

IN THE HIGH COURT OF KARNATAKA AT BENGALURU

DATED THIS THE 14TH DAY OF DECEMBER, 2021

PRESENT

THE HON'BLE MRS. JUSTICE S.SUJATHA

AND

THE HON'BLE MR. JUSTICE S.VISHWAJITH SHETTY

I.T.A.No.393/2016

BETWEEN:

1. The Pr. Commissioner of Income-tax, CIT(A)
C.R.Building,
Attavara,
Mangaluru-575 001.
2. The Asst. Commissioner of Income-tax,
Circle-2(1),
C.R.building,
Attavara,
Mangaluru-575 001.

... APPELLANTS

(By Sri K.V.Aravind, Adv.)

AND:

M/s. South Canara District,
Central Co-operative Bank Ltd.,
Sadashiva Sahakara Sadana,
K.S.Rao Road,
Mangaluru-575 002.
PAN: AABAT6621N

... RESPONDENT

**(By Sri A.Shankar, Senior Counsel for
Sri Bhairav Kuttaiah, Adv.)**

This ITA is filed under Section 260-A of the Income Tax Act praying to set aside the orders passed by the ITAT, Bengaluru in ITA No.1195/Bang/2015 dated 09.03.2016 confirming the order of the Appellate Commissioner and confirm the order passed by the Asst. Commissioner of Income Tax, Circle-2(1), Mangaluru.

This appeal coming on for Final Hearing, this day, **S.Sujatha J.**, delivered the following:

JUDGMENT

1. This appeal is filed by the revenue under Section 260A of the Income Tax Act, 1961 (for short, 'the Act'), challenging the order dated 09.03.2016 in ITA No.1195/Bang/2015 passed by the Income Tax Appellate Tribunal (for short, 'the Tribunal'), relating to the assessment year 2012-13, whereby the order of the Appellate Commissioner has been confirmed.

2. Though the appeal was admitted to consider the substantial question of law no.3 raised in the appeal, having heard the learned Counsel for the parties, we find it appropriate to admit all the substantial questions of law raised by the revenue, which reads as under:

"1. Whether on the facts and in the circumstances of the case, the Tribunal is right in law in holding that

the assessee can compute its income chargeable under the head business and profession under hybrid system of accounting when Sec.145 of the Act does not allow the assessee to follow such system of accounting and by ignoring the ratio given by the Hon'ble Supreme Court in the case of Thiagaraja Chetty vs. CIT (1953) reported in 24 ITR page 525 and Moorvi Industries Vs. CIT (1971) reported in 82 ITR page 835 wherein it was held that the income accrues, when it falls due and legally recoverable, irrespective of whether it is actually received or not, further failed to consider the law laid down by Hon'ble Supreme Court in the case of State of Travancore vs. CIT (1996) reported in 24 Tax-man page 337, wherein it was held that the concept of reality of the income and the actuality of the situation are relevant factors which go to the making up of accrual of income, but once accrual takes place and income accrues, the same cannot be defeated by any theory of real income?

2. Whether on the facts and in the circumstances of the case, the Tribunal is right in law in holding that the interest accrued on investments is not chargeable to tax when it is following unrecognized hybrid system of accounting?

3. Whether on the facts and in the circumstances of the case, the Tribunal is right in law in coming to the

conclusion that the expenditure which has no direct nexus, incurred by an independent charitable trust is allowable as expenditure of the assessee bank, when the income of the trust itself is exempted from taxation?

4. Whether on the facts and in the circumstances of the case, the Tribunal is right in law in holding that the amortization premium paid for acquisition of Government securities held as long term investment that are in the nature of capital investment is allowable as revenue expenditure?

3. Re: substantial question of law nos.1 & 2:-

The issues involved herein are no more res integra in view of the ruling of the coordinate bench of this Court in the case of **COMMISSIONER OF INCOME TAX VS CANFIN HOMES LTD.** - (2012) 347 ITR 382, whereby identical questions have been considered and answered in favour of the assessee and against the revenue. It has been categorically observed that the contention of the revenue that in respect of non-performing assets even though it does not yield any income as the assessee has adopted mercantile system of accounting, he has to pay tax on the revenue which has accrued notionally is without any basis. Therefore, substantial

questions of law nos.1 & 2 requires to be answered in favour of the assessee and against the revenue. This view is also fortified in the other coordinate bench decision in the case of the **COMMISSIONER OF INCOME TAX VS M/S. DAVANGERE DISTRICT CENTRAL CO-OPERATIVE BANK LIMITED** in ITA No.137/2015 disposed of on 13.11.2020 and in the case of Commissioner of **INCOME TAX VS VASISTH CHAY VYAAR LIMITED - (2011)196 TAXMAN 169**, which has been confirmed by the Hon'ble Supreme Court in the case of **COMMISSIONER OF INCOME TAX VS VASISTH CHAY VYAAR LIMITED - (2018)90 taxmann.com 365**.

