REPORTABLE

IN THE SUPREME COURT OF INDIA

CIVIL APPELLATE JURISDICTION

CIVIL APPEAL NO. 12274 OF 2016
(ARISING OUT OF SLP (C) NO. 22059 OF 2015)

GOPAL AND SONS (HUF) .....APPELLANT(S)

VERSUS

CIT KOLKATA-XI .....RESPONDENT(S)

J U D G M E N T

A.K. SIKRI, J.

The appellant/assessee, in the instant appeal, has raised following question of law for determination:

> "Whether in view of the settled principle that HUF cannot be a registered shareholder in a company and hence could not have been both registered and beneficial shareholder, loan/advances received by HUF could be deemed as dividend within the meaning of Section 2(22)(e) of the Income Tax Act, 1961 especially in view of the term "concern" as defined in the Section itself?"

2) The aforesaid question has arisen, which pertains to Assessment Year 2006-07, under the following circumstances:

3) The assessee herein had filed the return in respect of the said Assessment Year declaring his total income at Rs. 1,62,745/-.

The Assessing Officer (for short, 'AO') carried out the assessment resulting into passing of assessment orders dated 31st December, 2008 whereby the net income of the assessee was calculated at Rs. 1,30,31,280/-. Obviously, number of additions were made which contributed to the enhancement of income to the aforesaid figure, in contrast with the paltry income declared by the assessee. Here, we are concerned only with one addition which was made on account of deemed dividend within the meaning of Section 2(22)(e) of the Income Tax Act, 1961 (hereinafter referred to as the 'Act'). Suffice it to state that other additions were deleted by the Income Tax Appellate Tribunal (ITAT) and the position affirmed by the High Court, but the Revenue has not challenged those deletions.

4) Insofar as addition under Section 2(22)(e) of the Act is concerned, a sum of Rs. 1,20,10,988/- was added on this account. The assessee is a Hindu Undivided Family (HUF). During the previous year to the Assessment Year, the assessee had received certain advances from one M/s. G.S. Fertilizers (P) Ltd. (hereinafter referred to as the 'Company'). The Company is the manufacturer and distributor of various grades of NPK Fertilizers and other agricultural inputs. In the audit report and annual return

for the relevant period, which was filed by it before the Registrar of Companies (ROC), it was found that the subscribed share capital of the said Company was Rs. 1,05,75,000/- (i.e., 10,57,500 shares of Rs. 10/- each). Out of this, 3,92,500 number of shares were subscribed by the assessee which represented 37.12% of the total shareholding of the Company. From this fact, the AO concluded that the assessee was both the registered shareholder of the Company and also the beneficial owner of shares, as it was holding more than 10% of voting power. On this basis, after noticing that the audited accounts of the Company was showing a balance of Rs. 1,20,10,988/- as "Reserve & Surplus" as on 31st March, 2006, this amount was included in the income of the assessee as deemed dividend.

5) In the appeal filed by the assessee, the aforesaid addition was affirmed by the Commissioner of Income Tax (Appeals) (for short 'CIT(A)'). Though, this addition was questioned by the assessee on various grounds, we would take note of the submission which is advanced before us as the challenge is confined only on the basis of said submission. The assessee had argued that being a HUF, it was neither the beneficial shareholder nor the registered shareholder. It was further argued that the Company had issued shares in the name of Shri Gopal Kumar Sanei, Karta of the HUF,

and not in the name of the assessee/HUF as shares could not be directly allotted to a HUF. On that basis, it was submitted that provisions of Section 2(22)(e) of the Act cannot be attracted.

