

National Travel Services Vs. Commissioner of Income Tax, Delhi - VIII

C.A. No. 837 of 2018 @ S.L.P. (C) No. 27245 of 2017 · Supreme Court of India · 2018-01-18 · R.F. Nariman · Navin Sinha · F2J-C-1358

Full judgment text

National Travel Services Vs. Commissioner of Income Tax, Delhi - VIII

[Civil Appeal Nos. 2068-2071 of 2012]

[C.A. No. 837 of 2018 @ S.L.P. (C) No. 27245 of 2017]

R.F. Nariman, J.

1. Leave granted.

2. The present appeals raise an interesting question as to the correct interpretation of Section 2(22)(e) of the Income Tax Act, 1961, as amended in 1988.

3. The brief facts in order to decide the present controversy are as follows: The Assessee is a partnership firm consisting of three partners, namely, Mr. Naresh Goyal, Mr. Surinder Goyal and M/s Jet Enterprises Private Limited having a profit sharing ratio of 35%, 15% and 50% respectively. The Assessee firm had taken a loan of Rs. 28,52,41,516/- from M/s Jetair Private Limited, New Delhi. In this Company, the Assessee subscribed to the equity capital of the aforesaid Company in the name of two of its partners, namely, Mr. Naresh Goyal and Mr. Surinder Goyal totaling 48.19 per cent of the total shareholding. Thus Mr. Naresh Goyal and Mr. Surinder Goyal are shareholders on the Company's register as members of the Company. They hold the aforesaid shares for and on behalf of the firm, which happens to be the beneficial shareholder.

4. The question that arises in these appeals is as to whether Section 2(22)(e) of the Act gets attracted inasmuch as a loan has been made to a shareholder, who after the amendment, is a person who is the beneficial owner of shares holding not less than 10% of the voting power in the Company, and whether the loan is made to any concern in which such shareholder is a partner and in which he has a substantial interest, which is defined as being an interest of 20% or more of the share of the profits of the firm.

5. The Income Tax Act, 1922 contained the definition of "dividend" which reads as follows:-

"2. (6A) 'dividend' includes- ... (e) any payment by a company, not being a company, in which the public are substantially interested within the meaning of Section 23A, 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 or any payment by any such company on behalf or for the individual benefit of a shareholder, to the extent to which the company in either case possesses accumulated profits;"

6. This provision came up for consideration before a Bench of this Court in C.I.T., Andhra Pradesh vs. C.P. Sarathy Mudaliar, (1972) 4 SCC 531. In the context of the Assessee being a Hindu Undivided Family, the question of law set out in the aforesaid judgment is as follows:-

"Whether, on the facts and in the circumstances of the case, the amounts of Rs.5,790 and Rs.39,085 could be deemed to be the dividend income of the Hindu undivided family in the respective assessment years?" After setting out the aforesaid section, this Court held:

"6. Before a payment can be considered as dividend under Section 2 (6A)(e), the following conditions will have to be satisfied:

1. It must be a payment by a company not being a company in which the public are substantially interested within the meaning of Section 23A, any sum whether as representing a part of the assets of the company or otherwise by way of advance or loan.

(a) It must be an advance or loan to a shareholder, or

(b) a payment by the company on behalf or for the individual benefit of the shareholder, and

3. To the extent to which the company in either case possesses accumulated profits." After stating that there is no dispute that the first and last conditions are satisfied, in the said case, the Court went into condition 2(a). This was answered by the Court as follows:

"8. The only surviving question is whether a loan advanced by a company to a H.U.F., which is the real owner of the shares, can be considered as a loan advanced to its shareholder. It is well-settled⁵ that an H.U.F. cannot be a shareholder of a company. The shareholder of a company is the individual who is registered as a shareholder in the books of the company. The H.U.F., 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 H.U.F. was not the shareholder of the company. Mr. Sen did not contend otherwise.

9. Section 2 (6A)(e) gives an artificial definition of "dividend". It does not take in dividend actually declared or received. The dividend taken note of by that provision is a deemed dividend and not a real dividend. The loan granted to a shareholder has to be returned to the company. It does not become the income of the shareholder.

For certain purposes, the Legislature has deemed such a loan as "dividend". Hence, Section 2 (6A) (e) must necessarily receive a strict construction. When Section 2(6A)(e) speaks of "shareholder", it refers to the registered shareholder and not the beneficial owner. The H.U.F. cannot be considered as a shareholder either under Section 2 (6A)(e) or under Section 23A or under Section 16(2) read with Section 18(5) of the Act. Hence, a loan given to an H.U.F. cannot be considered as a loan advanced to a "shareholder" of a company."

