

(1997) 09 MAD CK 0061

In the Madras High Court

Case No : Tax Case No. 1104 of 1982 (Reference No. 665 of 1982)

Commissioner of Income Tax

APPELLANT

Vs

Smt. Savithiri Sam

RESPONDENT

Date of Decision : 17-09-1997

Acts Referred:

Income Tax Act, 1961 — Section 12(1B), 2(22), 2(6A)

Citation : (1999) 236 ITR 1003

Hon'ble Judges : Kanakaraj, J;K.M. Natarajan, J

Bench : Division Bench

Advocate : Deokinandan, for the Appellant; K.M.L. Majele, for the Respondent

Judgement

J. Kanakaraj, J.—The assessee is a shareholder in a private limited company called Sujani Textiles Ltd. Her husband late Shri G. N. Sam

was also a shareholder in that company. Her husband withdrew large sums of money on different dates from the said company. On December 31,

1961, there was a total sum of Rs. 3,68,345 on reserves made up of the following amounts :

(Rs.)

Reserves including provisions made for the assessment year 3,00,000

Surplus in the profit and loss account 19,865

Proposed dividends 48,480

Total 3,68,345.

2. For the assessment year 1962-63, a sum of Rs. 1,95,550 was assessed in the hands of her husband as deemed dividend by invoking the

provisions of section 2(22)(e) of the Income Tax Act. Deducting this amount of Rs. 1,95,550 from the reserves of Rs. 3,68,345 the balance of Rs.

1,72,795 was treated as deemed dividend and brought to tax in the hands of the assessee for the assessment year 1962-63. The relevant previous

year for the assessment year 1962-63 is the year ended on March 31, 1962. As on December 31, 1961, there was a debit balance of Rs.

4,73,241 in the estate of late G. N. Sam. This amount was transferred to the account of the assessee in the books of the said company. By such a

transfer, the said amount in the hands of the assessee was shown as debit balance in the assessee's account. The question in this case is whether

the said amount so transferred could be treated as payment made to her by the company in order that the amount would attract the provisions of

section 2(22)(e) of the Income Tax Act. According to the Income Tax Officer, it was constructive payment because the transfer resulted in

extinguishment of the liability of her husband to the company and the acceptance on the part of the assessee of that liability. The Commissioner

(Appeals) overruling the order of the Income Tax Officer reduced the amount as deemed dividend to only Rs. 43,550. The Tribunal determined

the loan amount taken by the assessee at only Rs. 15,542 and directed that the said amount alone should be treated as deemed dividend u/s 2(22)

(e). On the above facts and circumstances, the following question of law has been referred for consideration by this court, at the instance of the

Revenue.

Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that for the purposes of computation

of deemed dividend u/s 2(22)(e) of the Income Tax Act, 1961, there must be actual flow of cash from the company to the shareholder and the

transfer of money from the account of her husband to her account did not amount to a payment as envisaged in that section ?

3. For understanding the scope of section 2(22)(e) the relevant portion of the section may be extracted :

2(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 benefit, of

any such shareholder, to the extent to which the company in either case possesses accumulated profits.

4. The Tribunal while considering the application of section 2(22)(e) says that the first step is to ascertain the loan taken by the shareholder. The second step is to ascertain the accumulated profit. The Tribunal then proceeded to say that the Commissioner of Income Tax (Appeals) did not disobey the earlier order of the Tribunal because the Commissioner of Income Tax had been given a free hand to conduct the proceedings de novo.

5. On the question of the correct interpretation to be placed on section 2(22)(e) the Tribunal preferred to follow the judgment of this court in G.R.

