**IN THE INCOME TAX APPELLATE TRIBUNAL**
**PUNE BENCH "B", PUNE**

**BEFORE SHRI G.S. PANNU, ACCOUNTANT MEMBER**
**AND SHRI R.S. PADVEKAR, JUDICIAL MEMBER**

**ITA No.33/PN/2014**
**(Assessment Year : 2010-11)**

The Nanded District Central
Co-op. Bank Ltd.,
Nanded, Tq. Nanded,
Dist.- Nanded.

PAN : AAAAN0696A .... Appellant

Vs.

Dy. Commissioner of Income Tax,
Circle- 3, Nanded. .... Respondent

**ITA No.247/PN/2014**
**(Assessment Year : 2010-11)**

Dy. Commissioner of Income Tax,
Circle- 3, Nanded. .... Appellant

Vs.

The Nanded District Central
Co-op. Bank Ltd.,
Station Road, Nanded,
Dist.- Nanded.

PAN : AAAAN0696A .... Respondent

| | | |
|---|---|---|
| Assessee by | : | Mr. Sunil Pathak &<br>Mr. Suhas Bora |
| Department by | : | Mr. A. K. Modi, CIT,<br>Mr. Narendra Kumar, CIT &<br>Mr. S. P. Walimbe, Addl.CIT |
| Date of hearing | : | 15-09-2014 |
| Date of pronouncement | : | 14-10-2014 |

**ORDER**

**PER G. S. PANNU, AM**

The captioned cross-appeals by the assessee and the Revenue pertaining to the assessment year 2010-11, were heard together and are being disposed-off by way of a consolidated order for the sake of convenience and brevity. The captioned cross-appeals are directed against the order of the Commissioner of Income Tax (Appeals), Aurangabad dated 29.11.2013 which,

in turn, has arisen from an order dated 07.03.2013 passed by the Assessing Officer u/s 143(3) of the Income Tax Act, 1961 (in short "the Act").

2. Firstly, in appeal of the assessee vide ITA No.33/PN/2014, the following Grounds of Appeal have been raised :-

*"1] The learned CIT(A) erred in confirming the addition of Rs.110 Crs. on account of the grant received by the appellant bank from State Govt. as an income in the hands of the appellant bank.*

*2] The learned CIT(A) was not justified in treating the grant received of Rs.110 Crs. as an income when the grant received from the State Govt. constituted capital receipt in the hands of the appellant bank.*

*3] The learned CIT(A) erred in holding that the grant received constituted waiver of loan by the State Govt. and hence, it was an income in the hands of the appellant bank.*

*4] The learned CIT(A) failed to appreciate that -*

*a. The grant received of Rs.110 Crs. from the State Govt. was in the nature of capital receipt and thus, it could not be treated as an income.*

*b. The grant given by the State Govt. had to be treated as a financial aid to the appellant bank and therefore, it was a capital receipt.*

*c. Even assuming without admitting that the grant constituted waiver of loan given earlier by the State Govt., the loan sanctioned was for the purposes of making an FDR to maintain the SLR and not for meeting the day to day trading expenses and thus, the loan was on capital account and its waiver did not constitute income in the hands of the appellant bank.*

*d. The decision of Bombay H.C. in the case of Solid Containers was not applicable to the facts of this case.*

*5. The learned CIT(A) erred in disallowing the deduction u/s 36(1)(viia) of Rs.10,32,12,700/-*

*5.1] The learned CIT(A) failed to appreciate that the above deduction was allowable to the appellant bank even if, no provision was made in the accounts to the above extent.*

*6] The appellant requests for admission of additional evidences if any required in support of any of the above grounds of appeal."*

3. In brief, the relevant facts are that captioned assessee is a Non-scheduled Cooperative Bank engaged in the business of banking. For the assessment year under consideration, assessee bank filed a return of income on 16.10.2010 declaring total income at 'Nil'. The return was selected for

scrutiny assessment whereby after making certain disallowances the total income has been determined at Rs.181,85,34,355/-. Various additions/disallowances made by the Assessing Officer were carried in appeal before the CIT(A), who has allowed partial reliefs. The assessee is in appeal on the aforestated Grounds of Appeal challenging the additions sustained by the CIT(A) whereas the Revenue is in appeal challenging the reliefs allowed by the CIT(A). In this background, now we may proceed to adjudicate the captioned cross-appeals.

4. In the appeal of the assessee, the first issue raised by way of Ground of Appeal Nos.1 to 4 relates to an addition of Rs.110 crores made by the Assessing Officer by treating it as a revenue receipt chargeable to tax. The aforesaid sum represented loan received from the Government of Maharashtra in the past years which has been converted into a non-refundable grant during the year under consideration. The assessee treated the same as a capital receipt not chargeable to tax whereas the Assessing Officer and thereafter the CIT(A) has held the same to be a revenue receipt chargeable to tax. The Assessing Officer noticed that the grant was given by the Government of Maharashtra to enable the assessee-bank to recoup its negative net worth so that the assessee bank could come out of the restrictions imposed by Reserve Bank of India u/s 35A of the Banking Regulation Act, 1949. The stand of the Assessing Officer of treating such receipt as a revenue receipt chargeable to tax has also been upheld by the CIT(A), against which assessee is in appeal before us.

5. Before us, learned counsel for the assessee has vehemently submitted that the benefit conferred on the assessee by way of conversion of loan into grant by the Government of Maharashtra during the year was used for maintaining Statutory Liquidity Ratio (SLR) in compliance with the requirements of Reserve Bank of India so as to enable the assessee bank to

carry out its banking activities. According to the learned counsel, assessee is a non-scheduled District Co-operative Bank whose services are majorly used by the farmers and small depositors in smaller towns of Maharashtra. The learned counsel submitted that the action of the Government of Maharashtra is a welfare step to help the farmers and small the depositors of the assessee bank and the grant has been specifically given to maintain the SLR ratio with the Reserve Bank of India. In sum and substance, the stand of the appellant is that the objective of the Government was to help the farmers and small depositors of Nanded, and the grant enabled assessee-bank to maintain the SLR ratio with the Reserve Bank of India so that assessee bank could carry out its business of banking activity. It is sought to be made out on the basis of the material furnished in the Paper Book, which we shall advert to a little later, that the grant by Government of Maharashtra is an encumbered receipt inasmuch as the same is to be utilized only to be put in as SLR security with Reserve Bank of India. It was therefore contended that the aforesaid receipt was a capital receipt not chargeable to tax.

6. On the other hand, the learned CIT-DR appearing for the Revenue has relied upon the orders of the authorities below and has contended that the grant received by the assessee is a revenue receipt and that there was no prohibition that in future such amount cannot be used by the assessee in its regular business activity. According to the learned CIT-DR, it is only for the present that the grant has been invested in SLR securities to be maintained with RBI but in future it was available with the assessee for use in its regular business activity of banking. It has also been contended by the learned CIT-DR that the grant received has a direct nexus with assessee's business i.e. banking activities; and, the grant is to be understood as being given for the purpose of smooth functioning of the business of the assessee-bank. Thus, the grant was a revenue receipt chargeable to tax. In this manner, the learned CIT-DR has defended the order of the lower authorities. In this connection,

the learned CIT-DR has also placed reliance on the judgement of the Hon'ble Supreme Court in the case of Sahney Steel And Press Work Limited & Others. vs. CIT, 228 ITR 253 (SC).