7. This judgment was followed by another judgment of this Court in *M/s Rameshwari Lal Sanwormal vs. Commissioner of Income Tax, Assam* (1980) 2 SCC 371 which again arose in the context of a Hindu Undivided Family. *Sarathy Mudaliar's* case was followed in this judgment, and it was expressly stated that there was no conflict between this judgment and another judgment, namely, *C.I.T. vs. Rameshwari Lal Sanwormal*, (1972) 4 SCC 342, and that the Revenue's contention to refer *Sarathy Mudaliar's* case to a larger Bench was turned down.

8. The effect of these two judgments is clearly to hold that before Section 2(6A) (e) of the 1922 Act can be attracted, the "shareholder" referred to in the said provision must be a shareholder whose name is on the register of members of the Company. When the Income Tax Act, 1961 came into force and repealed the 1922 Act, the definition of "dividend" contained in Section 2(22)(e) was as follows:-

"Section 2. Definition - In this Act, unless the context otherwise requires,-

(22) "dividend" includes-

(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) by way of advance or loan to a shareholder, being a person who has a substantial interest in the company or any payment by any such company on behalf or for the individual benefits, of any such shareholder, to the extent to which the company in either case possesses accumulated profits;"

9. A cursory look at the aforesaid definition would go to show that the shareholder referred to in the aforesaid provision would continue to be a shareholder who is on the register of members of the Company with one additional feature, namely, that such shareholder should be a person who has a substantial interest in the Company. Admittedly, the aforesaid additional feature would make no difference to the position of law laid down in the aforesaid two decisions.

10. In 1988, however, this definition was amended to read as follows:-

"Section 2. Definition - In this Act, unless the context otherwise requires,-

(22) "dividend" includes-

(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 percent 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"

Explanation 2. - the expression "accumulated profits", in sub-clauses (a), (b), (d) and (e), shall include all profits of the company up to the date of distribution or payment referred to in those sub-clauses, and in sub-clause (c) shall include all profits of the company up to the date of liquidation, {but shall not, where the liquidation is consequent on the compulsory acquisition of its undertaking by the Government or a corporation owned or controlled by the Government under any law for the time being in force, include any profits of the company prior to three successive previous years immediately preceding the previous year in which such acquisition took place;

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;"

11. The Explanatory memorandum to the amendment thus made reads as follows:- "With the deletion of Section 104 to 109 there was a likelihood of closely held companies not distributing their profits to shareholders by way of dividends but by way of loans or advances so that these are not taxed in the hands of the shareholders. To forestall this manipulation, sub-clause (e) of clause (22) of Section 2 has been suitably amended. Under the existing provisions, payments by way of loans or advance to shareholders having substantial interest in a company to the extent to which the company possesses accumulated profits is treated as dividend.

The shareholders having substantial interest are those who have a shareholding carrying not less than 20 per cent voting power as per the provisions of clause (32) of Section 2. The amendment of the definition extends its application to payments made (i) to a shareholder holding not less than 10 per cent of the voting power, or (ii) to a concern in which the shareholder has substantial interest.

"Concern" as per the newly inserted Explanation 3 (a) to Section 2 (22) means a HUF or a firm or an association of persons or a body of individuals or a company. A shareholder having a substantial interest in a concern as per part (b) of Explanation 3 is deemed to be one who is beneficially entitled to not less than 20 per cent of the income of such concern.

10.3 The new provisions would, therefore, be applicable in a case where a shareholder has 10 per cent or more of the equity capital. Further, deemed dividend would be taxed in the hands of a concern where all the following conditions are satisfied:-

(i) where the company makes the payment by way of loans or advances to a concern.;

(ii) where a member or a partner of the concern holds 10 per cent of the voting power in the company; and

(iii) where the member or partner of the concern is also beneficially entitled to 20 per cent of the income of such concern. With a view to avoid the hardship in cases where advances or loans have already been given, the new provisions have been made applicable only in cases where loans or advances are given after 31st May, 1987."

These amendments will apply in relation to assessment year 1988-89 and subsequent years."

12. A reading of the amended definition would indicate that, after 31.05.1987, a "shareholder" is now a person who is the beneficial owner of shares holding not less than 10% of the voting power of the Company. Also, a new category has been added to the definition by introducing concerns in which such shareholder is a member or partner and in which he has a substantial interest.

Explanation (3) of the amended provision states that "concern" means Hindu Undivided Family, firm, association of persons, body of individuals, or a Company and further goes on to state that 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 20% of the income of such concern.

