INCOME TAX : Where payment had been made to by a company assessee, a partnership firm, and assessee was not a shareholder in company, it was neither a loan nor an advance, but a deferred liability and, thus, section 2(22) would not apply; fact that one of assessee's partner was shareholder in company was irrelevant

[2020] 119 taxmann.com 497 (Madras)

HIGH COURT OF MADRAS

Commissioner of Income Tax, Chennai

v.

T.Abdul Wahid & Co.*

T. S. SIVAGNANAM AND MRS. V. BHAVANI SUBBAROYAN, JJ.
T.C.A. NOS. 512 AND 513 OF 2018†
C.M.P. NO. 10632 OF 2018
SEPTEMBER 21, 2020

Section 2(22) of the Income-tax Act, 1961 - Deemed dividend (Loans and advances to shareholder) - Assessment years 2012-13 and 2014-15 - Whether section 2(22) would stand attracted when a payment is made by a company, in which public are not substantially interested by way of advance or loan to a shareholder - Held, yes - Assessee, a partnership firm, received unsecured loan from a company - Assessing Officer opined that one of partners of assessee-firm, being also a shareholder in said company, holding 26.25 per cent shares had substantial interest in firm and, consequently, concept of deemed dividend under section 2(22)(e) would apply - Whether since payment had been made to assessee, a partnership firm and assessee was not a shareholder in company, it was neither a loan nor an advance, but a deferred liability and, thus, section 2(22) would not apply - Held, yes [Para 12] [In favour of assessee]

CASE REVIEW

National Travel Services v. *CIT* [2018] 89 taxmann.com 332/253 Taxman 243/401 ITR 154 (SC) (para 12) and *Gopal and Sons (HUF)* v. *CIT* [2017] 77 taxmann.com 71/245 Taxman 48/391 ITR 1 (SC) (para 12) *distinguished.*

CASES REFERRED TO

T. Abdul Wahid & Co. v. *ACIT* [IT Appeal Nos. 1796 & 1797 (Mad.) of 2017, dated 17-10-2017] (para 1), *Gopal and Sons (HUF)* v. *CIT* [2017] 77 taxmann.com 71/245 Taxman 48/391 ITR 1(SC) (para 7), *Miss P. Saradas* v. *CIT* [1998] 96 Taxman 11/229 ITR 444 (SC) (para 7), *CIT* v. *National Travel Services* [2011] 14 taxmann.com 14/202 Taxman 327/[2012] 347 ITR 305 (Delhi) (para 7), *National Travel Services* v. *CIT* [2018] 89 taxmann.com 332/253 Taxman 243/401 ITR 154 (SC) (para 7), *CIT* v. *Ankitech (P.) Ltd.* [2011] 11 taxmann.com 100/199 Taxman 341/[2012] 340 ITR 14 (Delhi) (para 7), *Shair Sami Khatib* v. *ITO* [2018] 98 taxmann.com 453/259 Taxman 160/[2019] 411 ITR 637 (Bom.) (para 7), *Bhagavathy Velon* v. *Dy. CIT* [2019] 106 taxmann.com 67/264 Taxman 146 (Mad.) (para 7), *CIT* v. *C. Subba Reddy* [2017] 77 taxmann.com 320 (Mad.) (para 8) and *CIT* v. *Mathur Housing &*

Development Company [Civil Appeal No. 3961 of 2013, dated 5-10-2017] (para 9).

T. Ravi Kumar, Sr. Standing Counsel *for the Appellant.* **R. Sivaraman** *for the Respondent.*

JUDGMENT

T.S. Sivagnanam, J. - These appeals have been filed by the Revenue under section 260-A of the Income-tax Act, 1961 [the 'Act' for brevity] challenging the common order dated 17-9-2017 in I.T.A.Nos.1796/Mds/2017 *T. Abdul Wahid & Co.* v. *ACIT* [IT Appeal Nos. 1796 & 1797 (Mad.) of 2017, dated 17-10-2017] passed by the Income-tax Appellate Tribunal Madras 'A' Bench, Chennai [hereinafter referred to as 'Tribunal'] for the assessment years [for brevity 'AY'] 2012-2013 and 2014-2015.

2. Appeals were admitted on 11-9-2018 to decide the following substantial question of law:

> "Whether the Tribunal was right in holding that the deemed dividend under section 2(22) (*e*) is to be assessed in the hands of the share holder and not in the hands of the firm, which is contrary to the ruling of the Apex Court in the case of National Travel Services passed in Civil Appeal No. 2086 to 2071 of 2012 dated 18-1-2018"

Since the facts are identical for both the assessment years, it would suffice to refer to the facts for the assessment year 2012-2013.

