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PERADY VYAVASAYA SEVA SAHAKARI BANK LTD. vs. INCOME TAX OFFICER

IN THE ITAT BANGALORE BENCH 'A'

N. V. VASUDEVAN, VP & B. R. BASKARAN, AM.

ITA No. 1451/Bang/2019

Aug 6, 2021

(2021) 62 CCH 0383 BangTrib

Legislation Referred to

Section 80P

Case pertains to

Asst. Year 2016-17

Decision in favour of:

Matter remanded

Deductions—Deduction in respect of income of cooperative society— Assessee is a primary agricultural co-operative society engaged in business of acceptance of deposits from lenders, lending loans, providing banking facility in rural village — Assessee filed return of income under section 80P — Assessee society earned interest and dividend on investment in Bank — Assessee claimed deduction u/s. 80P(2)(d) on interest and dividend — With regard to remaining sum assessee claimed deduction u/s.80P(2)(a)(i) — AO denied benefit of deduction under section 80P(2)(d) and 80P(2)(a)(i) to assessee — CIT(A) confirmed order of AO — Held, claim of Assessee was that Co-operative Bank is essentially a Co-operative Society and therefore deduction has to be allowed under Clause (d) of Sec.80P(2) — Karnataka High Court followed decision of supreme Court in PCIT Vs. Totgars Co-operative Sale Society Ltd. 395 ITR 611 (Karn.) and held that interest earned from Schedule bank or co-operative bank is assessable under head income from other sources and therefore provisions of Sec.80P(2)(d) was not applicable to such interest income — It is thus clear that source of funds out of which investments were made remained same in AY 2007-08 to 2011-12 and in AY 1991-92 to 1999-2000 decided by Supreme Court — Therefore whether source of funds were Assessee's own funds or out of liability was not subject matter of

decision of Karnataka High Court in decision cited by DR — To this extent decision of Karnataka High Court in case of Tumkur Merchants Souharda Credit Co-operative Society Ltd. Vs. ITO still holds good — Hence, on this aspect, issue should be restored back to AO for a fresh decision after examining facts in light of these judgment of Apex Court rendered in case of Totgars Co-operative Sale Society Ltd. (supra) and of Karnataka high Court rendered in case of Tumukur Merchnts Souharda Co-operative Ltd. (supra — AO will afford opportunity of being heard to Assessee and filing appropriate evidence, if desired, by Assessee to substantiate its case, before deciding issue in set aside proceedings — Matter remanded.

Held

Claim of Assessee was that Co-operative Bank is essentially a Co-operative Society and therefore deduction has to be allowed under Clause (d) of Sec.80P(2).Karnataka High Court followed the decision of the supreme Court in PCIT Vs. Totgars Co-operative Sale Society Ltd. 395 ITR 611 (Karn.) and held that interest earned from Schedule bank or co-operative bank is assessable under the head income from other sources and therefore the provisions of Sec.80P(2)(d) was not applicable to such interest income. It is thus clear that the source of funds out of which investments were made remained the same in AY 2007-08 to 2011-12 and in AY 1991-92 to 1999-2000 decided by the Supreme Court. Therefore whether the source of funds were Assessee's own funds or out of liability was not subject matter of the decision of the Karnataka High Court in the decision cited by the DR. To this extent the decision of the Karnataka High Court in the case of Tumkur Merchants Souharda Credit Co-operative Society Ltd. Vs. ITO still holds good. Hence, on this aspect, the issue should be restored back to the AO for a fresh decision after examining the facts in the light of these judgment of the Apex Court rendered in the case of The Totgars Co-operative Sale Society Ltd. (supra) and of Karnataka high Court rendered in the case of Tumukur Merchnts Souharda Co-operative Ltd. (supra).

(para 10)

AO will afford opportunity of being heard to the Assessee and filing appropriate evidence, if desired, by the Assessee to substantiate its case, before deciding the issue in the set aside proceedings.

(para 12)

PCIT Vs. Totgars Co-operative Sale Society Ltd. 395 ITR 611 (Karn.), Tumkur Merchants Souharda Credit Co-operative Society Ltd. Vs. ITO referred.

Conclusion

Interest earned from Schedule bank or co-operative bank is assessable under head income from other sources and therefore provisions of Sec.80P(2)(d) was not applicable to such interest income.

In favour of

Matter remanded

Cases Referred to

Togar's Co-operative Sales Society Ltd. Vs. ITO 322 ITR 283(SC)

Tumkur Merchants Souharda Credit Co-operative Society Ltd. Vs. ITO 230 taxman 309 (Karn)

PCIT Vs. Totgars Co-operative Sale Society Ltd. 395 ITR 611 (Karn.)