7. The crux of the controversy in the present case revolves around the character of the grant received by the assessee from the Government of Maharashtra of Rs.110 crores. In order to determine the taxability of the grant received, it is essential to appreciate the object and purpose for which the grant has been given to the assessee-bank. We may briefly touch-upon the background of the matter, so as to understand the objective and purpose of the Government of Maharashtra for giving the grant to the assessee-bank. As noted earlier, the appellant before us is a non-scheduled District Central Co-operative Bank situated at Nanded, Maharashtra. The assessee bank is operating under a license granted by the Reserve Bank of India and is subject to the superintendence and control of the Reserve Bank of India in terms of the Banking Regulation Act, 1949. It transpires that the assessee bank was incurring losses and its net worth had become negative. The Reserve Bank of India by a communication dated 20.10.2005 issued directions u/s 35A of the Banking Regulation Act, 1949 restraining the assessee bank from carrying out normal banking activities, whereby assessee was restricted from accepting fresh deposits and also allowing withdrawals from existing accounts. The incurrence of expenditure was also restrained in accordance with such direction, a copy of which has been placed at pages 1 to 2 of the Paper. Thereafter, on 28.03.2007 the Government of Maharashtra agreed to provide Rs.20 crores to the bank as Government share capital. The infusion of such share capital was subject to certain terms and conditions, as can be seen from a copy of such order dated 28.08.2007, placed in the Paper Book at pages 6 to 7. The bank was required to open a separate fund- *"Repayment of Share Capital Fund"* and the capital introduced by the Government of Maharashtra was to be repaid out of such fund in yearly installments of Rs.2 crores after

expiry of 3 years from the date of receipt of the share capital. It is also provided that in case of any default in repayment of share capital, Government of Maharashtra was entitled to interest @ 12%. Similarly, in terms of a decision of the Government of Maharashtra dated 14.03.2008, the assessee bank was sanctioned a loan of Rs.100 crores carrying interest @ 6%. While sanctioning such loan, the Government of Maharashtra noted that the financial condition of the assessee bank was in a bad shape and that the bank was finding it difficult to carry out day to day operations. The Government of Maharashtra also took note of the directions of NABARD that the bank was to submit a proposal to the Central Government for obtaining relief from the provisions of section 11(1) of the Banking Regulation Act, 1949. While sanctioning such loan, certain conditions were put by the Government, as evidenced from the copy of the Government's sanction letter dated 14.03.2008, placed at pages 18 to 19 in the Paper Book. One of the condition prescribes was that the amount of Rs.100 crores shall be deposited by the assessee bank in an Escrow account to be opened with Maharashtra State Co-operative Bank. It was also mandated that the said Escrow account could be used by the assessee bank for the purpose of maintaining Statutory Liquidity Ratio (SLR) and for repayment of loan along with interest to the State Government. In this context, a tripartite agreement dated 28.02.2008 was also entered into between the assessee bank, Government of Maharashtra (through Principal Secretary, Co-operation and Marketing Department) and the Maharashtra State Co-operative Bank Ltd., a copy of which has been placed in the Paper Book at page 12 to 14. The following contents of the tripartite agreement are relevant :-

> *"i. The Nanded District Central Co-operative Bank Ltd. was identified as one of the Bank which is not complying with the provisions of Section 11(1) of Banking Regulation Act, 1949, as the financial health of the bank is precarious and the bank has been issue Directives from Reserve bank of India under section 35A of Banking Regulation Act 1949 (AACS) and the NABARD Regional Office, Pune vide their letter No.MRO.PN.DOS/447/H1-B (Nanded) 2007-08 dated 17.10.2007 has informed to the Commissioner for*

*Cooperation and Registrar of Co-operative Societies M.S. Pune, to provide external support (Monetary and Non Monetary) for revival of the bank.*

*ii. As per the recommendations of NABARD, the Government of Maharashtra has sanctioned loan of Rs.10.00 crores to Nanded District Central Co-operative Bank Ltd. on following terms and conditions that :-*

a. *Loan of Rupees 100.00 crores is sanctioned for maintaining statutory liquidity ratio as per banking Regulation Act.*

b. *Rate of Interest – 6.00% p.a.*

c. *Repayment schedule is as follows :*

*1st installment of Rs.25 crore due to 31.03.2009*

*2nd installment of Rs.25 crore due on 31.03.2010*

*3rd installment of Rs.50 crore due on 31.03.2011*

d. *The amount of Rs.100.00 crores is to be kept with Maharashtra State Co-operative Bank Ltd. in a separate ESCROW account styled as – "SLR of The Nanded District Central Co-operative Bank Ltd."*

e. *The repayment of Rs.100.00 crores and interest thereon the separate ESCROW account has to be maintained.*

*iii. The Nanded District Central Co-operative Bank Ltd. has prepared and submitted Action Plan to Government of India, for granting exemption under the provisions of Section 11(1) of the Banking Regulation Act, 1949 for the year 2008 to 2012. The said plan was vetted by Maharashtra State Co-operative Bank, approved by Government of Maharashtra and is recommended by NABARD to Reserve Bank of India.*

*iv. It is to be noted that as per the 'Action Plan', Nanded Dist. Central Cooperative Bank is required to maintain SLR investment as under :*

| | |
|---|---|
| *31.03.2008* | *64.27 crores* |
| *31.03.2009* | *89.27 crores* |
| *31.03.2010* | *129.27 crores* |
| *31.03.2011* | *184.27 crores* |
| *31.03.2012* | *219.27 crores* |

*v. Despite such approved Action Plan, The Nanded District Central Co-operative Bank Ltd. has agreed to maintain this amount of deposits of Rs. 100.00 crores if MSCB Ltd. on non withdrawal basis for three years and the amount is to be used for the purpose of repayment of Government loan sanctioned for the legal engagement as mentioned above.*

*Now by this deed of Tripartite Agreement the parties to this agreement, do hereby agree as under:*

*I. That the ESCROW account to be opened is to be used for maintaining SLR and for repayment of Government loan amount as per repayment schedule from this ESCROW account, and that the account is to be maintained at Maharashtra State Cooperative Bank Ltd. Mumbai only for these purposes and not for any other purpose and the account will have no other Lien or charge nor any attachment can be levied on the said account as this amount is for specified legal engagement.*

*II. The Maharashtra State Co-operative Bank is hereby authorised to draw Rs.25.00 crores and pay to Principal Secretary, Co-*

*operation Department, Government of Maharashtra, towards first installment on 31.03.2009 and subsequently Rs.25.00 crores as second installment on 31.03.2010 and Rs.50.00 crores as third installment as on 31.03.2011 from this ESCROW account.*

*III. For repayment of the interest amount of Government loan the amount of this ESCROW account will be invested in Fixed Deposit accounts and the same will be treated as ESCROW account and from the interest on Fixed deposits, the amount of Interest of Government loan i.e. is Rs. 6.00 crores will be remitted by MSC Bank Ltd,on behalf of the Nanded District Central Cooperative Bank during the year 2008-09 towards the payment of interest to Government of Maharashtra and Rs. 4.5 Crores for the Year 2009 -10 and Rs. 3.00 Crores for the Year 2010 - 11 through this ESCROW account (FDRs.)*

*IV. if amount of Government Loan is disbursed before 31.03.2008 the proportion of amount of interest will be paid by Maharashtra State Co-operative Bank Ltd on behalf of The Nanded District Central Cooperative Bank Limited, for period ending 31.03.2008."*

**[underlined for emphasis by us]**

8. As a consequence of the aforesaid tripartite agreement, a loan of Rs.100 crores was sanctioned by the Government of Maharashtra and the loan proceeds so received were deposited by the assessee-bank in an Escrow account maintained with Maharashtra State Co-operative Bank Ltd.. The amount was kept in fixed deposits for the purpose of maintaining SLR investments, as is evident by a communication dated 28.03.2008 addressed to the Maharashtra State Co-operative Bank Ltd., a copy of which has been placed in the Paper Book at page 23. At this stage, we may also make a mention of the earlier amount of Rs.20 crores infused by the Government of Maharashtra on 28.03.2007 as share capital in the assessee bank. In this connection, on 26.09.2008, NABARD informed the Government of Maharashtra that the share capital held by the Government in the assessee bank exceeded 25% and that the same should be restricted to 25%. As a result, the Government of Maharashtra vide letter dated 01.12.2008 informed the bank that out of Rs.20 crores invested in the share capital, only Rs.10 crores should be treated as part of share capital and the balance of Rs.10 crores be taken as an interest-free deposit lying with the assessee bank, a copy of such communication is placed at page 25 of the Paper Book.

