

IN THE INCOME TAX APPELLATE TRIBUNAL
COCHIN BENCH, COCHIN

BEFORE SHRI SATBEER SINGH GODARA, JUDICIAL MEMBER
AND
SHRI AMARJIT SINGH, ACCOUNTANT MEMBER

ITA No.426/Coch/2023 - Asst.Year 2015-2016
ITA No.427/Coch/2023 - Asst.Year 2015-2016

Karassery Service Co-operative Bank Limited, Mukkam Kozhikode – 673 602. PAN AACAK0055A	vs.	The Income Tax Officer Ward 2(3) Kozhikode.
(Appellant)		(Respondent)

Appellant by : --- None---
Respondent by : Sri.Sanjit Kumar Das, CIT-DR

Date of Hearing : 13.08.2024	Date of Pronouncement : 06.11.2024
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ORDER

PER BENCH :

These twin assessee's appeals in ITA Nos.426/Coch/2023 and 427/Coch/2023 for assessment year 2015-2016 and 2017-2018, respectively arises out of the order of the CIT(A)-NFAC, Delhi, Delhi's DIN & Order No.ITBA/NFAC/S/250/2023-24/1052404554(1) and 1052956029(1) dated 27.04.2023 and 18.05.2023, in proceedings

u/s.143(3) of the Income-tax Act, 1961; in short “the Act” hereinafter, respectively.

Case called twice. None appears at assessee’s behest. It is accordingly proceeded *ex parte* against the assessee.

2. We now advert to the assessee’s “lead” appeal ITA.No.326/Coch./2023 for the former assessment year 2015-2016 wherein the learned CIT(A)-NFAC has partly upheld the Assessing Officer’s action disallowing its sec.80P deduction claim reading as under :

4.3. DECISION

4.3.1 The appellant is a Primary Agricultural Credit Society as registered and certified by the Cooperative Departments and registered under the Kerala Co-operative Societies Act, 1961 as noted by the AO. The AO has not questioned status of the appellant as a cooperative bank as against cooperative society nor has observed any violations of the Kerala Co-operative Society’s Act.

4.3.2 The AO denied the appellant’s claim of deduction u/s 80P on the grounds that the appellant has failed to satisfy the test of Mutuality. The AO made the observation that the appellant has got 4 types of member – Class A, B, C & D. The bye laws of the co-operative society’s clearly distinguish Class A members as real members with all the rights of dividend, vote and administration while Class B & D were merely nominal members who can take loans against security but do not have any rights. The AO submitted that the Cardinal requirement for mutuality is that the contributor to the common funds must be entitled to participate in the surplus and all the participators in the surplus must be contributors to the common fund.

The AO placed reliance on the decision of Hon’ble Supreme Court in the case of *The Citizen Co-operative Society Limited, Hyderabad vs ACIT, Circle-9(1), Hyderabad* in Civil Appeal No. 10245 of 2017 dated 8.8.2017 where it was held that ‘the Nominal members cannot be treated as members and should be treated as “Public at large”. The AO observed that 80% of the deposits were collected from nominal members who don’t have any rights on the profits of the business whereas all the rights and benefits are restricted to Class A members. Hence, the AO was of the opinion that there is absolutely no identity between the contributors towards

surpluses and participators in the surpluses.

4.3.3 Section 80P(2)(a)(i) clearly states that in the case of a co-operative society which is engaged in carrying on the business of **banking** or providing credit facilities to its members, the whole of the amount of "profits and gains of business" attributable to any one or more of such activities shall be allowed as deduction in computing the Total Income of the assessee.

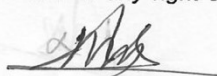
Section 80P(2)(a)(i) of the I.T Act recognizes two kinds of co-operative societies namely., (i) those carrying on the business of banking and (ii) those providing credit facilities to its members. It has been held by the **Apex Court in the case of Kerala State Co-operative Marketing Federation Ltd.**, that the correct way of reading the different heads of exemption enumerated in the section would be to treat each as a separate and distinct head of exemption. Whenever a question arises as to whether any particular category of an income of a co-operative society is exempt from tax what has to be seen is whether income fell within any of the several heads of exemption. If it fell within any one of the exemption, it would be free from tax notwithstanding that the conditions of another head of exemption are not satisfied and such income is not free from tax under that head of exemption.