6) We would like to reproduce that portion of Section 2(22)(e) of the Act at this stage, which is relevant for the instant appeal:

> "S.2(22) of the Income Tax:- Dividend includes:
> xxx xxx xxx
> (e) any payment by a company, not being a company in which the public are substantially interested, of any sum (whether as representing a part of the assets of the company or otherwise) [made after the 31st day of May, 1987, by way of advance or loan to a shareholder, being a person who is the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) holding not less than ten per cent of the voting power, or to any concern in which such shareholder is a member or a partner and in which he has a substantial interest (hereafter in this clause referred to as the said concern)] or any payment by any such company on behalf, or for the individual benefit, of any such shareholder, to the extent to which the company in either case possesses accumulated profits;
>
> but "dividend" does not include—
>
> xxx xxx xxx
>
> Explanation 3.— For the purposes of this clause,
>
> (a) "concern" means a Hindu undivided family, or a firm or an association of persons or a body of individuals or a company;
>
> (b) a person shall be deemed to have a substantial interest in a concern, other than a company, if he is, at any time during the previous

year, beneficially entitled to not less than twenty per cent of the income of such concern."

7) Taking note of the aforesaid provision, the CIT(A) rejected the aforesaid contention of the assessee. The CIT(A) found that examination of annual returns of the Company with Registrar of Company (ROC) for the relevant year showed that even if shares were issued by the Company in the name of Shri. Gopal Kumar Sanei, Karta of HUF, but the Company had recorded the name of the assessee/HUF as shareholders of the Company. It was also recorded that the assessee as shareholder was having 37.12% share holding. That was on the basis of shareholder register maintained by the Company. Taking aid of the provisions of the Companies Act, the CIT(A) observed that a shareholder is a person whose name is recorded in the register of the shareholders maintained by the Company and, therefore, it is the assessee which was registered shareholder. The CIT(A) also opined that the only requirement to attract the provisions of Section 2(22)(e) of the Act is that the shareholder should be beneficial shareholder. On this basis, the addition made by the AO was upheld.

8) Undeterred, the assessee approached the next higher forum, i.e., ITAT in the form of appeal under Section 253 of the Act. In this

endeavour, the assessee succeeded as appeal of the assessee was allowed holding that the ingredients of Section 2(22)(e) of the Act were not satisfied and, therefore, addition of the aforesaid nature could not be made.

For this purpose, the ITAT referred to the judgment rendered by its Mumbai Bench in the case of ***Binal Sevantilal Koradia (HUF)*** Vs. ***Department of Income Tax***[1]. In fact, the only exercise done by the ITAT in the said order was to quote from the aforesaid judgment with the observations that the issue is squarely covered by the said decision. In ***Koradia (HUF)***, it was held by the Tribunal that HUF cannot be said to be shareholder or a beneficial shareholder. Since these are the twin conditions to attract the provisions of Section 2(22)(e) of the Act, both have to be satisfied. As per the ITAT, since HUF, in law, cannot be a registered shareholder or a beneficial shareholder, provisions of Section 2(22)(e) would not be attracted.

9) As noticed above, the High Court, in the impugned judgment rendered in the appeal preferred by the Revenue, has reversed the judgment of the ITAT, thereby restoring the addition which was made by the AO. The order of the High Court reveals that it has done nothing but to extract the language of Section 2(22)(e) of the

1 ITA No. 2900/Mum/2011, AY 2007-08 dated 10.10.2012

Act and sustained the addition made by AO with one line observation, viz., 'the assessee did not dispute that the Karta is a member of HUF which has taken the loan from the Company and, therefore, the case is squarely within the provisions of Section 2(22)(e) of the Income Tax Act'.

10) The arguments before us remain the same. Mr. S.B. Upadhyay, learned senior counsel appearing for the assessee, argued that the ITAT had correctly explained the legal position that HUF cannot be either beneficial owner or registered owner of the shares and, therefore, no addition could be made under Section 2(22)(e) of the Act. For buttressing this submission, the learned counsel relied upon the following observations in judgment of this Court in ***CIT, Andhra Pradesh*** Vs. ***C.P. Sarathy Mudaliar***[2]:

> "....It is well settled that an HUF cannot be a shareholder of a company. The shareholder of a company is the individual who is registered as the shareholder ion the books of the company. The HUF, the assessee in this case, was not registered as a shareholder in books of the company nor could it have been so registered. Hence there is no gain-saying the fact that the HUF was not the shareholder of the company."

11) Learned Additional Solicitor General, on the other hand, after reading the relevant portions of the orders of AO and CIT(A),

2 1972 SCR 1076

submitted that on the facts of this case, the Revenue was justified in making the addition.

