank by multipurpose co-operative society is held eligible for deduction u/s. 80P(2)(d) of the Act. He further submitted that the assessee is a primary agricultural co-operative society engaged mainly in the business of providing credit facilities to its members and providing financial aids as well as

agricultural implements, seeds, fertilizers, pesticides etc. The assessee has earned interest on investments out of its operational fund used in business of lending to its members. The ld. CIT(A) has wrongly applied the judgments and not considered that investment in co-operative bank is a statutory requirement under Karnataka Co-operative Societies Act, 1959. Hence it is attributable to carrying on of business and society is eligible for deduction u/s. 80P(2) of the Act. He further submitted that interest income earned should not be taxed under the head income from other sources and it should be considered as business income. Even the assessee has not been granted deduction u/s. 80P(2)(d). The ld. CIT(A) has also not decided the issue in the light of Hon'ble Supreme Court judgment in the case of Kerala State Cooperative Agricultural and Rural Development Bank Ltd. in Civil Appeal No.10069/2016, order dated 14.09.2023 in which it has been held that co-operative bank is a co-operative society which is registered under Kerala Co-operative Societies Act and it is not a bank per se governed by RBI. He has also filed a written synopsis which is placed on record.

8. 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.

8.1 The Id. DR also submitted that the assessee has violated the principle of mutuality and lower authorities have relied on the judgment of Hon'ble Apex Court in the case of Citizen Co-operative Society Ltd. reported in (2017) 397 ITR 1 (SC). Accordingly the assessee is not eligible for deduction as observed by the lower authorities u/s 80P(2)(a)(i). He further submitted that in the case of Kerala State Co-operative Agricultural and Rural Development Bank Ltd. KSCARDB vs. Assessing Officer, (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. He submitted that the interest received from co-operative bank is governed by Banking Regulation Act, 1949. The Id. DR further submitted that for deduction or exemption provision the strict interpretation should be considered as decided by the Hon'ble Apex Court in the case of Commissioner of Customs (Import), Mumbai vs Dilip Kumar & Company reported in [2018] 95 taxmann.com 327 (SC)/[2018] 69 GST 239 (SC)/[2018]. The Id. DR submitted that in the case law relied by the assessee the literal interpretation of the section 80P(2) has not been done.

9. Considering the rival submissions, we note that the assessee is registered under Karnataka Co-operative Society Act 1959. During the course of assessment proceedings, the AO asked to submit details as

per notice u/s 142(1) and the AO noted as per Bye-laws that there are regular/normal members and nominal members. The regular members participate in day to day affairs, and nominal members have no role in the management of society, have no voting rights & no entitlement for share in the assets or profits. The sec. 20(2)(a) of the Karnataka Co-operative Society Act denies any right to vote to a nominal or associate members. Further the Nominal/Associate members are not entitled to attend the general meetings of the society, not eligible to contest on election. The assessee is doing business with non-members and the profit from such business is divided among the regular members of the society. The Id. DR submitted that as per the Karnataka Co-operative Society Act sec. 18 amended by the Act 2014, the associated/nominal members should not exceed 15% of the regular members, if it exceeds, then it has to be regularized within the period of six months. We note that the lower authorities have disallowed deduction on interest income received from providing credit facilities from all the members by following the judgment of Hon'ble Apex Court in the case of Citizen Co-operative Society Ltd., Hyderabad Vs. ACIT noted supra. The decision relied on by the Id. AR in the case of Mavilayi Service Co-operative Bank Ltd., (supra) is under Kerala Co-operative Societies Act in which it has been held that proportionate deduction u/s. 80P(2)(a)(i) should be granted to the assessee from the interest income received from providing credit facilities to its members but not from the non-members. The Para 33 of the said judgement says as under:-

“.....Once it is clear that the co-operative society in question is providing credit facilities to its members, the fact that it is providing credit facilities to non-members does not disentitle the society in question from availing of the deduction. The distinction between eligibility for deduction and attributability of amount of profits and gains to an activity is a real one. Since profits and gains from credit facilities given to non-members cannot be said to be attributable to the activity of providing credit facilities to its members, such amount cannot be deducted.”

The ratio of Hon'ble Apex Court in the case of Mavilayi Service Co-operative Bank Ltd., (supra) is very much applicable for computing the income attributable to the business of the assessee among the members and non-members. The assessee is governed by Karnataka Co-operative Societies Act, 1959 and assessee has to follow section 18 (amended) Act of 2014 and bye-laws of the society. We note that AO in para 5 has observed that nominal members do not have a right in share of profits of the assessee. The AO has to examine with the bylaws of the Society in regard to classification of members, their rights, sharing of profits of the society among the members (Regular/Nominal). In the event it is found that thee nominal/associate members are not members and they are not entitled from share of profits earned by the assessee, then the proportionate deduction u/s 80P(2)(a)(i) to be granted in terms of the judgment of Hon'ble Apex Court in the case of Mavilayi Service Co-operative Bank Ltd., (supra) on such income. The assessee is directed to produce the quantum of interest income received from all the categories of members for AO to carry out necessary verification. Accordingly we remit this issue to the AO for afresh consideration and determination of the interest

received from members and non-members from providing credit facilities and decide the issue as per law. The AO shall grant deduction on such interest income u/s 80P(2)(a)(i) of the Act that satisfies principle of mutuality as per bye-laws. Accordingly this issue is partly allowed for statistical purpose.