9. Now, we may refer to a decision of the Government of Maharashtra dated 10.08.2009, a copy of which has been placed at pages 28 to 31 of the Paper Book and the relevant portion of the said Government decision is reproduced hereunder :-

> "Introduction-
>
> *Reserve Bank of India has restricted Nanded District Central Co-operative Bank Ltd., Nanded from accepting deposits or making payment of deposit under provision 35(a) of Banking Regulation Act, 1949.*
>
> *Nanded District Central Co-operative Bank Ltd., Nanded is the only Central Cooperative bank in Maharashtra which has been restricted by Reserve Bank of India to accept deposits and to make payment of deposits. Keeping in mind the interest of farmers and depositors from District, it is utmost important that the transactions of bank are regularized in normal manner. As per the guidelines of Reserve Bank of India it is necessary that the net worth of bank becomes positive to remove the restrictions under provision 35(a) of Banking Regulation Act, 1949. Bank has presented two proposals before State Government to get financial assistance.*
>
> *According to this, under the provision 62(e) of Maharashtra Co-operative Societies Act, 1960 Nanded District Central Co-operative Bank Ltd. has converted this loan of Rs.100 cr. and Rs.10 cr. out of Rs.20 cr. received from State Government as part share capital which was converted into interest free deposit, into donation. In this way, total of Rs.110 cr. is provided as financial assistance from State Government to bank in the form of donation is under consideration of the Government.*
>
> *Decision of the Government:*
>
> *According to reference No.1, above : As per the decision of the Government, Nanded District Central Co-operative Bank had been granted a Share Capital Rs. 20 Cr. According to amendments made in Maharashtra Co-operative Societies Act, 1960, not more than 25% of share capital of an organization should be held by the Government.*
>
> *Therefore, the Government allowed Rs.10 cr. to be kept as interest free deposit out of Rs.20 cr. Government share capital and Rs.10 cr. were treated as share capital.*
>
> *The Government, has now decided to convert this interest free Deposit of Rs.10 crs. as Government "Grant of Rs.10 crs. w.e.f. 26.03.2007.*
>
> *According to reference No.2, above:- as per the decision of the Government loan of Rs.100 cr. at the interest rate of 6% p.a. was granted to bank on the condition of repayment of loan amount before 31.03.2011. Now, the Government has agreed to convert this amount in Grant to assure proper functioning of bank with effect from 14.03.2008."*
>
> **[underlined for emphasis by us]**

10. By way of the aforesaid decision, the sum of Rs.10 crores kept with the assessee bank as interest-free deposit and the loan of Rs.100 crores granted

@ 6% per annum was converted into a grant as a measure of financial assistance. The receipt of such grant by the assessee bank from the State Government is the subject-matter of controversy before us. The aforesaid decision of the Government of Maharashtra clearly brings out that the assessee bank was facing financial hardships and it was put under restrictions by the Reserve Bank of India in terms of section 35A of the Banking Regulation Act, 1949 whereby assessee bank was restricted from accepting deposits or making payment of deposits from the customers. The net worth of the assessee-bank was eroded and therefore the restrictions u/s 35A of the Banking Regulation Act, 1949 were imposed by the RBI. The Government of Maharashtra considered the aforesaid background and decided to provide financial assistance to the assessee bank. The financial assistance was formulated in the form of (i) converting the interest-free deposit of Rs.10 crores as Government grant of Rs.10 crores w.e.f. 26.03.2007; and, (ii) converting the Government loan of Rs.100 crores carrying interest @ 6% into a Government grant w.e.f. 14.03.2008. It is pertinent to note that the interest-free deposit and the Government loan were converted into a grant with effect from respective dates of their original sanctions. Factually speaking, the financial assistance rendered by the State Government was with the object of safeguarding the interest of farmers and depositors from the district. The aforesaid object was sought to be achieved by providing financial grant to the assessee-bank, and thereby enabling the assessee-bank to comply with the RBI mandate and getting the restrictions placed by the Reserve Bank of India u/s 35A of the Banking Regulation Act, 1949 removed and regularizing its normal banking functions.

11. In this background of the matter, now we may proceed to examine the legal position so as to determine as to whether the amount of Rs.110 crores is liable to be treated as a revenue receipt chargeable to tax or a capital receipt not chargeable to tax in the hands of the assessee.

12. In the course of hearing before us, learned CIT-DR appearing for the Revenue heavily relied upon the judgement of the Hon'ble Supreme Court in the case of Sahney Steel (supra) for the proposition that impugned grant received by the assessee is for the smooth running of assessee's business, and therefore it is to be treated as a revenue receipt chargeable to tax. The judgement of the Hon'ble Supreme Court in the case of Sahney Steel (supra) has laid down certain tests to be applied in judging the character of subsidy received by an assessee. In the case of Sahney Steel (supra), subsidy was given upto 10% of the capital investment calculated on the basis of quantum of investment in capital and, therefore it was urged on behalf of the assessee that subsidy was a capital receipt and not a revenue receipt. The subsidy granted in that case on the basis of refund of sales-tax on raw materials, machinery and finished goods was also urged to be of capital nature as the object of the granting refund of sales-tax was that assessee could set-up new business or expand the existing business. The aforesaid position urged by the assessee therein was dismissed on the basis of the analysis of the Subsidy Scheme therein, whereby it was found that subsidy was given by way of assistance in carrying on of the business and on facts, it was concluded that the subsidy given was to meet recurring expenses and not for acquiring capital asset. The Hon'ble Supreme Court also noted that subsidies were granted year after year only after setting-up of the new industry and after commencement of production and therefore such subsidy could be treated as an assistance given for the purpose of carrying on the business of the assessee. Under these circumstances, the subsidy therein was held to be on revenue account.

13. Subsequently, the Hon'ble Supreme Court in the case of CIT vs. Ponni Sugars and Chemicals Ltd., (2008) 306 ITR 392 (SC) has considered and explained the earlier judgement in the case of Sahney Steel (supra). It has been explained that the judgement in the case of Sahney Steel (supra) laid

down the basic test to be applied in judging the character of subsidy, which is to the effect that the character of subsidy has to be determined with respect to the purpose for which the subsidy is given. According to the Hon'ble Supreme Court, the point of time at which the subsidy is paid or the source or the form of subsidy is immaterial. Pertinently, as per the Hon'ble Supreme Court, it is the object for which the subsidy/assistance is given which determines the nature of subsidy; and, the form or mechanism through which the subsidy is given is not relevant.

14. In the background of the aforesaid legal position, we may now examine the facts of the present case. In the present case, it quite clear that the objective of the Government of Maharashtra to give grant to the assessee was to protect the interests of farmers and depositors from the Nanded district. The English translation of Government decision No.DCB-1206/P.K.5666/2-S dated 10.08.2009, placed at page 30 of the Paper Book gives an insight to the object of the Government. In the said Government decision, it is stated that *"Keeping in mind the interest of farmers and depositors from District, it is utmost important that the transactions of bank are regularized in normal manner"*. The aforesaid clearly shows that the object of the Government was to protect the interest of farmers and depositors from the Nanded district and for the said purpose the Government deemed it fit to provide financial assistance to the assessee-bank to enable it to regularize its functioning. Pertinently, the functioning of the bank was restrained by the RBI in the face of the restrictions imposed u/s 35A of the Banking Regulation Act, 1949. The objective and purpose of the Government was sought to be achieved by providing Rs.110 crores as a grant. The case made out by the Revenue is that the financial assistance given to the assessee-bank is for smooth running of its business and therefore it is to be regarded as a trading receipt. No doubt, the aforesaid sum has been used by the assessee for the purpose of maintain the Statutory Liquidity Ratio (SLR) as per the requirements of RBI,

which enabled the assessee-bank to regularize its banking operations. So, however, the form or mechanism of subsidy is not important, as held by the Hon'ble Supreme Court in the case of Ponni Sugars and Chemicals Ltd. (supra). The nature of subsidy has to be determined by the object for which the subsidy is given. The underlying object of the Government was to safeguard the interest of farmers and small depositors, and this object was sought to be achieved by the mechanism of providing financial grant to the assessee-bank and regularizing its normal banking activity. In this manner, it has to be deduced that the subsidy/grant in question has not been received by the assessee-bank is the course of a trade but it is of capital nature.