4.3.4 The appellant has heavily relied upon the decision of the **Supreme Court in the case of Mavilayi Service Co-operative Bank, Calicut (2021) 431 ITR 1 (SC)**. On the issue of Principle of Mutuality and the definition of members, the Apex Court in para 46 held that

"46. It must also be mentioned here that unlike the Andhra Act that Citizen Cooperative Society Ltd. (supra) considered, 'nominal members' are 'members' as defined under the Kerala Act. This Court in U.P. Cooperative Cane Unions' Federation Ltd., Lucknow v. Commissioner of Income Tax, Lucknow-I (1997) 11 SCC 287 referred to section 80P of the IT Act and then held:

"8. The expression "members" is not defined in the Act. Since a cooperative society has to be established under the provisions of the law made by the State Legislature in that regard, the expression "members" in Section 80-P(2)(a)(i) must, therefore, be construed in the context of the provisions of the law enacted by the State Legislature under which the cooperative society claiming exemption has been formed. It is, therefore, necessary to construe the expression "members" in Section 80-P(2)(a)(i) of the Act in the light of the definition of that expression as contained in Section 2(n) of the Cooperative Societies Act. The said provision reads as under:

"2. (n) 'Member' means a person who joined in the application for registration of a society or a person admitted to membership after such registration in accordance with the provisions of this Act, the rules and the bye-laws for the time being in force but a reference to 'members' anywhere in this Act in connection with the possession or exercise of any right or power or



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the existence or discharge of any liability or duty shall not include reference to any class of members who by reason of the provisions of this Act do not possess such right or power or have no such liability or duty;”

Considering the definition of ‘member’ under the Kerala Act, loans given to such nominal members would qualify for the purpose of deduction under section 80P(2)(a)(i).”

4.3.5 It further held that once a co-operative society provides credit facilities to its members, the fact that it also provides credit facilities to non-members does not disentitle it from availing of the deduction. The Kerala Act expressly permits loans to non-members under section 59(2) and (3) and the stand taken by the SC in the case of **Mavilayi Service Co-operative Bank(supra)** held the issue in favour of the appellant. The court held as under:-

47. Further, unlike the facts in *Citizen Cooperative Society Ltd.*

(*supra*), the Kerala Act expressly permits loans to non-members under section 59(2) and (3), which reads as follows:

“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.” Thus, the giving of loans by a primary agricultural credit society to non-members is not illegal, unlike the facts in *Citizen Cooperative Society Ltd. (supra)*.”

Thus, while the giving of loans to non-members is not prohibited as per the Kerala Act, as noted in para 33 of the order, which is quoted earlier with respect to cooperative bank definition, the profit and gains from credit facilities given to non members cannot be said to attributable to the activity to providing credit faculties to its members and such amounts cannot be deducted u/s 80P. However, the court also held that

46. It must also be mentioned here that unlike the *Andhra Act* that *Citizen Cooperative Society Ltd. (supra)* considered, ‘nominal members’ are ‘members’ as defined under the *Kerala Act*”

4.3.6. Thus, associate members or nominal members cannot be held not to be


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members under the Kerala Act. The AO has not made any observation in this respect, as to the business with non-members and only dealt with difference classes of members, stating that class 'A' are the real members. In this respect, the appellant states that there is no activity with non-members. The judgement of Citizen Co-operative Society is not applicable to appellant is doing business only with its members which include nominal members (B, C & D Class Members). The depositors and borrowers are all members of the society and as such there is no violation of any section of the Kerala Co-Operatives Registration Act and its Rules. The Society is not transacting with any outsider. As against this, Citizen Co-Operative Society transacted with outsiders, i.e., with non-members. Further, as held by the Apex court in the Mavilayi case (quoted supra), nominal members are also members as per the definition under Kerala Act. There is thus, no violation of principle of Mutuality by the appellant. Hence, the AO is directed to **allow the deduction u/s 80P, subject to the underneath directions.**

4.3.7 Section 80P(2)(d) of the Act specifically exempts interest earned from funds invested in co-operative societies. For the AY 2015-16 the AO observed that the appellant Society has invested in different societies in the form of fixed deposits, shares etc and interest has been earned on such investment. The AO observed the following investment and deposits done by the appellant in other societies :

Details of Investment	Closing Balance as on 31.03.2015 (Rs.)
Shares and Investments/FD IN KDC, KODENCHERY	1,00,00,000
Shares and Investments/FD IN KDC, KUNNAMANGALAM	3,15,00,000
Shares and Investments/FD IN KDC EVENING	70,00,000
Shares and Investments/FD IN KDC, MAIN branch	3,50,00,000
Shares and Investments/FD IN KDB MUKKAM	29,50,00,000
Shares and Investments/FD IN Treasury	2,50,00,000
Shares and Investments/FD IN OTHER INSTI	12,42,48,500