10. Further in respect of deduction u/s 80P(2)(d), 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) and/or 80P(2)(d) on the interest income earned on its investments amount made with District co-operative banks. 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. 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 of the Income Tax Act and assessee is eligible to make a claim of deduction u/s. 80P(2)(a)(i) as business income. Further, the assessee also submitted that the investments were made in co-operative banks which are co-operative society. It is

submitted by the Id. AR that interest received on such investments are to be allowed for deduction u/s. 80P(2). In support of his argument, the assessee relied on the following decisions:

- (i) Mavilayi Service Co-op. Bank Ltd. [2021] 123 taxmann.com 1 (SC).
- (ii) Tumkur Merchants Souharda Credit Co-op. Ltd. reported in 55 taxmann.com 447.
- (iii) ITAT decision in ITO vs M/s Irula Snake Catchers Industrial Co-operative Society Ltd. [TS-5808- ITAT-2022 9 Chennai)-O]
- (iv) M/S Kerala State Co-operative Agricultural & Rural Development Bank Ltd. vs AO [2023] 154 taxmann.com 305 (SC).
- (v) Saptagiri Pattina Souhadra Sahakari Sangha Niyamitha vs ITO [2024] 162 taxmann.com 855 (Bangalore Trib.).

11. 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 interest income on such

investment is operational income is rejected. Even if the maintainability of SLR requirement is out of internal fund/external funds then no deduction shall be allowed u/s. 80P(2)(a)(i), since the interest income received on such investments from co-operative banks is not attributable to main business of the appellant. The issue regarding the word “attributable” has been discussed elaborately by the Hon’ble Apex Court in the case of M/s Totgar’s 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.

11.1 Admittedly, it is a matter of fact borne from the record that the legislature in all its wisdom had inserted the provisions of Section 80P(2)(a)(i) of the Act as a part of deductions from carrying on the business of banking or providing credit facilities to its members by a Co-operative Society. Although the contention of the Ld. AR that interest received from deposit under compulsion is to be considered u/s 80P(1)(a)(i), the AO considered it as income u/s 56 of the Act. As per our considered opinion, going by the rule of literal interpretation that has to be adopted while construing the scope and gamut of a statutory provision, the same does not merit acceptance. As Section 80P(2)(a)(i) does not carve out any exception as regards the applicability of the same in a case where the investments are made under compulsion or as per any direction from Registrar of co-operative society, the aforesaid contention of the Ld. AR that the same could be considered for

deduction u/s. 80P(2)(a)(i) cannot be accepted. This view of ours that statutory provision has to be construed as per the rule of literal interpretation is supported by the judgment of the Hon'ble Supreme Court in the case of *New Noble Educational Society v. Chief CIT* [[2022\] 143 taxmann.com 276/\[2023\] 290 Taxman 206/\[2023\] 448 ITR 594/\[CA No. 3793 to 3795 of 2014 dated 19-10-2022\]](#). The Hon'ble Apex Court observed that if the language is unambiguous and capable of only one meaning, that alone should be applied and not any other, based on the surmise that the legislature intended it to be so. In other words, it is only in case of ambiguity that the court can use other aids to discern the true meaning, but where the statute is clear and the words are plain, the legislation has to be given effect in its own terms. Since, in the case of the assessee interest income received is from investments from Banks which cannot be attributed to the main business of providing credit facilities to its members, same cannot be held to be allowable as deduction u/s 80P(2)(a)(i) of the Act.

12. We note from the submissions of the ld. AR that the assessee has invested its fund in commercial bank as well as in co-operative banks and earned interest thereon. Section 80P(2)(d) describes that if the assessee has received interest from the co-operative society, then the assessee is eligible for claim of deduction on such interest received. In the judgment of Hon'ble Apex Court 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 (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/ 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 received from co-operative banks. We note that the assessee has also received interest from co-operative banks which is governed by the Banking Regulation Act of 1949 and this argument of the Id. DR has not been denied by the Id. AR of the assessee. The Section 80P(2)(d) describes that if the assessee has received interest/dividend from the co-operative society, then the assessee is eligible for claim of deduction on such interest/dividend, however we note that the assessee has received interest from co-operative bank but it is not clear whether the interest payer (co-operative bank) is a bank and registered with Reserve Bank of India and holding licence from RBI for carrying out banking business as per RBI Act. In addition, the judgment of Hon'ble Apex Court in the case of Kerala State Co-operative Agricultural and Rural Development Bank Ltd. KSCARDB vs. The Assessing Officer, Trivandrum & Ors. (supra) in which 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 received from co-operative banks, therefore this issue is also remitted back to the AO for verification of interest received from co-operative bank in above terms. If AO finds that the co-operative bank is carrying its banking business

activities in the light of the above judgment, the deduction u/s. 80P(2)(d) on such interest income should not be granted.

13. We further note that the assessee has received interest from other co-operative banks/commercial banks on its investments. The revenue authorities have considered the entire interest as income from other sources u/s. 56 including the interest received from co-operative bank 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 banks. 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 entire interest income from bank (co-operative bank and scheduled bank).

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

Pronounced in the open court on this 03rd day of July, 2024.

Sd/-
(KESHAV DUBEY)
JUDICIAL MEMBER

Sd/-
(LAXMI PRASAD SAHU)
ACCOUNTANT MEMBER

Bangalore,
Dated, the 03rd July, 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.