

**IN THE INCOME TAX APPELLATE TRIBUNAL
“D” BENCH, MUMBAI**

**BEFORE MS PADMAVATHY S, AM &
SHRI RAHUL CHAUDHARY, JM**

**I.T.A. No. 658/Mum/2024
(Assessment Year: 2017-18)**

Rameshwar Co-operative Bank Ltd. Prathamesh Horizone, Ground Floor, New MHB Colony, Borivali (W), Mumbai-400091. PAN : AAABR0114Q	Vs.	ACIT, Circle-1(3)(1) Aayakar Bhavan, M.K. Road, Mumbai-400020.
Assessee)	:	Respondent)

Assessee/Appellant by : Ms. Aarti Sathe & Ms. Aasavari
Kadam, CA

Revenue/Respondent by : Shri Nayanjyoti Nath, Sr. DR

Date of Hearing : 23.07.2024

Date of Pronouncement : 29.07.2024

ORDER

Per Padmavathy S, AM:

This appeal by the assessee is against the order of the Commissioner of Income Tax(Appeals) / National Faceless Appeal Centre, Delhi [for short 'the CIT(A)] dated 18.12.2023 for the AY 2017-18. The assessee has raised the following grounds of appeal:

“1. The learned Commissioner of Income Tax (Appeals), Income Tax Department, National Faceless Appeal Centre (NFAC) has erred in confirming the disallowance made by learned Assessing officer of a sum of Rs 45,00,736/- being 1/3 of the total interest paid on Saving and Fixed Deposits being of Rs 1,35,02,208/, treating it as related to investments made in "Held to Maturity"

securities without considering the fact the your petitioner is a Co-operative Bank engaged in the Banking Business and has to pay the interest on the saving deposits and various fixed deposit and these deposits are being used by the bank to provide loans to the parties.

2. The Learned Commissioner of Income Tax (Appeals) Income Tax Department, National Faceless Appeal Centre (NFAC) has ignored the fact that bank has earned interest on Loans and Advance of Rs 1,92,88,580/-, interest on Fixed Deposits with Mumbai District Central Co-operative Bank limited of Rs 14,44,574/-and interest on Government Securities of Rs 43,30,391.94 and has not been considered while upholding the order passed by the learned assessing officer. As per guide line of Reserve Bank of India, the bank has to compulsory to keep certain amount as investments in the government securities, which every bank in India has to follows. The Bank has earned interest income on these government securities including held to maturity securities of Rs 43,30,391.94 but the same was ignored while confirming the disallowance of the interest paid of Rs 45,00,736/-on the presumption that interest on deposits is on account HTM securities and treating it as part of the interest paid on deposits which are used in investing the same in Held To Maturity security, was uncalled for.”

2. The assessee is a co-operative Bank and carries on banking business under the banking license issued by Reserve Bank of India (RBI). The business of the assessee involves acceptance of various deposit from general public, providing banking facilities, providing loans and advances as per RBI Guidelines, and the main source of income to the assessee is interest received on loans and investments. The assessee filed the original return of income on 08.10.2017 for AY 2017-18 declaring total income of Rs. 47,70,350/-. The case was selected for scrutiny and the statutory notices were duly served on the assessee. During the course of assessment the AO noticed that the assessee has claimed a sum of Rs. 1,35,02,208/- as "interest on deposits and borrowings". The AO further noticed that the assessee having investments under three categories (i) Held to Maturity (HTM), (ii) Available for Sale (AFS) and (iii) Held for Trading (HFT). The AO

held that the investment in category of HTM is capital in nature and therefore the interest pertaining to such investment should be disallowed. Since the assessee did not furnish details pertaining to the interest component attributable to the investment in category of HTM, the AO proceeded to make disallowance of 1/3rd of the interest expenses i.e. Rs. 45,00,736/- (1/3rd of Rs. 1,35,02,208/-). Aggrieved the assessee preferred further appeal before the CIT(A). The assessee submitted before the CIT(A) that it is required to maintain the investments in these three categories as per the directive issued by the RBI which is binding in nature. The assessee further submitted that the income arising from the investment from HTM have been already offered to tax and that the AO is not correct in making adhoc disallowance. The CIT(A) however did not accept submission of the assessee and upheld the addition made by the AO.

