

**IN THE INCOME TAX APPELLATE TRIBUNAL
'A' BENCH : BANGALORE**

**BEFORE SMT. BEENA PILLAI, JUDICIAL MEMBER AND
SHRI WASEEM AHMED, ACCOUNTANT MEMBER**

ITA No. 1383/Bang/2024
Assessment Year: 2017-18

Karkal Taluk Agricultural Produce Marketing Society Ltd., D No.309, Karkala TAPCMS, Mangalore Road, Karkala, Udupi District. PAN – AAAAK 1129 K	Vs.	The Income Tax Officer, Ward – 3, Udupi. The NFAC, Delhi
APPELLANT		RESPONDENT

Assessee by	:	Shri Prasanna Shenoy, CA
Revenue by	:	Smt. Neha Sahay, JCIT

Date of hearing	:	27.08.2024
Date of Pronouncement	:	29.08.2024

ORDER

PER WASEEM AHMED, ACCOUNTANT MEMBER:

This is an appeal filed by the assessee against the order passed by the NFAC, Delhi dated 24/04/2024 vide DIN No. ITBA/NFAC/S/250/2024-25/1064315441(1) for the assessment year 2017-18.

2. The first issue raised by the assessee is that the Id. CIT(A) erred in not allowing the deduction on interest earned from the co-operative bank under the provisions of sec. 80P(2)(a)(i)/80(2)(d) of the Act.

3. Briefly stated facts are that the assessee in the present case is a society and filed the return of income declaring income at Rs. Nil after claiming the deduction u/s 80P(2)(a)(i) of the Act. The AO during the assessment proceedings found that the assessee has earned income on the money deposited with scheduled bank and co-operative bank amounting to Rs. 87,81,488/-, which was not eligible for deduction u/s 80P(2)(a)(i) /80P(2)(d) of the Act, therefore, the AO disallowed the same and added to the total income of the assessee.

4. Aggrieved, assessee preferred an appeal to the Id. CIT(A) who has allowed the ground of appeal of the assessee in part by observing as under:

"The basic facts in the case laws cited by the A.O. were availability of surplus funds which were invested in various instruments like FDs/MutualFunds/Securities etc to earn profit. In the instant case, the facts are different. The appellant submitted that funds were deposited as per requirement of Karnataka State Cooperative Rules 1960 which mandated 28% of total deposits collected to be kept with other Co-operative Banks and Co-operative Societies. The appellant claimed that it was not surplus funds which were kept to earn profit. I find merit in this contention of the appellant. Keeping deposits with SCDCC Bank, other Co-operative Banks and Co-operative Societies were part of the condition imposed by the statutory authority to conduct the appellant's business. Therefore the interest received from SCDCC Bank and other Co-operative Banks and Co-operative Societies cannot be construed as income from other sources and had to be considered as income from business activity under head profits and gains from business or profession and therefore is eligible for deduction u/s 80P(2)(a)(i). This argument further strengthened by the Hon'ble Supreme Court judgment in Nawanshahar Central Co-operative Bank Ltd [2007] 160 Taxman 48 (SC) wherein it was held that investment made by a banking concern as a statutory requirement is eligible for deduction u/s 80P. The same was also clarified by the CBDT circular No. 18/2015 dated 02.11.2015 in view of the Apex Court judgment. Considering these facts, the interest earned by the appellant as a part of statutory requirement continues to be income from business and therefore eligible for deduction u/s 80P(2)(a)(i). To that extent relief is allowed to the appellant. In case, the appellant had made investment in other than what was required under of Karnataka State Cooperative Rules 1960, the interest earned on such investment would be taxed under income from other sources u/s 56. Needless to say the appellant would get proportionate deduction on expenses to earn such interest income. Thus addition on interest earned to the extent of investment made in bank, other than statutory

requirement, reduced by proportionate expenses for earning such income is upheld and no deduction u/s 80P is allowed on such income. The issue of interest earned by the co-operative society from investment made in cooperative bank is thus partly allowed."

5. Being aggrieved by the order of the Id. CIT(A), the assessee is in appeal before us.

6. The Id. AR before us submitted that interest from cooperative bank is eligible for deduction as the money was deposited in the bank under the guidelines of Karnataka State Co-operative Rules 1960. Thus, such interest is eligible for deduction u/s 80P(2)(a)(i) of the Act.

7. On the other hand, the Id. DR contended that the Id. CIT(A) in his order has already allowed the deduction of the interest with respect to the deposits made with the co-operative bank under the guidelines of Karnataka State Co-operative Rules 1960. As such according to the Id. DR, there is no grievance to the assessee. The Id. DR vehemently supported the order of the authorities below.

8. We have heard the rival contentions of both the parties and perused the materials available on record. On perusal of the order of the Id. CIT(A), the relevant extract reproduced above, we note that the Id. CIT(A) has already granted relief to the assessee with respect of the deposits made with the co-operative bank under the guidelines of Karnataka State Co-operative Rules 1960. Furthermore, the Id. CIT(A) has also directed the AO to allow the expenditure u/s 57 of the Act against the interest income to be taxed u/s 56 of the Act. As such, we do not find any infirmity in the order of Id. CIT(A). Moreover, at the

time of hearing, the Id. AR has also not brought anything contrary in the finding of the Id. CIT(A).