3. The assessee filed the return of income on 30-9-2012 admitting the total income of Rs. 1,19,26,530/-. An order was passed under section 143(3) of the Act on 25-3-2015 assessing the said income. The assessment was reopened by issuance of notice under section 148 of the Act dated 5-2-2016. The reason being that a sum of Rs. 2 Crores was shown as unsecured loan obtained from M/s Abdul Wahid Tanneries Pvt., Ltd., [hereinafter referred to as the 'company'] by the assessee firm; One of the partners of the assessee firm, namely, Mr. T. Rafeeq Ahmed, who holds 35% stake in the assessee partnership firm, is also a share holder in the company holding 26.25% shares. Therefore, it was stated that the share holder of the company had substantial interest in the firm and consequently, the concept of deemed dividend under section 2(22)(*e*) of the Act would apply.

4. The assessee objected to the reopening and filed written submissions. However, the assessing officer confirmed the proposal in the notice under section 148 of the Act and completed the assessment *vide* order dated 29-12-2016 under section 143(3) read with section 147 of the Act for the assessment year 2012-2013 and under section 143(3) of the Act for the assessment year 2014-2015 by an order dated 30-12-2016. Aggrieved by the same, the assessee preferred appeals before the Commissioner of Income-tax [Appeals] - 5, Chennai (CIT(A)), who dismissed the appeals by order dated 27-6-2017. Challenging the same, the assessee filed appeals before the Tribunal, which was allowed by the Tribunal, challenging the same, the Revenue is before us by way of these Tax Case Appeals.

5. Mr. T. Ravikumar, learned senior standing counsel for the appellant referred to section 2(22)(*e*) and explained the concept of deemed dividend. Referring to the facts recorded by the assessing officer in the assessment order dated 29-12-2016, it is submitted that the assessee firm had shown a sum of Rs. 2 Crores as unsecured loan obtained from the company during the year and one of the partner of the assessee firm was having 35% stake in the assessee firm and he was also a major share holder in the company holding 26.25% shares and therefore, the partner is substantially interested in the firm. Further, the company was having accumulated profit of Rs. 3,90,02,578/- for the year ending 31-3-2012. Further, it is submitted that the assessee themselves claimed that the said amount as unsecured loan and auditor had also certified in the balance sheet as unsecured loan; the payment for the purposes of section 2(22)(*e*) need not be cash payments; a journal entry is sufficient for creditor or debtor between the share

holder and the company is sufficient.

6. It is further submitted such loan or advance has to be treated as dividend to the extent of accumulated profits [excluding capitalized profit]. Further, loan or advance may be given directly to a share holder or it may be given for the benefit of share holder or on behalf of share holder. Thus, it is submitted that the assessing officer rightly treated the loan as deemed dividend under section 2(22)(*e*) of the Act. It is further submitted that before the CIT(A), a new ground was canvassed by the assessee stating that the assessee was purchasing finished leather from the company for manufacture of shoe and shoe uppers and during the financial year ending 31-3-2012, the assessee firm had to pay a sum of Rs. 6,31,49,598/- to the company towards the supply of leather. Further, to maintain working capital ratio for the purpose of retaining existing working capital facility from the bank, Rs. 2 crores was transferred from the sundry creditors for trade running account of the company, as deferred liability, which was shown under the balance sheet under the head of "unsecured loan", since the amount was payable after one year, otherwise, the assessee firm should have declared the same under 'current liability' payable within a day.

7. It is also submitted that this reasoning was rightly not accepted by the CIT(A). However, without considering the factual and the legal position, the Tribunal erroneously reversed the orders passed by the assessing authority as confirmed by the CIT(A). In support of his contention, the learned counsel referred to the decisions in the case of *Gopal and Sons (HUF)* v. *CIT* [2017] 77 taxmann.com 71/245 Taxman 48/391 ITR 1(SC); *Miss (P.) Saradas* v. *CIT* [1998] 96 Taxman 11/229 ITR 444 (SC); *CIT* v. *National Travel Services* [2011] 14 taxmann.com 14/202 Taxman 327/[2012] 347 ITR 305 (Delhi); *National Travel Services* v. *CIT* [2018] 89 taxmann.com 332/253 Taxman 243/401 ITR 154 (SC), which doubted the correctness of the decision in the case of *CIT* v. *Ankitech (P.) Ltd.* [2011] 11 taxmann.com 100/199 Taxman 341/[2012] 340 ITR 14 (Delhi). The decision of *Shair Sami Khatib* v. *ITO* [2018] 98 taxmann.com 453/259 Taxman 160/[2019] 411 ITR 637 (Bom.) and the decision of the Hon'ble Division Bench of this Court in *Bhagavathy Velon* v. *Dy. CIT* [2019] 106 taxmann.com 67/264 Taxman 146 (Mad.)