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Shares and Investments/SHARE OTHER	5,00,000
TOTAL	52,82,48,500

4.3.8. In other years under appeal of A.Y. 2007-08, 2012-13, the appellant raised an additional ground of allowing exemption for interest income on deposits. While the appellant technically did not raise the additional grounds of appeal related to interest income received from other co-operative societies in the year under consideration, the power of CIT(A) to decide on issues that arise because of the appeal is clear from the Explanation to section 251 which states as under:

"In disposing of an appeal, the Commissioner (Appeals) may consider and decide any matter arising out of the proceedings in which the order appealed against was passed, notwithstanding that such matter was not raised before the Commissioner (Appeals) by the appellant."

4.3.9. In the current year, it is not clear whether the appellant received interest income from deposits or dividend from shares. What is available is a list of entities in which investments in shares or FDs is done. In this context, the Hon'ble Supreme Court again case of Mavilayi (quoted supra) has made a distinction between cooperative bank and cooperative society as under in para 45 :-

"...Further, section 80P(4) is to be read as a proviso, which proviso now specifically excludes co-operative banks which are co-operative societies engaged in banking business i.e. engaged in lending money to members of the public, which have a license in this behalf from the RBI. Judged by this touchstone, it is clear that the impugned Full Bench judgment is wholly incorrect in its reading of Citizen Cooperative Society Ltd. (supra)...."

Thus, the judgement in Mavilayi Service Cooperative Bank is about making a distinction between cooperative credit societies and cooperative banks. When cooperative banks are treated as a distinct species from cooperative credit societies, the question comes as to whether these can still be treated as cooperative societies in context of section 80P(2)(d) and interest earned from them be exempt.

4.3.10. There are a plethora of judgments on this aspect. However, the last judicial decision of HC as available with this appellate authority is the judgement in case of Principal Commissioner of Income-tax, Hubballi v. Totagars Co-operative Sale Society [2017] 83 taxmann.com 140, in which the court held as under:-

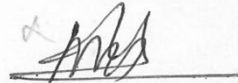

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"hence, the income by way of interest earned by deposit or investment of idle or surplus funds does not change its character irrespective of the fact whether such income of interest is earned from a schedule bank or a co-operative bank and thus, clause (d) of Section 80P(2) of the Act would not apply in the facts and circumstances of the present case. The person or body corporate from which such interest income is received will not change its character, viz. interest income not arising from its business operations, which made it ineligible for deduction under Section 80P of the Act, as held by the Hon'ble Supreme Court."

4.3.11. The judgement referred to by the Honourable HC in the above context is the judgement of the Apex Court in case of the same appellant Totgars Co-operative Sale Society Ltd. vs. Income-tax Officer (SC) (2010) 188 Taxman 282 wherein the Apex Court held that interest income from deposits with banks cannot be held to income from business for the appellant and is not eligible for deduction u/s 80P(2)(a)(iv). The Apex Court upheld the decision to bring to tax the interest income from bank deposits as income from other sources u/s 56. Relying on the same, the Karnataka HC has held that interest from cooperative banks too being not interest income from the business of the appellant is not eligible for deduction u/s 80P(2)(d) too. In the current case too, the appellant being a credit society engaged in business of accepting deposits and lending loans to all its members, did not earn the interest income from the interest paid by the members, but earned the same on deposits with the cooperative banks. Thus, it is not interest from business and it is not interest from other cooperative societies and therefore, the same is held as not eligible for deduction u/s 80P.

4.3.12 Thus, while the appellant is not a cooperative bank hit by the provisions of section 80P(2)(d) and is eligible for deduction u/s 80P(2)(a)(iv) of the IT Act, the specific income of interest from Kozhikode District cooperative bank is not income from its business nor income from cooperative societies and therefore, not eligible for deduction u/s 80P(2)(d). Therefore, the AO is directed to bring this interest income of Rs. 1,37,07,869/- to tax. However, section 80P(2)(d) of the Act specifically exempts interest earned from funds invested in co-operative societies. Therefore, to the extent of the interest earned from investments made by the appellant with any co-operative society, it is entitled to deduction of the whole of such income under section 80P(2)(d) of the Act.

