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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Date of decision: 27th August, 2014.

\+ **INCOME TAX APPEAL 569/2013**

MANTOLA CO-OPERATIVE THRIFT & CREDIT SOCIETY LTD.
..... Appellant

Through Mr. Sanjay Kumar, Jr. Standing Counsel.

versus

COMMISSIONER OF INCOME TAX ..... Respondent

Through Mr. Ajay Vohra, Ms. Kavita Jha and Mr. Vaibhav Agnihotri, Advocates.

CORAM:
HON'BLE MR. JUSTICE SANJIV KHANNA
HON'BLE MR. JUSTICE V. KAMESWAR RAO

SANJIV KHANNA, J. (ORAL)

Heard the learned counsel for the parties in this appeal, which relates to assessment 2008-09 and impugns order dated 28th September, 2012, by which it has been held that the interest income, earned by the appellant-assessee, from the fixed deposits did not qualify for the exemption under Section 80P(2)(a)(i) of the Income Tax Act, 1961 ('Act', for short).

2. The appellant-assessee, a cooperative thrift and credit society, was engaged in the activity of providing credit facilities to its members. However, the finding recorded by the Assessing Officer and the Income Tax Appellate Tribunal (Tribunal, for short) is that the

appellant-assessee had surplus funds, which were not required f carrying on the business of granting credit facilities to the members. The said surplus funds were invested in fixed deposit receipts with commercial banks, for an average maturity period of 500 days.

3. In fact, the argument raised before us is that as per the bye-laws of the appellant cooperative society, only 50% of the thrift mobilised/collected from the members could be given as credit to the members, and the balance had to be kept in FDRs or other income earning avenues. It was submitted that the alleged surplus in fact formed the corpus and therefore interest earned was exempted.

4. Provisions of Sections 11 to 13 of the Act have no application in determining exemption under Section 80P or in determining whether interest income was taxable under the head "income from business" or "income from other sources". Such differentiation between corpus or non-corpus funds is not mandated and stipulated in Section 80P and for determining the head of income; "income from business or profession" or "income from other sources". There is a clear finding that the interest of Rs.1,43,11,462/- was earned by way of investment of surplus funds in FDRs with banks. The submission made by the appellant assessee itself indicates and predicates that interest was earned by investing surplus funds in fixed deposits.

5. The term or expression, "income" has been defined in Section

2(24) of the Act. By way of Finance Act, 2006, sub-section (viia) w inserted to stipulate that profits and gains of business of banking, including credit facilities, carried on by a cooperative society with its members, is taxable and is included in the term, "income". The aforesaid definition of term "income" is inclusive and a broad one. Thus, the income of the appellant-assessee would be taxable under Section 2(24), including the income earned by way of interest on the FDRs with commercial banks. Section 80P provides partial exemption, restricted to the specified "earning" or "incomes" in sub-section (2), and not the entire income. For the purpose of the present appeal, Section 80P(2) clause (a)(i) is material. Relevant part of the said provision and clause (iii), for the sake of convenience, is reproduced below:-

> "80P. Deduction in respect of income of co-operative societies.--(1) Where, in the case of an assessee being a co-operative society, the gross total income includes any income referred to in sub-section (2), there shall be deducted, in accordance with and subject to the provisions of this section, the sums specified in sub-section (2), in computing the total income of the assessee.
>
> (2)The sum referred to in sub-section (1) shall be the following namely:-
>
> (a) in the case of a co-operative society engaged in-
>
> (i) carrying on the business of banking or providing credit facilities to its members or
>
> (ii) x x x x x x x

(iii) the marketing of agricultural produce grown by its members, or

x x x x x x

The whole of the amount of profits and gains of business attributable to any one or more of such activities."

6. No doubt, the term "attributable" is much wider than the term "derived from", but the question still remains, whether the interest income earned from the FDRs out of surplus funds, which were not to be made available and given as credit to the members, can be treated as income attributable to providing credit facilities to members. We need not dilate on the said question as the issue was considered and stands answered by the Supreme Court in the case of ***Totgars' Co-operative Sale Society Ltd. Vs. Income Tax Officer, Karnataka***, [2010] 322 ITR 283. In the said case, the assessee, a cooperative credit society, had provided credit facilities to its members and was also marketing agricultural produce of its members. It had surplus funds, which were invested in short-term deposits and securities, like in the present case where the surplus funds were invested in FDRs for an average period of 500 days. The Supreme Court examined the issue whether the interest income from the said surplus funds was eligible for exemption under Section 80P(2)(a)(i) as income attributable to profit and gains of business. It was observed that interest received from members for providing credit facilities to them was exempt. Further, anything

attributable to the said income would also be covered under Secti 80P. It was highlighted that exemption is partial and not complete, i.e. the whole income of the cooperative society does not get exemption. In the facts of the said case, it was observed that the deduction being in respect of certain incomes, the interest income earned out of surplus fund, would not qualify for deduction as it was assessable under the head "income from other sources".