15. In-fact, in a somewhat similar situation, the decision of the House of Lords in the case of Seaham Harbour Dock Co. vs. Crook (1931) 16 Tax Cases 333 (HL) is relevant. The import of the said judgement and its significance in the present fact-situation becomes aptly clear from the following discussion in the judgement of the Hon'ble Supreme Court in the case of Ponni Sugars and Chemicals Ltd. (supra) :-

> *"15. In the decision of the House of Lords in the case of Seaham Harbour Dock Co. vs. Crook (1931) 16 Tax Cases 333 (HL) the Harbour Dock Co. had applied for grants from the Unemployment Grants Committee from funds appropriated by Parliament. The said grants were paid as the work progressed the payments were made several times for some years. The Dock Co. had undertaken the work of extension of its docks. The extended dock was for relieving the unemployment. The main purpose was relief from unemployment. Therefore, the House of Lords held that the financial assistance given to the company for dock extension cannot be regarded as a trade receipt. It was found by the House of Lords that the assistance had nothing to do with the trading of the company because the work undertaken was dock extension. According to the House of Lords, the assistance in the form of a grant was made by the Government with the object that by its use men might be kept in employment and, therefore, its receipt was capital in nature. The importance of the judgement lies in the fact that the company had applied for financial assistance to the Unemployment Grants Committee. The Committee gave financial assistance from time to time as the work progressed and the payments were equivalent to half the interest for two years on approved expenditure met out of loans. Even though the payment was equivalent to half the interest amount payable on the loan (interest subsidy) still the House of Lords held that money received by the company was not in the course of trade but was of capital nature. The judgement of the House of*

*Lords shows that the source of payment or the form in which the subsidy is paid or the mechanism through which it is paid is immaterial and that what is relevant is the purpose for payment of assistance. Ordinarily such payments would have been on revenue account but since the purpose of the payment was to curtail/obliterate unemployment and since the purpose was dock extension, the House of Lords held that the payment made was of capital nature."*

16. In the case before the House of Lords, a Dock company had applied for grants from Unemployment Grants Committee. The grants were paid for the work undertaken by the Dock company for extension of its docks. The extended dock was for relieving unemployment. The main purpose was relief from unemployment. The financial assistance was given from time to time as the work progressed and it was equivalent to half the interest on approved expenditure met out of loans by the Dock company. Even though the grant was a payment of interest payable on loans, still the House of Lords held that the money received by the Dock company was not in the course of trade but was of capital nature. The said judgement shows that the mechanism through which a subsidy is paid is immaterial, and that what is of relevance is the purpose for the payment of assistance. The House of Lords noted that the Government provided assistance in the form of grant with the object that by its use, men might be kept in employment. As per the Hon'ble Supreme Court ordinarily, such-like payments would have been on revenue account but since the purpose of payment was to curtail/obliterate unemployment and dock extension, therefore the House of Lords held that the payment was of capital nature.

17. In the case before us also even if the grant received by the assessee bank has been used for meeting SLR requirements of RBI, which is relatable to its banking activity, yet the purpose of the payment made by the Government was to safeguard the interest of farmers and small depositors in the district Nanded. The strategy of providing financial assistance by way of the impugned grant was a mechanism devised by the Government of

Maharashtra with the purpose of safeguarding the interest of farmers and depositors from the Nanded district, and the same clearly emerges from the Government decision dated 10.08.2009 (supra). Therefore, in our considered opinion, following the legal position explained by the Hon'ble Supreme Court in the case of Ponni Sugars and Chemicals Ltd. (supra) and having regard to the facts of the present case and keeping in mind the object and purpose of providing the impugned financial assistance to the assessee, we are inclined to uphold the plea of the assessee that the impugned grants received are not in the course of any trade but is of capital nature, which is not chargeable to tax. Thus, on this aspect, assessee has to succeed.

18. Before parting, we may refer to a decision relied upon by the Assessing Officer in the case of Solid Containers Ltd. vs. DCIT, (2009) 308 ITR 417 (Bom) to hold the issue against the assessee. In the said case, the loan taken by the assessee was waived and the same was sought to be taxed as a revenue receipt on the ground that it was a benefit received in the course of trading activity. The said judgement does not help the case of the Revenue before us because in the case before the Hon'ble High Court it was a loan taken for trading activities, and the waived amount was retained in business by the assessee. Under these circumstances, the waiver of the loan was considered as a revenue receipt chargeable to tax. In so far as the present case before us is concerned, the facts as per our discussion in the earlier paragraphs show that they stand on an entirely different footing. In the case before us, the Government of Maharashtra, with the object of safeguarding the interest of farmers and depositors from Nanded district formulated a strategy to provide financial assistance to the assessee-bank in the form of a Government grant. Such a transaction between the Government and the assessee-bank cannot be regarded to have been carried out by the assessee in the course of any business activity. In-fact, it cannot be said in the present case that the impugned grant has been received by the assessee in the

course of any trading activity. Therefore, the ratio of the judgement of the Hon'ble Bombay High Court in the case Solid Containers Ltd. (supra) is not applicable in the present case.

19. Another decision relied upon by the Assessing Officer is that of Hyderabad Bench of the Tribunal in the case of DCIT vs. A.P. State Electricity Board, (2011) 130 ITD 1 (Hyd.). In the case before the Hyderabad Tribunal, subsidy received by the assessee from the State Government was to meet part of the expenditure incurred for improvement of power lines damages due to cyclone. Having regard to the facts of the case, the Tribunal concluded that the aforesaid subsidy enabled the assessee to run its business profitably and therefore the amount of subsidy constituted revenue receipt. Clearly, the facts in the case before the Hyderabad Bench of the Tribunal are quite different from those before us inasmuch the object of the impugned grant paid by the Government is quite different than enabling the assessee to run its business profitably.

20. Since, we have adjudicated the issue by relying on the principles laid down by the Hon'ble Supreme Court in the aforesaid cases, we have refrained from discussing other decisions which were cited at Bar in the course of hearing before us. In any case, the principles formulated in the other decisions cited at Bar are not in conflict with the propositions considered by us in the earlier paragraphs, based on the judgements of the Hon'ble Supreme Court.

21. In conclusion, we therefore set-aside the order of the CIT(A) and direct the Assessing Officer to delete the addition of Rs.110 crores for the reasons mentioned above. Thus, assessee succeeds on the Grounds of Appeal No.1 to 4.

22. Now, we may take-up the Ground of Appeal No.5 raised by the assessee, which is with respect to the denial of its claim for deduction u/s 36(1)(viia) of the Act to the extent of Rs.10,32,12,700/-. In this context, the relevant facts are that assessee claimed deduction u/s 36(1)(viia) of the Act in respect of the Provision for bad and doubtful debts amounting to Rs.15,47,62,700/-, which has been restricted to Rs.5,15,50,000/- by the income-tax authorities. The claim has been restricted to the actual amount of Provision made in the books of account for bad and doubtful debts of Rs.5,15,50,000/- as against assessee's claim for deduction of Rs.15,47,62,700/-.