8. Mr. R. Sivaraman, learned counsel appearing for the respondent submitted that the fundamental error committed by the assessing officer and the CIT(A) is on facts because the amount of Rs. 2 Crores paid to the assesseee firm is neither a loan nor an advance, but a deferred liability. The assessee firm is not a beneficial share holder or a registered share holder. The share holder is a partner of the assessee firm and the shares held by him in the Private Limited Company is, in his individual capacity and therefore, the firm is not a beneficial owner. Referring to the balance sheet of the respondent, as on 31-3-2012, it is submitted that the investments have been showed in Schedule D appended to the balance sheet and no where, this, amount of Rs. 2 Crores figures, therefore, the assessing officer and the CIT(A) erred in holding that it is an investment in the name of the assessee. The learned counsel referred to the circular issued by the Central Board of Direct Taxes dated 12-6-2017, wherein it has been stated that trade advances, which are in the nature of commercial transactions would not fall within the ambit of word "advance" in section 2(22)(*e*) of the Act. Reference was made to the decision of Division Bench of this Court in the case of *CIT* v. *C. Subba Reddy* [2017] 77 taxmann.com 320 (Mad.). The Ledger accounts were referred to show that the transaction was a business transaction. Further, the learned counsel submitted that the decision in the National Travel Services is clearly distinguishable on facts and in that regard referred to the facts noted in Paragraph No. 3 of the said Judgment.

9. Further, it is submitted that the decision in Gopal and Sons also is distinguishable on facts as in Paragraph No. 17 of the Judgment, the Court has specifically recorded that the assessee in the said case is the beneficial share holder, whereas on facts, it is not so, in the assessee's case. Further, it is submitted that a batch of civil appeals in [Civil Appeal No. 3961 of 2013 dated 5-10-2017] etc., batch in *C.I.T.* v. *Mathur Housing & Development Company* was dismissed by the Hon'ble Supreme Court by Judgment wherein the correctness of the Judgment in the case of Ankitech Private Limited was also considered

and the Judgments stood affirmed. Further, on facts it is submitted that it is incorrect on the part of the CIT(A) to observe that the assessee had raised the contention that the amount of Rs. 2 Crores was a business transaction, was never raised by the assessee at any earlier point of time, when the fact remains it was raised and it was noted by the assessing officer himself in the assessment order for AY-2014-2015.

10. We have elaborately heard Mr. T. Ravikumar, learned senior standing counsel for the appellant/revenue and Mr. R. Sivaraman, learned counsel appearing for the respondent/assessee.

11. Section 2(22)(*e*) of the Act, which defines dividend, an inclusive definition, includes any payment by a company, not being a company in which the public are substantially interested, of any sum made after the 31-5-1987, by way of advance or loan, to a share holder, being a person, who is the beneficial owner of shares holding not less than 10% of the voting power, or to any concern in which such share holder is a member or a partner and in which he has a substantial interest or any payment by any such company on behalf, or for the individual benefit, of any such share holder, to the extent to which the company in either case possesses accumulated profits.

12. The said provision would stand attracted when a payment is made by a company, in which public are not substantial interested by way of advance or loan to a share holder, being a person who is the beneficial owner of the shares. On facts, it is clear that the payment has been made to the assessee, a partnership firm. The partnership firm is not a share holder in the company. If such is the factual position, the decision in the case of National Travel Services relied on by the revenue cannot be applied, nor the case of Gopal and Sons, as they are factually distinguishable. The records placed before the assessing officer clearly shows the nature of transaction between the firm and the company and it is neither a loan nor an advance, but a deferred liability. These facts have been noted by the assessing officer. In such circumstances, this Court is of the view that the Tribunal rightly reversed the order passed by the CIT(A) affirming the order of the assessing officer.

For the above said reasons, we find no grounds to interfere with the order passed by the Tribunal and accordingly, dismisses the present appeals and answer the substantial question of law against the Revenue. Consequently, connected miscellaneous petition is closed. No costs.

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*In favour of assessee.

†Arising out of Tribunal's order in IT Appeal Nos. 1796 & 1797/Mds/2017, dated 17-10-2017.