Counsel appeared:

Sheethal R. Borkar, Advocate for the Appellant.: Kannan Narayanan for the Respondent

N. V. VASUDEVAN, VP.

1. This is an appeal by the assessee against the order dated 27.03.2019 of CIT(A), Mangaluru, relating to Assessment Year 2016-17.

2. The assessee is a primary agricultural co-operative society engaged in the business of acceptance of deposits from lenders, lending loans, providing banking facility in rural village. The assessee filed return of income for the relevant AY declaring nil income after claiming deduction of Rs.1,04,78,572/- under section 80P of the Income Tax Act, 1961 (Act).

3. During the relevant previous year, the assessee society earned Rs. 36,86,567/- as interest and Rs.4,05,009/- as dividend on investment in South Canara District Co-op. Bank. The assessee claimed deduction u/s. 80P(2)(d) of the Act on the interest and dividend earned through investments in South Canara District Co-op. Bank. With regard to the remaining sum of Rs.63,87,940/- (Rs.1,04,79,516 - Rs.40,91,576), the assessee claimed deduction u/s.80P(2)(a)(i) of the Act. According to the assessee, it was engaged in the business of providing credit facilities to its members, the whole of the amount of profits and gains of business attributable to such activities is deductible under section 80P(2)(a)(i) of the Act being profits attributable to the activity of providing credit facilities to its members.

4. As far as deduction u/s. 80P(2)(a)(i) is concerned, the AO was of the view that as per the bye-laws of the society nominal members and associated members were also eligible for becoming members of the assessee, besides regular members. The AO was of the view that nominal and associate members of the Assessee did not having voting rights and were not entitled to participate in the profits of the society. In the aforesaid circumstances, the AO was of the view that income in question did not satisfy the requirements of principles of mutuality laid down by the Hon'ble Supreme Court in the case of Citizen C-operative Society Ltd. v. ACIT [2017] 86 taxmann.com 114 (SC). The AO therefore denied the deduction u/s. 80P(2)(a)(i) of the Act. As far as deduction u/s. 80P(2)(d) is concerned, the AO was of the view that the interest income earned by the assessee was to be regarded as income from other sources and therefore deduction cannot be allowed as it was not in the nature of business income. In doing so, he relied upon the decision of the Hon'ble High Court of Karnataka in the case of Totgars Co-operative Sales Society, 83 taxman.com 140 (Kar) wherein reliance was placed by the Hon'ble Court on the decision of the Hon'ble Supreme Court in the case of The Togar's Co-operative Sales Society Ltd. Vs. ITO 322 ITR 283(SC) wherein the Hon'ble Supreme Court held that the benefit of deduction u/s.80P(2)(a)(i) of the Act is only on income which is assessable under the head income from business. Interest earned on Investment of surplus funds not immediately required in short term deposits and securities by a co-operative society providing credit facilities to members or marketing agricultural produce to members is not business income but income from other sources and the society is not entitled to special deduction.

5. Following the aforesaid decisions, the AO denied the benefit of deduction under section 80P(2)(d) and 80P(2)(a)(i) of the Act to the assessee. The CIT(A) confirmed the order of the AO.
6. Aggrieved by the order of the CIT(A), the assessee is in appeal before the Tribunal.
7. On the issue of deduction u/s.80P(2)(a)(i) of the Act, the learned Counsel for the assessee filed before us a decision of the Hon'ble ITAT, Bengaluru Bench in the case of Puttur Primary Co-operative Agriculture and Rural Development Bank Ltd., Vs. ITO in ITA No.1449/Bang/2019, order dated 14.06.2021 for Assessment Year 2016-17. According to the learned Counsel for the assessee, the Tribunal has decided identical issue that arises for consideration in this appeal and has remanded the issue for consideration with the following observation:

"4. We heard Ld D.R and perused the record. The first issue relates to the claim of deduction u/s 80P(2)(a)(i) of the Act. We notice that an identical issue has been considered by the co-ordinate bench in the case of Karkala Co-op S Bank Ltd (supra), wherein an identical issue has been restored to the file of AO for examining it afresh. For the sake of convenience, we extract below the relevant observations made by the co-ordinate bench:-

"4. The Ld. A.R. submitted that the law on deduction of 80P(2)(a)(i) of the Act available to credit co-operative societies has since been settled by Hon'ble Supreme Court in the case of Mavilayi Service Co-operative Bank Ltd. Vs.CIT (2021) 123 taxmann.com 161 (SC). He submitted that the Hon'ble Supreme Court has held that the expression "Members" is not defined in the Income-tax Act. Hence, it is necessary to construe the expression "Members" in section 80P(2)(a)(i) of the Act in the light of definition of that expression as contained in the concerned co-operative societies Act. The Ld. A.R. submitted that the Hon'ble Supreme Court has considered the decision rendered by it in the case of Citizen Co-operative Society Ltd. (supra) and observed that the ratio decidendi of Citizen Co-operative Society Ltd. must be given effect to. Accordingly, he submitted that the assessee should be allowed deduction u/s 80P(2)(a)(i) of the Act.