23. In brief, the relevant facts are that assessee is a Co-operative Bank engaged in the business of banking. In terms of Section 36(1)(viia) of the Act, assessee is entitled to claim deduction in respect of any Provision for bad and doubtful debts made on account of aggregate average advances made by the rural branches of such bank. The section provides that such deduction shall not exceed 7.5% of the total income (computed before making any deduction under this clause and Chapter VI-A of the Act) and an amount not exceeding 10% of the aggregate average advances made by the rural branches of such bank. In terms of the said Section 36(1)(viia) of the Act, assessee being a Co-operative Bank, worked out the deduction at Rs.15,47,62,700/- and claimed the same in the return of income. In the course of assessment proceedings, Assessing Officer noted that as against the claim of Rs.15,47,62,700/-, assessee had made a Provision for bad and doubtful debts of Rs.5,15,50,000/- only in the books of account. For the said reason, the Assessing Officer restricted the deduction under Section 36(1)(viia) of the Act to the extent of the Provision for bad and doubtful debts made in the books of account i.e. Rs.5,15,50,00,000/- and the balance of Rs.10,32,12,700/- was disallowed. The CIT(A) has also sustained the action of the Assessing Officer, against which the assessee is in further appeal before us.

24. In the above background, it was a common ground between the parties that an identical controversy has been considered by the Pune Bench of the Tribunal in the case of Shri Mahalaxmi Co-op. Bank Ltd. vs. ITO vide ITA No.1658/PN/2011 order dated 29.10.2013. In the case of Shri Mahalaxmi Co-op. Bank Ltd. (supra) it has been held, following the judgement of the Hon'ble Punjab & Haryana High Court in the case of State Bank of India vs. CIT, (2005) 272 ITR 54 (P&H), that the deduction u/s 36(1)(viia) of the Act relating to the Provision for bad and doubtful debts was allowable to the extent of Provision actually created in the books of account in the relevant year or the amount calculated as per section 36(1)(viia) of the Act, whichever is lower. Following the said decision, which continues to hold the field as it has not been altered by any higher authority, the plea of the assessee on this ground has to fail. In order to impart completeness to this order, we hereby reproduce the following portion of the order of the Tribunal in the case of Shri Mahalaxmi Co-op. Bank Ltd. (supra) which shall elucidate the reasoning that weighed with the Bench to decide the issue :-

> *"9. We have carefully considered the rival submissions. We have also anxiously perused the authorities cited at Bar in order to determine the controversy on hand. The relevant portion of Section 36(1)(viia) of the Act, as applicable for the assessment year under consideration i.e. A.Y. 2008-09 reads as under : -*
>
> > *"[(viia) [in respect of any provision for bad and doubtful debts made by –*
> >
> > *(a) a scheduled bank [not being [* * *] a bank incorporated by or under the laws of a country outside India] or a non-scheduled bank [or a co-operative bank other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank], an amount [not exceeding seven and one-half per cent] of the total income (computed before making any deduction under this clause and Chapter VIA) and an amount not exceeding [ten] per cent of the aggregate average advances made by the rural branches of such bank computed in the prescribed manner :*
>
> *10. A bare perusal of aforesaid section clearly brings out that the deduction specified therein is in "respect of any provision for bad and doubtful debts made by……." an eligible assessee. The presence of the aforesaid expression in the section supports the plea of the Revenue, which is to the effect that the deduction allowable under Section 36(1)(viia) of the Act is in respect of the provision "made" by the assessee. In our considered opinion,*

*the judgement of the Hon'ble Punjab & Haryana High Court in the case of State Bank of Patiala (supra) clearly covers the controversy in favour of the Revenue and belies the interpretation sought to be canvassed by the assessee. In the case before the Hon'ble High Court, assessee-bank had originally filed its return of income for assessment year 1985-86 claiming deduction under Section 36(1)(viia) of the Act at Rs.1,90,36,000/-. After filing of the return the provisions of Section 36(1)(viia) of the Act were amended by Finance Act, 1985 whereby deduction was enhanced to 10% of the profit or 2% of the aggregate average advances made by rural branches of the bank, whichever was higher. On account of the amended provisions, assessee filed a revised return of income on 24.04.1986 enhancing the claim for deduction from Rs.1,90,36,000/- to Rs.1,94,21,000/-. The Assessing Officer restricted the deduction under Section 36(1)(viia) of the Act to Rs.1,90,36,000/- only and disallowed the balance on the ground that in the books of account pertaining to the relevant assessment year, assessee had made a Provision for bad and doubtful debts of Rs.1,90,36,000/- only. The assessee argued that the Provision of Rs.1,90,36,000/- was made in the Balance-Sheet finalized on 14.02.1985 which was as per the unamended provisions of Section 36(1)(viia) of the Act and that in view of the amendment of Section 36(1)(viia) of the Act permitting higher claim of deduction, the assessee could not have possibly made the higher Provision in the Balance-Sheet finalized on a prior date, but it made up the shortfall by making an adequate Provision in the Balance-Sheet of the subsequent assessment year. On this basis, it was sought to be made out that there was substantial compliance with the requirement of law of making Provision for bad and doubtful debts and therefore assessee justified the claim of deduction for the complete amount of Rs.1,94,21,000/- and not restricted to Rs.1,90,36,000/-. The CIT(A) as well as the Tribunal negated the plea of the assessee and accordingly, the matter was carried before the Hon'ble Punjab & Haryana High Court. The Hon'ble High Court referred to the provisions of Section 36(1)(viia) of the Act and observed that "…..the deduction allowable under the above provisions is in respect of the provision made" and further went on to hold that "…..making of a provision for bad and doubtful debts equal to the amount mentioned in this section is must for claiming such deduction." In view of the aforesaid judgement of the Hon'ble Punjab & Haryana High Court, in our view, the position sought to be canvassed by the assessee deserves to be repelled. We reproduce hereinafter the relevant portion of the order of the Hon'ble High Court, which reads as under :-*

> *"5. Sec.36(1)(viia) of the Act as applicable to the asst. yr. 1985-86, reads as under :*
>
> *"in respect of any provision for bad and doubtful debts made by a scheduled bank [not being a bank approved by the Central Government for the purposes of cl.(viiia) or a bank incorporated by or under the laws of a country outside India] or a non-scheduled bank, an amount not exceeding ten per cent of the total income (computed before making any deduction under this clause and Chapter VI-A) or an amount not exceeding two per cent of the aggregate average advances made by the rural branches of such bank, computed in the prescribed manner, whichever is higher."*
>
> *6. A bare perusal of the above shows that the deduction allowable under the above provisions is in respect of the provision made. Therefore, making of a provision for bad and doubtful debts equal to the amount mentioned in this section is a must for claiming such deduction. The Tribunal has rightly pointed out that this issue stands*

*further clarified from the proviso to cl.(vii) of s.36(1) of the Act, which reads as under :*

*"Provided that in the case of an assessee to which cl.(viia) applies, the amount of the deduction relating to any such debt or part thereof shall be limited to the amount by which such debt or part thereof exceeds the credit balance in the provision for bad and doubtful debts account made under that clause."*

*7. This also clearly shows that making of provision equal to the amount claimed as deduction in the account books is necessary for claiming deduction under s. 36(1)(viia) of the Act. The Tribunal has distinguished various authorities relied upon by the assessee wherein deductions had been allowed under various provisions which also required creation of reserve after the assessee had created such reserve in the account books before the completion of the assessment. It has been correctly pointed out that in all those cases, reserves/provisions had been made in the books of account of the same assessment year and not of the subsequent assessment year.*

*8. In the present case, the assessee has not made any provision in the books of account for the assessment year under consideration, i.e., 1985-86, by making supplementary entries and by revising its balance sheet. The provision has been made in the books of account of the subsequent year.*

*9. We are, therefore, satisfied that the Tribunal was right in holding that since the assessee had made a provision of Rs.1,19,36,000 for bad and doubtful debts, its claim for deduction under s. 36(1)(viia) of the Act had to be restricted to that amount only. Since the language of the statute is clear and is not capable of any other interpretation, we are satisfied that no substantial question of law arises in this appeal for consideration by this Court.*