3. The ld. AR submitted that as per the RBI mandate the assessee being in the banking business is required to maintain the investment in the above three categories. The ld. AR in this regard drew our attention to the relevant circular of the RBI (page 38 to 40 of PB). The ld. AR further submitted that the assessee being a co-operative bank is bound by the Circulars of the RBI and that in assessee's case the investment in category of HTM are in Government Securities specified by RBI. The ld. AR drew our attention to the financial statement of the assessee containing the various categories of investments and to substantiate that the income from all categories of investments including those from investment in category of HTM are offered to tax (page 1 & 2 of PB). The ld. AR submitted that the interest expense claimed by the assessee is towards various deposits taken from public and is incurred in the normal course of business. The ld. AR further submitted that the AO has asked the assessee to submit the mapping of interest

expenses to investment in category of HTM which is practically impossible since there cannot be a one to one match. The ld. AR also submitted that the disallowance made by the AO is adhoc in nature and that the AO has not made any adjustment to the income offered from HTM but has only disallowed the interest. Accordingly the ld. AR argued that the arbitrary disallowance of interest which the assessee has incurred in the normal course of business is not sustainable.

4. The ld. DR on the other hand argued that the assessee should have provided the breakup of interest and in the absence of such breakup the AO has correctly made the adhoc disallowance.

5. We heard the parties and perused the material on record. The assessee is a co-operative bank and holds a banking license issued by the RBI. The assessee as part of regular business of banking accepts deposit from public, provides banking facility and also provides loans and advances to general public. The assessee being a co-operative bank is governed by the Regulations of RBI and accordingly maintains investments under various categories. From the perusal of the financial statements, we notice that the assessee is holding investments in Government of India / State Securities to the tune of Rs. 6.89 crores and that these securities are classified as investment in category of HTM. We also notice that the assessee has earned interest of Rs. 43,30,391/- from Government Securities and is being part of income offered to tax. The contention of the revenue is that the investment in category of HTM are capital in nature and therefore the corresponding interest expenses needs to be disallowed and accordingly 1/3rd of the total interest expenditure claimed was disallowed. In this regard we notice that the AO has not brought anything on record on the basis of which the investment in category of

HTM are held as capital in nature. We also notice that the AO though has held that the investment in category of HTM as capital, has not made any adjustment to the income that is offered to tax from such investment but has disallowed only the interest expenditure which according to the AO is attributable to the said investment. We are unable to appreciate the action of the AO to disallow the proportionate interest expenditure whereas no relief is given for income earned from the impugned investments.

6. Further the interest claimed by an assessee gets disallowed under certain circumstances such as, where the assessee is earning tax free income out of borrowed funds, the assessee is giving interest free loans out of borrowed funds and that the interest expenses are not incurred in the regular course of business etc. We notice that the assessee is accepting various types of deposits from the general public and the funds so collected are kept in investments as per the RBI Guidelines which governs the assessee. We further notice that the assessee is earning income out of the various types of investments and claims the payment of interest is on the deposits and borrowings against such income. Therefore there is merit in the submission of the assessee that the payment of interest is incurred in the regular course of the business of the assessee i.e. banking business and that no disallowance is warranted unless the AO is able to establish otherwise.

7. The reason as quoted by the AO for making the adhoc disallowance is that the assessee was unable to provide the breakup of interest that is attributable to the various categories of investments. This in our considered view is not the right basis since in a banking business the funds collected from public through various modes are pooled and invested in various categories of investments as per the

applicable RBI Guidelines. Therefore, it is only fair to accept the contention that it may not be possible to map the funds/deposits collected from the general public to the investments unless there is a mandate that certain types of funds/deposits collected have to be kept in certain modes of investments. Accordingly in our considered view, making an adhoc disallowance of 1/3rd of interest expenditure merely for the reason that the assessee has not provided a one-to-one mapping without bringing any other adverse finding on record is not tenable. To summarise, we hold that the AO is not correct in making the adhoc disallowance without bringing anything on record to show that the interest expenditure is not incurred in the regular course of business, without proving that the income against which the interest is claimed is not offered to tax and for the mere reason that the assessee has not submitted the breakup of interest. In view of these discussions and considering the facts of the present case, we hold that the arbitrary disallowance made by the AO is not sustainable and liable to be deleted. We direct the AO accordingly.

8. In the result, the appeal of the assessee is allowed.

Order pronounced in the open court on 29-07-2024.

Sd/-
(RAHUL CHAUDHARY)
Judicial Member

**SK, Sr. PS*

Sd/-
(PADMAVATHY S)
Accountant Member

Copy of the Order forwarded to :

1. The Assessee
2. The Respondent
3. DR, ITAT, Mumbai
4. Guard File

5. CIT

BY ORDER,

(Dy./Asstt. Registrar)
ITAT, Mumbai