7. Learned counsel for the appellant-assessee has submitted that the aforesaid decision should not be applied to the facts of the present case, for the assessee in ***Totgars' Cooperative Sale Society Ltd.*** (supra) was not only functioning as a cooperative credit society, but was also carrying on business of marketing of agricultural produce. Reference was made to paragraph 10 of the said decision and it was submitted that the surplus funds, which were generated, were out of marketing of agricultural produce. The first distinction pointed out does not compel and is unacceptable, as the assessee in the said case was a cooperative credit society. Exemption on interest earned on investment of surplus funds was the question, answered. How and why the assessee generated the surplus funds, did not determined whether the interest income was taxable under the head "income from business or profession" or "income from other sources". Surplus funds did not change their nature and character, depending on how they were

initially earned. Further in clause (iii), profits and gains attributable to marketing of the agricultural produce of members stands exempt. The issue specifically raised was, whether the interest income earned on short-term deposits and securities out of surplus funds would be treated as profit and gains of the business attributable to providing credit facilities. It is in this context, the Supreme Court observed:-

> " The assessing officer held, on the facts and circumstances of these cases, that the interest income which the assessee(s) had disclosed under the head "Income from business" was liable to be taxed under the head "Income from other sources". In this connection, the assessing officer held that the assessee Society had invested the surplus funds as, and by way of, investment by an ordinary investor, hence, interest on such investment has got to be taxed under the head "Income from other sources". Before the assessing officer, it was argued by the assessee(s) that it had invested the funds on short-term basis as the funds were not required immediately for business purposes and, consequently, such act of investment constituted a business activity by a prudent businessman; therefore, such interest income was liable to be taxed under Section 28 and not under Section 56 of the Act, and, consequently, the assessee(s) was entitled to deduction under Section 80-P(2)(*a*)(*i*) of the Act. This argument was rejected by the assessing officer as also by the Tribunal and the High Court, hence, these civil appeals have been filed by the assessee(s)."

" At the outset, an important circumstance needs to be highlighted. In the present case, the interest held not eligible for deduction under Section 80-P(2)(*a*)(*i*) of the Act is not the interest received from the members for providing credit facilities to them. What is sought to be taxed under Section 56 of the Act is the interest income arising on the surplus invested in short-term deposits and securities *which surplus was not required for business purposes*. The assessee(s) markets the produce of its members and wholesale proceeds at times were retained by it. In this case, we are concerned with the tax treatment of such amount. Since the fund created by such retention was not required immediately for business purposes, it was invested in specified securities. The question before us is—whether interest on such deposits/securities, which strictly speaking accrues to the members' account, could be taxed as business income under Section 28 of the Act? In our view, such interest income would come in the category of "Income from other sources", hence, such interest income would be taxable under Section 56 of the Act, as rightly held by the assessing officer. In this connection, we may analyse Section 80-P of the Act. This section comes in Chapter VI-A, which, in turn, deals with "Deductions in respect of certain incomes". The headnote to Section 80-P indicates that the said section deals with deductions in respect of income of cooperative societies. Section 80-P(1), inter alia, states that where the gross total income of a cooperative society includes any income from one or more specified activities, then such income shall be deducted from the gross total income in computing the total taxable income of the assessee Society. An income, which is attributable to any of the specified activities in Section 80-P(2) of the