*11. In view of the aforesaid interpretation of Section 36(1)(viia) of the Act by the Hon'ble Punjab & Haryana High Court, the orders of the lower authorities deserve to be upheld inasmuch as the assessee has not made a Provision for bad and doubtful debts in the books of account equal to the amount of deduction sought to be claimed under Section 36(1)(viia) of the Act, and therefore, in our view, the lower authorities were justified in restricting the deduction to Rs.50,00,000/-, being the amount of Provision actually made in the books of account.*

*12. The learned counsel for the assessee has cited certain decision in support of his proposition that the claim of deduction under Section 36(1)(viia) of the Act is not linked to making of a Provision in the account books. At the outset, we may observe that the decisions relied upon by the assessee are of various Benches of the Tribunal and not of any High Court. Therefore, the judgement of the Hon'ble High Court in the case of State Bank of Patiala (supra), which is contrary to the decisions of the Tribunal relied upon by the assessee; and being solitary judgement of a High Court, is required to be applied, having regard to the established norms of judicial discipline. For the said reason, we refrain from discussing each of the decisions of the Tribunal relied by the assessee before us.*

*13. The other plea of the assessee was that the contents of the CBDT Circular dated 26.11.2008 (supra) is contrary to the provisions of Section 36(1)(viia) of the Act and therefore the same should be disregarded. In our view, the following explanation in respect of Section 36(1)(viia) of the*

*Act rendered by the CBDT in Circular dated 26.11.2008 (supra) by way of para 2(iii)(b) as under :-*

> *"(b) The deduction for provision for bad and doubtful debts should be restricted to the amount of such provision actually created in the books of the assessee in the relevant year or the amount calculated as per provisions of section 36(1)(viia), whichever is less."*

*is in line with the interpretation of the section rendered by the Hon'ble Punjab & Haryana High Court and cannot be said to be contrary to the provisions of the Act. Therefore, the reliance placed by the lower authorities on the CBDT Circular dated 26.11.2008 (supra) cannot be faulted.*

*14. Before parting, we may refer to the decision of the Hon'ble Supreme Court in the case of Catholic Syrian Bank Ltd. (supra) relied upon by the assessee and also the decision of our co-ordinate Bench in the case of Jaysingpur Udgaon Sahakari Bank Ltd. (supra). We have carefully perused the said decision and found that the issue before the Hon'ble Supreme Court in the case of Catholic Syrian Bank Ltd. (supra) was quite different; and, in any case none of the observations of the Hon'ble Supreme Court run contrary to the pronouncement of the Hon'ble Punjab & Haryana High Court in the case of State Bank of Patiala (supra) to the effect that making of a Provision for bad and doubtful debts equal to the amount mentioned in Section 36(1)(viia) of the Act is must for claiming such deduction. Therefore, the judgement of the Hon'ble Supreme Court in the case of Catholic Syrian Bank Ltd. (supra) does not help the assessee in the present controversy before us. Further, even in the case of Jaysingpur Udgaon Sahakari Bank Ltd. (supra), the Tribunal has merely set-aside the matter for adjudication afresh back to the file of the Assessing Officer and it does not contain any positive finding with respect to the controversy before us.*

*15. In the result, considering the aforesaid discussion, in our view, the orders of the authorities below on this aspect are liable to be upheld. We hold so."*

25. Following the aforesaid reasoning in the case of Shri Mahalaxmi Co-op. Bank Ltd. (supra), the claim of the assessee for deduction u/s 36(1)(viia) of the Act is liable to be restricted to the actual amount of Provision for bad and doubtful debts made in the books of account. As a result, the income-tax authorities have rightly allowed the deduction u/s 36(1)(viia) of the Act to the extent of Rs.5,15,50,000/- and not Rs. Rs.15,47,62,700/-, as contended by the assessee. Thus, on this Ground assessee fails.

26. In the result, the appeal of the assessee vide ITA No.33/PN/2014 is treated as partly allowed.

27. Now, in cross-appeal of the Revenue vide ITA No.247/PN/2014, the following Grounds of Appeal has been raised :-

> *"1. The CIT(A) is not justified in deleting the addition on account of Sticky Advances/NPA at Rs.3,49,75,000/- for the following reasons.*
>
> *i) The provisions of Section 145 & 43D are applicable to Interest on Sticky Advances/NPA.*
>
> *ii) The provisions of Section 45Q of RBI Act cannot override Section 43D of the Income tax Act. Since both the Acts operate in different fields.*
>
> *iii) The assessee Bank is adopting Hybrid method of accounting (Cash and Mercantile) which is not allowable simultaneously in the case of Non-Schedule Banks contrary to the provisions of the Income-tax Act.*
>
> *iv) The decision in the case of UCO Bank Vs. CIT (1993) 237 ITR 889 (SC) is not applicable to the instant case as the above cited decision is regarding a commercial bank and therefore the exemption u/s 43D of the Act cannot be extended to a Non Schedule Cooperative Banks & decision in Southern Technologies Vs. JCIT 320 ITR 577 (SC) is applicable in the instant case.*
>
> *v) The CBDT Circular No. F 201/81/84 ITA-II dt. 09/10/1984 is applicable in the case of the assessee bank. This Circular stipulates following two conditions for availing the benefit of the circular. The assessee bank has not fulfilled both these conditions.*
>
> *1. The assessee should be Banking Company.*
>
> *2. Such Interest should have remained uncovered for consecutively for three previous years.*
>
> *The assessee bank has not fulfilled both these conditions.*
>
> *2. The order of the A.O. be restored and the CIT (A) be vacated."*

28. Although, Revenue has raised multiple Grounds of Appeal, but the solitary dispute relates to an addition of Rs.3,49,75,000/- made by the Assessing Officer on account of interest income on sticky advances/Non-Performing Asset advances. Briefly put, the controversy can be summarized as follows. The assessee is a non-scheduled Co-operative Bank carrying on banking business in terms of a license issued by Reserve Bank of India (RBI), and is thus governed by Circulars of RBI relating to Prudential Norms, Income Recognition, Asset Classification, Provisioning and other related matters. In terms of such Prudential Norms of RBI, assessee did not account for interest

relating to Non-Performing Assets (NPAs) i.e. advances to customers which were classified as NPAs in terms of the RBI guidelines. The Assessing Officer was of the opinion that interest income even in relation to such NPAs was liable to be included in this year's total income, having regard to the mercantile system of accounting followed by the assessee. As per the Revenue, the provisions of section 43D of the Act, which provide that interest income relatable to NPAs classified as per the RBI guidelines shall be charged to tax in the year in which it is credited or received by the assessee, whichever is earlier, was not applicable to the assessee, since the assessee was not a scheduled bank or any other entity prescribed in section 43D of the Act. Thus, as per the Assessing Officer, interest income on NPA advances accrued to the assessee and accordingly, he brought to tax such interest income of Rs.3,49,75,000/-, which is the subject-matter of dispute before us.