4.3.13. Therefore, the AO is required to verify the details of other income received not from business of the appellant – with its members but from **investment of surplus whether in shares or FDs**, and bring the same to tax except those earned from cooperative societies (cooperative banks not being included in cooperative societies) and the deduction allowable to the appellant under **section 80P to the extent of such income is restricted.**



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4.3.14. Further, the appellant has shown Rs. **15,22,603/- as dividend** received as verified in its ROI. Such income is also not income from the business of the appellant, ie from activities of credit facilities to members. This is also not eligible for deduction u/s 80P as it is in nature of income from other sources under section 56. However, appellant has shown the same as profit from business and not income from other sources in the ROI. This amount is to be brought to tax as IFOS, **not eligible for deduction u/s 80P.**

6. In result, the appeal of the appellant is **Partly Allowed.**

3. Suffice to say, the Revenue's first and foremost vehement contention is that the assessee has not derived its interest income from regular members only and therefore, the same is not allowable for the deduction herein in light of Citizen Co-operative Society Ltd vs. CIT (2017) 84 taxmann.com 114 (SC).

4. Learned DR could hardly dispute the clinching fact that their lordships' recent landmark decision in Mavilayi Service Co-operative Bank Ltd., vs. CIT [2021] 431 ITR 1 (SC) has settled the issue in assessee's favour and against the department that such a distinction *qua* the category of members is not permissible once the same

confirms to the relevant State Government Cooperative law; norms.

5. The Revenue's next vehement arguments in light of The Totagars Cooperative Sales Society vs. ITO [2010] 322 ITR 283 (SC) that assessee's interest income derived from deposits in cooperative banks herein is not eligible for the impugned deduction. We notice in this factual backdrop that the hon'ble jurisdictional high court in its recent judgment in PCIT v. Peroorkada Service Co-op. Bank Ltd. [2022] 442 ITR 141 (Ker) has already accepted the assessee's contentions as under : -

"12.2. Section 80P deals with Co-operative Societies' computation of income. As already noted, it has four sections and several sub-sections and clauses. The Parliament has considered the various situations in which the exigible income and the deductible income of the assessee is considered while computing the income of the assessee. For getting deduction, in our considered view, the assessee must also establish that

the interest income earned by the assessee is from a Co-operative Society. As a matter of fact, in the case on hand, there is no dispute that it is not from a Co-operative Society registered under Kerala Co-operative Societies Act. The interest income earned from District Co-operative Bank/State Co-operative Bank, in the facts and circumstances of the case, do come within Section 80P(2)(d). Therefore, the income constitutes income from other sources and the only eligible deduction is covered by Section 80P(2)(d) viz. Interest or dividend derived by the assessee from its investments with any other Co-operative Society. The source of interest income is from Bank and Treasury, interest income received from Treasury be included in the computation of total income of the assessee. In other words, interest earned from Treasury is inadmissible for deduction and interest income from Co-operative Societies registered under the Kerala Co-operative Societies Act are eligible for deduction. The contra consideration of Commissioner of Income Tax (Appeals)

and the Tribunal is incorrect and liable to be modified as stated above. Hence, it is held that the interest income earned by the assessee does not come within the ambit of Section 80P(2)(a)(i) and permissible deduction of interest income is limited to Co-operative Societies/Banks registered under Kerala Co-operative Societies Act under clause (d) of the Act and effect order on the above lines is made by the Assessing Officer. The questions are accordingly answered.”

6. We accordingly accept the assessee's sole substantive grievance as well as the “lead” appeal ITA.No.426/Coch./2023 in very terms and leave it open for the learned to Assessing Officer to frame his consequential computation as per law after examining all the relevant facts. Ordered accordingly.

7. Same order to follow in assessee's latter appeal ITA.No.427/Coch./2023 since raising identical sole substantive grounds.

8. These assessee's twin appeals ITA.Nos.426 and 427/Coch./2023 are allowed in above terms. A copy of this common order be placed in the respective case files.

Order pronounced in the open court on this 06th day of November, 2024.

Sd/-
(AMARJIT SINGH)
ACCOUNTANT MEMBER

Sd/-
(SATBEER SINGH GODARA)
JUDICIAL MEMBER

Cochin ; Dated 06th November, 2024.

VBP/-

Copy to :

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2. The Respondent.
3. The CIT(A), Concerned.
4. The CIT Concerned.
5. The DR, ITAT, Cochin.
6. Guard File.

Asst.Registrar/ITAT, Cochin