5. The Ld. D.R., on the contrary, submitted that the issue of deduction needs to be examined afresh in the light of decision rendered by Hon'ble Supreme Court in the case of Mavilayi Service Co-operative Bank Ltd. (supra). Accordingly, he submitted that this issue may be restored to the file of the A.O.

6. We heard the parties on this issue and perused the record. We find merit in the submission made by Ld. D.R. Since the Hon'ble Supreme Court has settled many issues in the decision rendered by it in the case of Mavilayi Service Co-operative Bank Ltd. (supra) and since the facts prevailing in the instant case needs to be examined afresh in the light of the principles enunciated by Hon'ble Supreme Court in the above said case, we are of the view that the issue of deduction u/s 80P(2)(a)(i) of the Act requires fresh examination at the end of the A.O. Accordingly, we set aside the order passed by Ld. CIT(A) on this issue in both the years under consideration and restore them to the file of the A. O. in both the years for examining it afresh as discussed above."

5. Since the facts are identical, following the decision rendered by the co-ordinate bench, we restore this issue to the file of the AO with similar directions.

8. The learned DR relied on the order of the CIT(A). We have considered the rival submissions. As the issues involved in the present appeal are identical to the issues decided by the Tribunal cited by the learned Counsel for the assessee, we restore the issue to the AO to examine the claim of the assessee afresh as directed by the Tribunal in the aforesaid order.

9. As far as the deduction u/s.80P(2)(d) of the Act is concerned, the learned AR relied on the decision of the Hon'ble Karnataka High Court in the case of Tumkur Merchants Souharda Credit Co-operative Society Ltd. Vs. ITO 230 taxman 309 (Karn) wherein the Hon'ble Karnataka High Court considered the decision of the Hon'ble Apex Court in the case of The Totgar's Co-operative Sales Society (supra) and held that interest income in respect of temporary parking of own surplus funds not immediately required is eligible for deduction u/s.80P(2)(a)(i) of the Act. The learned DR relied on a subsequent decision of the Hon'ble Karnataka High Court in the case of PCIT Vs. Totgars Co-operative Sale Society Ltd. 395 ITR 611 (Karn.) wherein it was held that interest income had to be assessed under the head income from other sources and hence not entitled to deduction u/s.80P of the Act.

10. We have carefully gone through the judgment relied by the learned DR. The facts of the case before the Hon'ble Karnataka High Court in the decision cited by the learned DR was that the Hon'ble Court was considering a case relating to Assessment Years 2007-2008 to 2011- 2012. In case decided by the Hon'ble Supreme Court in the case of the very same Assessee, the Assessment years involved was AY 1991-92 to 1999-2000. The nature of interest income for all the AYs was identical. The bone of contention of the Assessee in AY 2007-08 to 2011-12 was that the deduction under Section 80P(2) of the Act is claimed by the respondent assessee under Section 80P(2)(d) of the Act and not under Section 80P(2)(a) of the Act which was the claim in AY 1991-92 to 1999-2000. The reason given by the Assessee was that in AY 2007-08 to 2011-12 investments and deposits after the Supreme Court's decision against the assessee Totgar's Co-operative Sale Society Ltd. (supra), were shifted from Schedule Banks to Co-operative Bank. U/s.80P(2)(d) of the Act, income by way of interest or dividends derived by a Co-operative Society from its investments with any other Co-operative Society is entitled to deduction of the whole of such interest or dividend income. The claim of the Assessee was that Co-operative Bank is essentially a Co-operative Society and therefore deduction has to be allowed under Clause (d) of Sec.80P(2) of the Act. The Hon'ble Karnataka High Court followed the decision of the supreme Court in The Totgars Co-operative Sales Society Ltd. (supra) and held that interest earned from Schedule bank or co-operative bank is assessable under the head income from other sources and therefore the provisions of Sec.80P(2)(d)of the Act was not applicable to such interest income. It is thus clear that the source of funds out of which investments were made remained the same in AY 2007-08 to 2011-12 and in AY 1991-92 to 1999-2000 decided by the Hon'ble Supreme Court. Therefore whether the source of funds were Assessee's own funds or out of liability was not subject matter of the decision of the Hon'ble Karnataka High Court in the decision cited by the learned DR. To this extent the decision of the Hon'ble Karnataka High Court in the case of Tumukur Merchants Souharda Co-operative Ltd. (supra) still holds good. Hence, on this aspect, the issue should be restored back to the AO for a fresh decision after examing the facts in the light of these judgment of the Hon'ble Apex Court rendered in the case of The Totgars Co-operative Sale Society Ltd. (supra) and of Hon'ble Karnataka high Court rendered in the case of Tumukur Merchnts Souharda Co-operative Ltd. (supra).