4. Re: substantial question of law no.3:-

The Assessing Officer has recorded a finding that the assessee has incurred the expenditure made towards M/s. Navodaya Grama Vikasa Charitable Trust with a description NGVCT Animator salary as per the directions of their controlling authority i.e., NABARD. Under the provisions of the Act, no exception could be allowed unless the same has been incurred by the assessee for earning taxable income and it should be in the nature of revenue. Having observed so, denied the exception claimed by the assessee for the reason

that the same has no relevance to the taxable income and the same having been incurred as per the directions of the controlling authority.

5. In the appeal before the CIT (Appeals), it has been held that the said exception though made on account of the directive from NABARD, there is also commercial exigency. It has also recorded that there was sufficient mobilization of loans and advances and deposits directly relatable to the said expenditure has been established by the assessee. There being relatable deposits to the loans and advances, the objective being laudable, allowed the appeal filed by the assessee deleting the addition made by the Assessing Officer. On appeal preferred by the revenue before the Tribunal, the order of the Commissioner of Income Tax (Appeals) has been confirmed dismissing the appeal.

6. On extensive analysis of the factual aspects, the Tribunal has arrived at a conclusion that though the assessee is promoting the formation of self help groups in the Districts of Dakshina Kannada and Udupi, and the loans are given to such self help groups for home industries like candle making,

soap making and such other activities, the income generated by such self help groups come back to the assessee as deposits. The commercial exigency being established under the provisions of Section 37(1) of the Act, the same has been considered in the light of the judgment of the Hon'ble Rajasthan High Court in **RAJASTHAN SPINNING AND WEAVING MILLS LTD. - 274 ITR 465**, which has been rendered following the decision of the Hon'ble Apex Court in the case of **SASOON J. DAVID & CO. P. LTD. VS CIT - 118 ITR 261 (SC)**. Having regard to the legally settled principles with reference to the expression 'wholly or exclusively' used in Section 37(1) of the Act, the Tribunal has dismissed the appeal filed by the revenue. We find it appropriate to quote the relevant paragraph of the said decision, which reads as under:

"20. It has to be observed here that the expression "wholly and exclusively" used in section 10(2)(xv) of the Act does not mean 'necessarily'. Ordinarily it is for the assessee to decide whether any expenditure should be incurred in the course of his or its business. Such expenditure may be incurred voluntarily and without any necessity and if it is incurred for promoting the business and to earn profits, the

assessee can claim deduction under section 10(2) (xv) of the Act even though there was no compelling necessity to incur such expenditure. It is relevant to refer at this stage to the legislative history of section 37 of the Income-tax Act, 1961 which corresponds to section 10(2) (xv) of the Act. An attempt was made in the Income-tax Bill of 1961 to lay down the 'necessity' of the expenditure as a condition for claiming deduction under section 37. Section 37(1) in the Bill read "any expenditure laid out or expended wholly, necessarily and exclusively for the purposes of the business or profession shall be allowed" The introduction of the word 'necessarily' in the above section resulted in public protest. Consequently when section 37 was finally enacted into law, the word 'necessarily' came to be dropped. The fact that somebody other than the assessee is also benefited by the expenditure should not come in the way of an expenditure being allowed by way of deduction under section 10(2) (xv) of the Act if it satisfies otherwise the tests laid down by law. This view is in accord with the following observations made by this Court in CIT v. Chandulal Keshavlal & Co. [1960] 3 SCR 38 at page 48:"

7. In the light of the said decision, the expenses incurred by the assessee cannot be held to be not allowable expenses under Section 37 of the Act. The CIT (Appeals) as well as the Tribunal has analyzed the factual aspects in the background of the legal principles, which by any stretch of imagination cannot be held to be perverse or arbitrary. More over, these factual aspects recorded by the fact finding authorities cannot be interfered. Accordingly, the substantial question of law no.3 is answered in favour of the assessee and against the revenue.

8. Re: substantial questions of law no.4:-

It is not in dispute that these substantial question of law raised by the revenue are squarely covered by the ruling of the coordinate bench decision of this Court in the case of **COMMISSIONER OF INCOME-TAX, HUBLI VS KARNATAKA VIKAS GRAMEEN BANK - (2017)79 taxmann.com 359** and in the case of **COMMISSONER OF INCOME TAX, BANGALORE VS ING VYSYA BANK LTD. - (2020)114 taxmann.com 506**, wherein the substantial question of law being answered in favour of the assessee and against the revenue. Hence, we answer substantial question

of law no.4 in favour of the assessee and against the revenue.

Resultantly, the appeal stands dismissed.

**Sd/-
JUDGE**

**Sd/-
JUDGE**

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