29. The learned CIT(A) disagreed with the Assessing Officer, and thus the Revenue is in appeal before us. At the time of hearing, it was a common point between the parties that an identical controversy has been considered by the Pune Bench of the Tribunal in the case of ACIT vs. The Omerga Janta Sahakari Bank Ltd. vide order in ITA No.350/PN/2013 dated 31.10.2013. In the said precedent, the Tribunal considered the judgement of the Hon'ble Delhi High Court in the case of M/s Vasisth Chay Vyapar Ltd., 330 ITR 440 (Del) as well as the judgement of the Hon'ble Madras High Court in the case of CIT vs. Sakthi Finance Ltd., (2013) 31 taxmann.com 305 (Madras), which had expressed divergent views with respect to the issue of accrual of interest income on NPA advances; and, following the proposition that in the absence of any judgement of the Jurisdictional High Court, there being contrary judgements of the non-jurisdictional High Courts, a decision which was favourable to the assessee was to be followed in view of the reasoning laid down by the Hon'ble Supreme Court in the case of CIT vs. Vegetable Products Ltd., (1973) 88 ITR 192 (SC) and, thus it was held that the issue was liable to

be decided in favour of the assessee. The relevant discussion in the order of the Tribunal dated 31.10.2013 (supra) is reproduced as under :-

> "*8. We have carefully considered the rival submissions. In so far as the applicability of section 43D of the Act to the assessee is concerned, there is a convergence of opinion between the assessee and the Revenue to the effect that the same is not applicable to the assessee. Ostensibly, assessee is a Co-operative Bank carrying on banking business in terms of a license granted by RBI and is not a 'scheduled bank' included in second schedule of RBI so as to fall within the scope of section 43D of the Act. Notably, section 43D of the Act prescribes that interest income on such categories of bad and doubtful debts as prescribed by the RBI guidelines shall be chargeable to tax in the year in which such interest income is credited by the assessee in the Profit and Loss account or in the year of actual receipt, whichever is earlier. Since assessee is not an entity covered within the scope of section 43D of the Act, the present controversy cannot be adjudicated in the light of section 43D of the Act, and it is liable to be decided on general principles as to whether the impugned income has accrued to the assessee during the year under consideration.*
>
> *9. In this connection, we find that the Visakhapatnam Bench of the Tribunal in the case of The Durga Cooperative Urban Bank Ltd. (supra) has considered an identical controversy. The assessee before the Visakhapatnam Bench was a Co-operative Bank operating under a license issued by RBI but was not a 'scheduled bank' so as to fall within the scope of section 43D of the Act. The issue related to taxability of interest income relating to NPAs, which as per the Revenue was liable to be taxed on accrual basis in line with mercantile system of accounting adopted by the assessee therein. The assessee, on the other hand, contended that having regard to the guidelines issued by RBI regarding accounting of interest on NPAs, no interest income accrued in respect of NPAs and that the same was to be taxed only on receipt basis. The Tribunal observed that the question of taxability of interest on NPAs classified by RBI, was considered by the Hon'ble Delhi High Court in the case of M/s Vasisth Chay Vyapar Ltd. (supra) wherein after considering the decision of the Hon'ble Supreme Court in the case of Southern Technologies Ltd. (supra) it was held that interest income relatable to NPAs was not includible in total income on accrual basis since the same did not accrue to the assessee. The following discussion by the Visakhapatnam Bench of the Tribunal in the case of The Durga Cooperative Urban Bank Ltd. (supra) is worthy of notice :-*
>
> > *"8. We have heard the rival contentions and carefully perused the record. The question of taxability of interest on NPAs has been considered by the Hon'ble Delhi High Court in the case of M/s Vasisth Chay Vyapar Ltd (Supra); wherein the Hon'ble Delhi High Court took into account the decision rendered by the Hon'ble Supreme Court in the case of Southern Technologies Ltd (Supra). In the case of M/s Vasisth Chay Vyapar Ltd, the assessee therein was a non banking financial company and it was also bound by the "Prudential norms directions" issued by the Reserve Bank of India for Income recognition and asset classification. The assessee did not include the interest income relatable to NPA assets in its total income. The Assessing Officer, however, added the said interest as the income of the assessee by holding that it had "accrued" to the assessee even it was not realized as the assessee was following mercantile system of accounting. The learned CIT (A) affirmed the order of the Assessing*

*Officer. However, the ITAT deleted the aforesaid income. Hence the revenue preferred appeal before the Hon'ble Delhi High Court.*

*8.1 After hearing the rival submissions, the Hon'ble Delhi High Court took note of sec.45Q of Reserve Bank of India Act which reads as under:*

> ***"Chapter IIIB to override other laws.***
>
> *45Q. The provisions of this Chapter shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force or any instrument having effect by virtue of any such law".*

*The High Court took note of the fact that the provision of 45Q of Reserve Bank of India has overriding effect over any other law. Then the Hon'ble High Court also considered accounting standard "AS-9" on "Revenue recognition" and also extracted following relevant portion from the said accounting standard:*

> ***9. Effect of uncertainties on Revenue Recognition***
>
> *9.1 Recognition of revenue requires that revenue is a measurable and that at the time of sale or the rendering of the service, it would not be unreasonable to expect ultimate collection.*
>
> *9.2 Where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, e.g., for escalation of price, export incentives, interest etc., revenue recognition is postponed to the extent of uncertainty involved. In such cases, it may be appropriate to recognize revenue only when it is reasonably certain that the ultimate collection will be made. Where there is no uncertainty as to ultimate collection, revenue is recognized at the time of sale or rendering of service even though payments are made by installments.*
>
> *9.3 When the uncertainty relating to collectability arises subsequent to the time of sale or the rendering of the service, it is more appropriate to make a separate provision to reflect the uncertainty rather than to adjust the amount of revenue originally recorded.*
>
> *9.4 An essential criterion for the recognition of revenue is that the consideration receivable for the sale of goods, the rendering of services or from the use of others of enterprise resources is reasonably determinable. When such consideration is not determinable within reasonable limits, the recognition of revenue is postponed.*
>
> *9.5 When recognition of revenue is postponed due to the effect of uncertainties, it is considered as revenue of the period in which it is properly recognized".*

*8.2 The Delhi High Court also considered the decision rendered in the following cases:*

> *i) CIT vs. Elgi Finance Ltd., 293 ITR 357 (Mad)*
>
> *ii) CIT vs. KKM Investments (Cal) – SLP dismissed by Supreme Court (310 ITR 4)*
>
> *iii) CIT vs. Motor Credit Co (P) Ltd., 127 ITR 572 (Mad)*
>
> *iv) UCO Bank vs. CIT 237 ITR 889 (SC)*

*v) CIT vs. Shoorji Vallabhdas & Co 46 ITR 144 (SC)*

*vi) Godhra Electricity Co. Ltd., Vs.CIT 225 ITR 746*

*vii) CIT vs. Goyal M G Gases (P) Ltd., 303 ITR 159 (Del)*

*viii) CIT vs. Eicher Ltd., ITA No.431/2009 dated 15.7.2009 (Del)*

*8.3 After considering the Accounting Standard 9 and the various case law listed above, the Hon'ble Delhi High Court held that the interest on NPA advance cannot be treated as "accrued" to the assessee.*

*8.4 Before the Delhi High Court, the revenue took support of the decision of the Hon'ble Supreme Court in the case of Southern Technologies Ltd (Supra). The Delhi High Court considered the said decision of Hon'ble Apex Court and explained the same as under:*

> *"We have already held that even under the Income Tax Act, interest income had not accrued. Moreover, this submission of Mr. Sabharwal is based entirely on the judgment of the Supreme Court in the case of Southern Technology (Supra).* ***No doubt, in first blush, reading of the judgment gives an indication that the Court has held that Reserve Bank of India Act does not override the provisions of the Income Tax Act.*** *However, when we examine the issue involved therein minutely and deeply in the context in which that had arisen and certain observations of the Apex Court contained in that very judgment, we find that the proposition advanced by Mr.Sabharwal may not be entirely correct.* ***In the case before the Supreme Court, the assessee a NBFC debited Rs.81,68,516 as provision against NPA in the profit and loss account, which was claimed as deduction in terms of Section 36(1) (vii)*** *of the Act. The Assessing Officer did not allow the deduction claimed as aforesaid on the ground that the provision of NPA was not in the nature of expenditure or loss but more in the nature of a reserve, and thus not deductible under section 36(i)(vii) of the Act.* ***The Assessing Officer, however, did not bring to tax Rs.20,34,605/- as income (being income accrued under the mercantile system of accounting).*** *The dispute before the Apex Court centered around deductibility of provision for NPA.* ***After analyzing the provisions of the Reserve Bank of India Act, their Lordships of the Apex Court observed that in so far as the permissible deductions or exclusions under the Act are concerned, the same are admissible only if such deductions/exclusions satisfy the relevant conditions stipulated therefore under the Act. To that extent, it was observed that the Prudential Norms do not override the provisions of the Act.*** *However, the Apex Court made a distinction with regard to "Income Recognition" and held that* ***income had to be recognized in terms of the Prudential Norms, even though the same deviated from mercantile system of accounting and/or section 45 (sic. 145) of the Income Tax Act.*** *It can be said, therefore, that the Apex Court approved the 'real income' theory which is engrained in the Prudential Norms for recognition of revenue by NBFC".*