11. Another aspect with regard to the deduction u/s.80P(2)(d) of the Act, is with regard to what is the quantum of interest income that should be brought to tax by the AO, in case the deduction is denied to the Assessee u/s.80P(2)(d) of the Act. On this aspect, the learned Counsel for the assessee filed before us a decision of the Hon'ble ITAT, Bengaluru Bench in the case of Puttur Primary Co-operative Agriculture and Rural Development Bank Ltd., Vs. ITO in ITA No.1449/Bang/2019, order dated 14.06.2021 for Assessment Year 2016-17 wherein the tribunal held that the Assessee should be allowed expenses and the entire gross interest cannot be taxed. The following were the relevant observations of the Tribunal:

6. The next issue relates to the deduction claimed by the assessee u/s 80P(2)(d) of the Act in respect of interest income. Identical issue has been considered by the co-ordinate bench in the case of Karkala Co-op S Bank Ltd (supra). For the sake of convenience, we extract below the relevant observations made by the co-ordinate bench:-

"7. The next common issue relates to rejection of deduction claimed u/s 80P(2)(d) of the Act in respect of interest income earned from fixed deposits kept with bank. We noticed earlier that the A.O. has observed in Assessment Year 2015-16 that the interest income received by the assessee from deposits kept with banks is not eligible for deduction u/s 80P(2)(c) & 80P(2)(d) of the Act since the assessee is not eligible for deduction u/s 80P(2)(a)(i) of the Act. In AY 2016-17, the AO assessed the interest income received on bank deposits under the head "Income from other sources" and denied deduction claimed u/s 80P(2)(d) of the Act. The Ld CIT(A) confirmed the action of the AO on this issue.

8. The Ld. A.R. submitted that the assessee is entitled to claim deduction allowable u/s 57 of the Act in respect of cost of funds and proportionate administrative and other expenses. In support of this submission, the Ld. A.R. placed reliance on the decision rendered by Hon'ble High Court of Karnataka in the case of Totgars Co-operative Sale Society Ltd. Vs. ITO (2015) 58 taxmann.com 35 (Karn). The Ld. A.R. submitted that the assessee in the above said case had put forth identical claim claim before Hon'ble Supreme Court in the case reported as Totgars Co-operative Sale Society Ltd. Vs. ITO (2010) 188 taxmann.com 282 and the Hon'ble Supreme Court, vide 14 of its order, had restored the question raised by the assessee to the file of Hon'ble High Court of Karnataka. Consequent thereto, the Hon'ble High Court of Karnataka has passed the order in the case reported in 58 taxmann.com 35 and held that the Tribunal was not right in coming to the conclusion that the interest earned by the appellant is an income from other sources without allowing deduction in respect of proportionate cost, administrative expenses incurred in respect of such deposits. Accordingly, the Ld. A.R. prayed that the A.O. may be directed to allow deduction of proportionate cost, administrative and other expenses, if the A.O. proposes to assess the interest income earned from bank deposits as income under the head "other sources".

9. We heard Ld. D.R. on this issue. We find merit in the prayer of the assessee, since it is supported by the decision rendered by Hon'ble High Court of Karnataka in the case of Totgars Co-operative Sale Society Ltd. Vs. ITO (2015) 58 taxmann.com 35 (Karn). Accordingly, we direct the A.O. to allow deduction of proportionate cost, administrative and other expenses, if the A. O. proposes to assess the interest income earned from bank deposits as income under the head "other sources".

7. In the instant case, the assessee has earned both interest income and dividend income. In view of the decision rendered by the jurisdictional Hon'ble High Court of Karnataka, the assessee is entitled for deduction of proportionate cost, administrative and other expenses. Accordingly, we set aside the order passed by Ld CIT(A) on this issue and restore the same to the file of the AO with similar directions.

12. The AO will afford opportunity of being heard to the Assessee and filing appropriate evidence, if desired, by the Assessee to substantiate its case, before deciding the issue in the set aside proceedings.

13. In the result, appeal of the assessee is treated as allowed for statistical purposes.

Pronounced in the open court on the date mentioned on the caption page.

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