12) Section 2(22)(e) of the Act creates a fiction, thereby bringing any amount paid otherwise than as a dividend into the net of dividend under certain circumstances. It gives an artificial definition of *'dividend'.* It does not take into account that dividend which is actually declared or received. The dividend taken note of by this provision is a deemed dividend and not a real dividend. Loan or payment made by the company to its shareholder is actually not a dividend. In fact, such a loan to a shareholder has to be returned by the shareholder to the company. It does not become income of the shareholder. Notwithstanding the same, for certain purposes, the Legislature has deemed such a loan or payment as *'dividend'* and made it taxable at the hands of the said shareholder. It is, therefore, not in dispute that such a provision which is a deemed provision and fictionally creates certain kinds of receipts as dividends, is to be given strict interpretation. It follows that unless all the conditions contained in the said provision are fulfilled, the receipt cannot be deemed as dividends. Further, in case of doubt or where two views are possible, benefit shall accrue in favour of the assessee.

13) A reading of clause (e) of Section 2(22) of the Act makes it clear that three types of payments can be brought to tax as dividends in the hands of the share holders. These are as follows:

> (a) any payment of any sum (whether as representing a part of the assets of the company or otherwise) by way of advance or loan to a shareholder.
>
> (b) any payment on behalf of a shareholder, and
>
> (c) any payment for the individual benefit of a shareholder.
>
> *[See:* ***Alagusundaran Vs. CIT; 252 ITR 893 (SC)]***

14) Certain conditions need to be fulfilled in order to attract tax under this clause. It is not necessary to stipulate other conditions. For our purposes, following conditions need to be fulfilled:

(a) Payment is to be made by way of advance or loan to any concern in which such shareholder is a member or a partner.

(b) In the said concern, such shareholder has a substantial interest.

(c) Such advance or loan should have been made after the 31st day of May, 1987.

15) Explanation 3(a) defines "concern" to mean HUF or a firm or an association of persons or a body of individuals or a company. As

per Explanation 3(b), a person shall be deemed to have a substantial interest in a HUF if he is, at any time during the previous year, beneficially entitled to not less than 20% of the income of such HUF.

16) In the instant case, the payment in question is made to the assessee which is a HUF. Shares are held by Shri. Gopal Kumar Sanei, who is Karta of this HUF. The said Karta is, undoubtedly, the member of HUF. He also has substantial interest in the assessee/HUF, being its Karta. It was not disputed that he was entitled to not less than 20% of the income of HUF. In view of the aforesaid position, provisions of Section 2(22)(e) of the Act get attracted and it is not even necessary to determine as to whether HUF can, in law, be beneficial shareholder or registered shareholder in a Company.

17) It is also found as a fact, from the audited annual return of the Company filed with ROC that the money towards share holding in the Company was given by the assessee/HUF. Though, the share certificates were issued in the name of the Karta, Shri Gopal Kumar Sanei, but in the annual returns, it is the HUF which was shown as registered and beneficial shareholder. In any case, it cannot be doubted that it is the beneficial shareholder. Even if

we presume that it is not a registered shareholder, as per the provisions of Section 2(22)(e) of the Act, once the payment is received by the HUF and shareholder (Mr. Sanei, karta, in this case) is a member of the said HUF and he has substantial interest in the HUF, the payment made to the HUF shall constitute deemed dividend within the meaning of clause (e) of Section 2(22) of the Act. This is the effect of Explanation 3 to the said Section, as noticed above. Therefore, it is no gainsaying that since HUF itself is not the registered shareholder, the provisions of deemed dividend are not attracted. For this reason, judgment in ***C.P. Sarathy Mudaliar***, relied upon by the learned counsel for the appellant, will have no application. That was a judgment rendered in the context of Section 2(6-A)(e) of the Income Tax Act, 1922 wherein there was no provision like Explanation 3.

18) We, thus, do not find any merit in this appeal, which is accordingly dismissed.

.....J.
(A.K. SIKRI)

.....J.
(ABHAY MANOHAR SAPRE)

NEW DELHI;
JANUARY 04, 2017.