Act, would be eligible for deduction. The word "income" has been defined under Section 2(24)(*i*) of the Act to include profits and gains. This sub-section is an inclusive provision. Parliament has included specifically "business profits" into the definition of the word "income". Therefore, we are required to give a precise meaning to the words "profits and gains of business" mentioned in Section 80-P(2) of the Act. In the present case, as stated above, the assessee Society regularly invests funds not immediately required for business purposes. Interest on such investments, therefore, cannot fall within the meaning of the expression "profits and gains of business". Such interest income cannot be said also to be attributable to the activities of the Society, namely, carrying on the business of providing credit facilities to its members or marketing of the agricultural produce of its members. When the assessee Society provides credit facilities to its members, it earns interest income. As stated above, in this case, interest held as ineligible for deduction under Section 80-P(2)(*a*)(*i*) is not in respect of interest received from members. In this case, we are only concerned with interest which accrues on funds not required immediately by the assessee(s) for its business purposes and which have been only invested in specified securities as "investment". Further, as stated above, the assessee(s) markets the agricultural produce of its members. It retains the sale proceeds in many cases. It is this "retained amount" which was payable to its members, from whom produce was bought, which was invested in short-term deposits/securities. Such an amount, which was retained by the assessee Society, was a liability and it was shown in the balance sheet on the liability side. Therefore, to that extent, such interest income cannot be said to be attributable either to the activity mentioned in Section 80-P(2)(*a*)(*i*) of the Act or in Section 80-P(2)(*a*)(*iii*) of the Act. Therefore, looking to the facts and circumstances of this case, we are of the view that the assessing officer was right in taxing the interest

> income, indicated above, under Section 56 of the Act."

8. The present case is of surplus funds, which were not required for carrying on business of providing credit facilities to members. Half of the funds mobilised/collected from the members could be used for providing credit to the members. The balance amount had to be retained and used for specified purpose, other than providing credit facilities to members. This amount was deposited in FDRs for an average period of 500 days. Bye-laws of the appellant cooperative society prescribed that 50% of the amount mobilised/collected would not be given on credit to the members. These constituted surplus funds as has been held by the Assessing Officer and by the Tribunal. It is on these funds that the interest was earned. The interest earned from the aforesaid funds as held by the Supreme Court in ***Totgars' Cooperative Sale Society Ltd.*** (supra), would fall under Section 56 and would be taxable under the head "income from other sources".

9. Another contention raised by the appellant-assessee is that the assessee was engaged or carrying on business of banking. He submits that wide interpretation should be given to the "banking" and grant of thrift and credit should be construed as banking. It is not possible to accept the said contention and give this extended and broad meaning to the term "banking". The appellant-assessee is a cooperative thrift

society and not a banking company and the expression "business banking" cannot be given a spacious meaning to unrealistically expand the term beyond acceptable limits. Business of banking connotes and is different from activities undertaken by the appellant. The aforesaid wide meaning, as suggested, would also be contrary to the dicta and the ratio of the decision in ***Totgars' Cooperative Sale Society Ltd.*** (supra).

10. As far as principle of mutuality is concerned, this would not have any application in view of sub-section (24), sub-clause (viia) to Section 2 of the Act. Thus, if we accept that the appellant-assessee was a cooperative society and providing credit facilities to its members, clause (viia) to sub-section (24) to Section 2 would be applicable. Even otherwise on the principle of mutuality, the Supreme Court in ***Bangalore Club Vs. CIT***, (2013) 350 ITR 509 has held that the interest earned on FDRs with banks would not be covered by the principle of mutuality as the transactions were not between the contributors and the beneficiary, but were between the assessee and a third person.

11. At this stage, learned counsel for the appellant-assessee has pointed out that the Commissioner of Income Tax (Appeals) had decided the issue in their favour, and therefore other contentions raised regarding expenses covered under Section 57(3) i.e. allowability of

expenditure having nexus with earning of the said income was n examined. This ground/argument was in alternative. Learned counsel for the Revenue submits that this question may be remitted to the Commissioner of Income Tax (Appeals) as he had not decided the said question having allowed the appeal in entirety holding that the entire interest was exempt under Section 80P. We appreciate the stand taken by the learned counsel for the Revenue and accordingly the matter is remitted on the said aspect to the Commissioner of Income Tax (Appeals) for decision.

12. Similarly, with regard to the claim for deduction under Section 80P(2)(i), we find that there was no discussion or finding by the Commissioner of Income Tax (Appeals) , though this ground/issue was raised. This has happened because the Commissioner of Income Tax (Appeals), as noted above, had granted exemption to the entire income earned by the appellant-assessee under Section 80P(2)(i)(a). Learned counsel for the respondent-Revenue submits that this issue could be examined by the Commissioner of Income Tax (Appeals) on merits. We take the statement on record.

The appeal is disposed of. No Costs.

SANJIV KHANNA, J.

V. KAMESWAR RAO, J.

AUGUST 27, 2014
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