*9. The Hon'ble Supreme Court in the case of M/s Southern Technologies Ltd (Supra) dissected the matter into two parts viz., a) Income Recognition and b) permissible deduction/exclusions under the Income Tax Act. In so far as income recognition is concerned, the Hon'ble Supreme Court held that Section 145 of the Income Tax Act has no role to play and the Assessing Officer has to follow Reserve Bank of India directions 1998, since by virtue of 45Q of the Reserve Bank of India Act, an overriding effect is given to the directions of*

*Reserve Bank of India vis-à-vis income recognition principles in the Companies Act 1956. In so far as computation of income under the Income Tax Act is concerned, (which involves deduction of permissible deductions and exclusions) the admissibility of such deductions shall be governed by the provisions of the Income Tax Act. The relevant observations of the Hon'ble Supreme Court are extracted below:*

> ***"Applicability of Section 145***
>
> *40. At the outset, we may state that in essence RBI Directions 1998 are Prudential/Provisioning Norms issued by RBI under Chapter IIIB of the RBI Act, 1934. These Norms deal essentially with Income Recognition. They force the NBFCs to disclose the amount of NPA in their financial accounts. They force the NBFCs to reflect "true and correct" profits.* ***By virtue of Section 45Q, an overriding effect is given to the Directions 1998 vis-à-vis "Income Recognition" principles in the Companies Act, 1956.*** *These Directions constitute a code by itself. However, these Directions 1998 and the IT Act operate in different areas. These Directions 1998 have nothing to do with computation of taxable income.* ***These Directions cannot overrule the 'permissible deductions" or "their exclusion" under the IT Act.*** *The inconsistency between these Directions and Companies Act is only in the matter of Income Recognition and presentation of Financial Statements. The Accounting policies adopted by an NBFC cannot determine the taxable income. It is well settled that the Accounting Policies followed by a company can be changed unless the AO comes to the conclusion that such change would result in understatement of profits.* ***However, here is the case where the AO has to follow the Reserve Bank of India Directions 1998 in view of Section 45Q of the Reserve Bank of India Act. Hence, as far as Income Recognition is concerned, Section 145 of the IT Act has no role to play in the present dispute".***

*10. Turning to the facts of the case before us, the assessee herein is a cooperative bank and it is not in dispute that it is also governed by the Reserve Bank of India. Hence the directions with regard to the prudential norms issued by the Reserve Bank of India are equally applicable to the assessee as it is applicable to the companies registered under the Companies Act. The Hon'ble Supreme Court has held in the case of Southern Technologies Ltd (Supra), that the provision of 45Q of Reserve Bank of India Act has an overriding effect vis-à-vis income recognition principle under the Companies Act. Hence Sec.45 Q of the RBI Act shall have overriding effect over the income recognition principle followed by cooperative banks also. Hence the Assessing Officer has to follow the Reserve Bank of India directions 1998, as held by the Hon'ble Supreme Court.*

*10.1 Based on the prudential norms, the assessee herein did not admit the interest relatable to NPA advances in its total income. The Hon'ble Delhi High Court in the case of Vasisth Chay Vyapar Ltd (Supra) has held that the interest on NPA assets cannot be said to have accrued to the assessee. In this regard, the following observations of Hon'ble Delhi High Court in the above cited case are relevant:*

> *"What to talk of interest, even the principle amount itself had become doubtful to recover. In this scenario it was legitimate move to infer that interest income thereupon has not "accrued".*

*The said decision of the Hon'ble Delhi High Court is equally applicable to the issue in our hands. Accordingly we do not find any infirmity with the decision of the learned CIT (A) in holding that the interest income*

*relatable on NPA advances did not accrue to the assessee. Accordingly we uphold his order."*

*10. Following the aforesaid discussion, which has been rendered on an identical issue under similar circumstances, we find no reasons to interfere with the ultimate conclusion of the CIT(A) in deleting the impugned addition relating to interest income in respect of NPAs.*

*11. So, however, the learned Departmental Representative has submitted that the Hon'ble Madras High Court in the case of CIT vs. Sakthi Finance Ltd., (2013) 31 taxmann.com 305 (Madras) has differed with the judgement of the Hon'ble Delhi High Court in the case of M/s Vasisth Chay Vyapar Ltd. (supra) on a similar issue, i.e. relating to interest income on NPAs. The learned Departmental Representative further pointed out that the Hon'ble Madras High Court followed the decision of the Hon'ble Supreme Court in the case of Southern Technologies Ltd. (supra) in holding that interest on NPAs was assessable to tax on accrual basis. We have carefully considered the submissions put-forth by the learned Departmental Representative based on the judgement of the Hon'ble Madras High Court in the case of Sakthi Finance Ltd. (supra). The controversy before the Hon'ble Madras High Court related to non-recognition of interest income on NPAs by the assessee following the RBI guidelines. The Hon'ble Madras High Court took the view that the judgement of the Hon'ble Supreme Court in the case of Southern Technologies Ltd. (supra) also applied to the Income Recognition Norms provided by RBI and therefore it held the interest income on NPAs is liable to be taxed on accrual basis and not in terms of RBI's guidelines. But the Hon'ble Delhi High Court in the case of M/s Vasisth Chay Vyapar Ltd. (supra) has taken a view that Southern Technologies Ltd. (supra) case did not apply to the Income Recognition Norms prescribed by RBI. Ostensibly, there is divergence of opinion between the Hon'ble Delhi High Court and the Hon'ble Madras High Court as noted by the Hon'ble Madras High Court in its order.*

*12. In so far as, present case is concerned there is no judgment of the Jurisdictional High Court. We are faced with two contrary judgments of the non-jurisdictional High Court. In such a situation, we are inclined to prefer a view which is favourable of the assessee following the judgement of the Hon'ble Supreme Court in the case of CIT vs. Vegetable Products Ltd. (1973) 88 ITR 192 (SC).*

*13. Therefore, in view of the aforesaid discussion, we are inclined to follow the decision of our co-ordinate Bench in the case of The Durga Cooperative Urban Bank Ltd. (supra) and accordingly the order of the CIT(A) is liable to the affirmed. We hold so.*

*14. In the result, the appeal of the Revenue is dismissed."*

30. Since it was a common point between the parties that the facts and circumstances in the present case are identical to those considered by us in the case of The Omerga Janta Sahakari Bank Ltd. (supra), following the said precedent the present claim of the assessee deserves to be upheld. Thus, the order of the CIT(A) is hereby affirmed and the Revenue has to fail on this aspect.

31. In the result, appeal of the Revenue is dismissed.

32. Resultantly, whereas the appeal of the assessee is partly allowed that of the Revenue is dismissed.

Order pronounced in the open Court on 14th October, 2014.

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|---|---|
| **Sd/-** | **Sd/-** |
| **(R.S. PADVEKAR)** | **(G.S. PANNU)** |
| **JUDICIAL MEMBER** | **ACCOUNTANT MEMBER** |

Pune, Dated: 14th October, 2014.

*Sujeet*

*Copy of the order is forwarded to: -*

1) The Assessee;
2) The Department;
3) The CIT(A), Aurangabad;
4) The CIT, Aurangabad;
5) The DR "B" Bench, I.T.A.T., Pune;
6) Guard File.

By Order

//True Copy//

Assistant Registrar
I.T.A.T., Pune