8.1 Before parting, we are inclined to give direction to the AO that while calculating the amount eligible for deduction u/s 80P(2)(a)(i) of the Act, the principles laid down by the Hon'ble Supreme Court in the case of Kerala State Co-operative Agricultural and Rural Bank Ltd., Vs. ACIT reported in 154 taxmann.com 305 wherein it was observed that if the Co-operative Bank is not carrying out any banking business, then in our considered view, the deduction on account of interest on the investment made in such Co-operative Bank cannot be denied for the reason that such Co-operative Bank is not a bank. The Hon'ble Supreme Court in the case of Kerala State Co-operative Agricultural and Rural Bank Ltd., Vs. ACIT reported in 154 taxmann.com 305 observed that the assessee was a state-level agricultural and rural development bank and governed under the Kerala Co-operative Societies Act, 1969 as a co-operative society. The activity of the assessee was to provide credit facilities to its members. Accordingly, the assessee claimed a deduction under Section 80P(2)(a)(i) of the Act in the return of income. But the AO disallowed the same on the reasoning that the assessee was a cooperative bank and, therefore, it was hit by the provisions of section 80P(4) of the Act and thus would not be eligible for claiming deduction under section 80P(2) of the Act. Finally, the issue reached the Hon'ble Apex Court where it was held that banking is defined under section 5(b) of the Banking Regulation Act, 1949 to mean accepting, for the purpose of lending or investment, deposits of money from the public, repayable on demand or otherwise, and withdrawal by cheque, draft, order or otherwise. Therefore, a banking company must transact banking

business with the public. If a co-operative society would not transact the business of banking as defined in Section 5(b), it would not be a co-operative bank within the meaning of section 56 of Banking Regulation Act and would be entitled to the benefit of deduction under Section 80P(2) of the Act. Since, the assessee society was an apex co-operative society within the meaning of Kerala State Co-Operative Agricultural Development Banks Act, 1984 (State Act, 1984) whose primary object was to provide financial accommodation to its members who were all other co-operative societies and not members of the public, it was not a co-operative bank within the meaning of section 5(b) read with Section 56 of Banking Regulation Act. Accordingly, the deduction under Section 80P could not be denied to the assessee by invoking Section 80P(4) of the Act. In view of the above, we hold that if the Co-operative Bank is not functioning the business of banking as defined u/s 5(b) of Banking Regulation Act, then such Co-operative Bank shall be considered as Co-operative Society for the purpose of the deduction claimed u/s 80P(2)(d) of the Act. Therefore, in our considered view, such interest income will be eligible for deduction u/s 80P(2)(d) of the Act. However, if the Co-operative Bank is carrying out banking activities as defined u/s 5(b) of the Bank Regulation Act, then the assessee shall not be entitled for the deduction with respect to the interest earned on the investments made with such bank under the provisions of sec. 80P(2)(d) of the Act. Hence, the ground of appeal of the assessee is partly allowed.

9. **The next issue** raised by the assessee in ground No. 3 is that the Id. CIT(A) erred in disallowing the deduction of the expenditure of Rs. 33,52,411/- representing the provision made for the interest on the deposits.

10. The AO during the assessment proceedings found that the assessee is recording interest income on a cash basis whereas the interest expenses on deposits on the mercantile basis. According to the AO, the assessee was following hybrid system of accounting, which is not recognized under the provisions of Act. Accordingly, the AO worked out the provisions made by the assessee with respect to the interest expense on deposits created in the year under consideration amounting to Rs. 33,52,411/- only and disallowed the same by adding to the total income of the assessee.

11. On appeal, the Id. CIT(A) directed the AO to allow the enhanced deduction u/s 80P(2)(a)(i) of the Act while disallowing the provisions on account of interest expenses on the deposits of Rs. 33,52,411/- only. However, the Id. CIT(A) further observed that such provisions will have implication on the tax liability under MAT provisions, which is not taxed neutral. Accordingly, the Id. CIT(A) directed the AO to calculate the amount eligible for deduction u/s 80P(2)(a)(i) of the Act as per the provisions of law and compute the tax liability under the provisions of MAT under section 115JB of the Act afresh.

12. Being aggrieved by the order of the Id. CIT(A), the assessee is in appeal before us.

13. The Id. AR before us at the time of hearing has not pointed out any infirmity in the order passed by the Id. CIT(A), whereas the Id. DR vehemently supported the order of the authorities below.

14. We have heard the rival contentions of both the parties and perused the materials available on record. Admittedly, the disallowance made by the AO on account of the provisions made by the assessee for Rs. 33,52,411/- will enhance the deduction eligible to the assessee u/s 80P(2)(a)(i) of the Act. Therefore, we hold that such disallowance made by the AO is tax neutral. Thus, we hold that there is no infirmity in the direction of the Id. CIT(A). Regarding the direction of the Id. CIT(A) for calculation of tax under MAT, as per the provisions of law, we do not find any infirmity. Accordingly, the ground raised by the assessee is hereby dismissed.*

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

Order pronounced in court virtually on 29th day of August, 2024

Sd/-

(BEENA PILLAI)
Judicial Member
Bangalore
Dated, 29th August, 2024
/ vms /

Sd/-

(WASEEM AHMED)
Accountant Member

Copy to:

1. The Applicant
2. The Respondent
3. The CIT
4. The CIT(A)
5. The DR, ITAT, Bangalore.
6. Guard file

By order

Asst. Registrar, ITAT, Bangalore