13. Shri Ujjwal A. Rana, learned advocate, appearing on behalf of the appellants, has argued before us that a judgment had been delivered by the very Division Bench in another case C.I.T. vs. Ankitech

Private Limited reported in [2012] 340 ITR 14 (Del). The same Division Bench had arrived at a conclusion, following other judgments of other Courts and Tribunals, that the expression "shareholder" would continue to mean a registered shareholder even after the amendment, and that, this being the case, it is clear that the impugned judgment has taken an about turn and has sought to distinguish the earlier judgment when it was squarely applicable.

He has also placed before us an order dated 05.10.2017 passed in Civil Appeal No. 3961 of 2013 [C.I.T., Delhi-II vs. Madhur Housing and Development Company] in which this Court has expressly affirmed the reasoning of the aforesaid earlier judgment. In his view, therefore, this judgment ought to have been followed, and if it had been followed, it is clear that the firm, not being a registered shareholder, could not possibly be a person to whom Section 2(22)(e) would apply.

14. As opposed to this, Shri Guru Krishnakumar, learned senior advocate, appearing on behalf of the Revenue, has sought to support the impugned judgment by pointing out that the impugned judgment itself has made a distinction between the facts in Ankitech (supra) and in the present case. According to him, the impugned judgment has reference only to the second limb of the amended definition, namely, to the limb which deals with any concern in which such shareholder is a member and not to the first limb, which deals with a shareholder being a person who is the beneficial owner of shares. According to him, therefore, the Division Bench rightly sidestepped the decision in Ankitech (supra) and correctly arrived at the conclusions to the two questions raised.

15. This then brings us to the Division Bench judgment in the present case. In para 17, after referring to various judgments referred to by us hereinabove, the Division Bench posed two questions to be answered by it as follows:-

"(1) To attract the first limb of Section 2 (22) (e) of the Act, is it necessary that the person who has received the advance or loan is a shareholder and also beneficial owner. To put it otherwise, whether both the conditions are required to be satisfied will depend upon the interpretation to be given to the words "being a person who is a beneficial owner of shares....." which was inserted by amendment in the aforesaid provision carried out by the Finance Act, 1987 w.e.f. 1st April, 1988.

(2) Whether the assessee who is a partnership firm can be treated as 'shareholder' because of the reason that it has purchased the shares in the name of the two partners."

16. It answered the first question by stating that the expression "being a person who is a beneficial owner of shares" would be in addition to the shareholder first being a registered shareholder of the Company. The Division Bench then states that, therefore, in order to attract Section 2(22)(e) both conditions have to be satisfied. So far as the second question is concerned, the Division Bench went on to state that a partnership firm can be treated as a shareholder but that it is not necessary that it has to be a registered shareholder.

17. We are of the view that it is very difficult to accept the reasoning of the Division Bench. It is not enough to say that Ankitech's case refers to the second limb of the amended definition, whereas the present case refers to the first limb, for the simple reason that the word "shareholder" in both limbs would mean exactly the same thing. This is for the reason that the expression "such shareholder" in the second limb would show that it refers to a person who is a "shareholder" in the first limb.

18. This being the case, we are of the view that the whole object of the amended provision would be stultified if the Division Bench judgment were to be followed. Ankitech's case, in stating that no change was made by introducing the deeming fiction insofar as the expression "shareholder" is concerned is, according to us, wrongly decided. The whole object of the provision is clear from the Explanatory memorandum and the literal language of the newly inserted definition clause which is to get over the two judgments of this Court referred to hereinabove. This is why "shareholder" now, post amendment, has only to be a person who is the beneficial owner of shares.

One cannot be a registered owner and beneficial owner in the sense of a beneficiary of a trust or otherwise at the same time. It is clear therefore that the moment there is a shareholder, who need not necessarily be a member of the Company on its register, who is the beneficial owner of shares, the Section gets attracted without more. To state, therefore, that two conditions have to be satisfied, namely, that the shareholder must first be a registered shareholder and thereafter, also be a beneficial owner is not only mutually contradictory but is plainly incorrect.

Also, what is important is the addition, by way of amendment, of such beneficial owner holding not less than 10% of voting power. This is another indicator that the amendment speaks only of a beneficial shareholder who can compel the registered owner to vote in a particular way, as has been held in a catena of decisions starting from Mathalone vs. Bombay Life Assurance Co. Ltd., [1954] SCR 117.

19. This being the case, we are prima facie of the view that the Ankitech judgment (supra) itself requires to be reconsidered, and this being so, without going into other questions that may arise, including whether the facts of the present case would fit the second limb of the amended definition clause, we place these appeals before the Hon'ble Chief Justice of India in order to constitute an appropriate Bench of three learned Judges in order to have a relook at the entire question.

20. Ordered accordingly.

.....J. (R.F. Nariman)

.....J. (Navin Sinha)

New Delhi;

January 18, 2018

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