Govindarajulu Naidu and Another Vs. Commissioner of Income Tax, . The Income Tax Officer, on, the other hand, had preferred to follow a

Division Bench judgment of this court in T. Sundaram Chettiar Vs. Commissioner of Income Tax, Madras, . Though he did not actually refer to the

decision, he had in fact applied the ratio of the said decision. Our task is, therefore, simplified in the sense we have only to find out whether the

Tribunal was right in following the later decision in G.R. Govindarajulu Naidu and Another Vs. Commissioner of Income Tax, and whether good

and sufficient reasons had been given for ignoring the earlier decision in G.R. Govindarajulu Naidu and Another Vs. Commissioner of Income Tax,

, was a case in which a shareholder had borrowed large sums of money from the company. At her death, her son inherited the estate and became

the owner of her shares in the company. Her son also undertook the liability of his mother to the company and made himself indebted to the

company for the amount of principal and interest due by her. Under these circumstances, under the earlier Act identical provisions of law were

applied and the loan was treated as a dividend income and brought to tax. The Division Bench on the above facts held as follows (page 292) :

It is urged on behalf of the assesseees that the loans were advanced by the companies only to Visalakshi Achi and that there was no payment "by

the companies to the assesseees," and that section 12(1B) is, therefore, inapplicable. It is not disputed-and indeed it cannot be disputed-that had

Visalakshi Achi been alive in the year of assessment and if she was the assessee in that year, transactions between her and the companies would

fall quite clearly within the ambit of the taxing provision. The crucial question, therefore, is was there a payment "by the companies to the

assesseees" ? As stated already the assesseees themselves undertook to discharge the loans due by their mother to the two companies. It is not

necessary that payment should have been made by the company to the shareholder in the current coins of the realm. Earl Jowitt points out in his

Dictionary of English Law under the caption "payment" as follows : at page 1318 : "Payment in fact is an actual payment from the payer to the

payee; payment in law is a transaction equivalent to actual payment". We are unable to agree with the contention urged on behalf of the assesseees

that inasmuch as no sum of money was received in cash or in specie by the assesseees from the companies, there can be no payment within the

meaning of section 12(1B) of the Act. The substantial requirement to attract the applicability of section 12(1B) is that there should be the jurial

relationship of debtor and creditor between the shareholder and the company.

6. The Division Bench also held that the date of payment for the purpose of ascertaining the accumulation of profits of the company is the date on

which each of the assesseees made himself personally liable to the companies.

7. G.R. Govindarajulu Naidu and Another Vs. Commissioner of Income Tax, , is a case where the assessee family held 3,300 partly paid up

shares in a private limited company. In the year ended on December 31, 1956, a sum of Rs.,1,50,202 was debited to the profit and loss account

and credited to the development rebate reserve account. Similarly, for the year ended on December 31, 1957, also a similar exercise was

undertaken. In the assessment years 1957-58 and 1958-59, the development rebate reserve amounted to Rs. 3,58,212. After eliminating the

opening debit balance and the interest amount, the advances received by the assessee-family during the year amounted to Rs. 7,111.52. The

Income Tax Officer considered this amount as dividend u/s 2(6A)(e), as according to him, the company had accumulated profits of over Rs.

1,50,000 in the shape of development rebate reserve. Similarly, for the year ending March 31, 1959, a sum of Rs. 1,46,728 was assessed as

dividend u/s 2(6A)(e) for the same reason. The sum of Rs. 1,46,728 was arrived at by adding up the withdrawals during the year and the amount

of first and second calls of the share monies payable on 3,300 shares held by the

company. It is needless to point out that section 2(6A)(e) is the predecessor to section 2(22)(e). The Division Bench had taken note of the earlier judgment reported in *T. Sundaram Chettiar Vs. Commissioner of Income Tax, Madras*, and also certain other decisions relating to the word "payment" and came to the conclusion that the observations in *T. Sundaram Chettiar Vs. Commissioner of Income Tax, Madras*, were clearly distinguishable. The later Division Bench held that in the earlier case, there was a factual payment of loan by the company to the shareholder at the first instance. It was felt that there was no need for actual payment because the assessee himself had agreed to the continuation of the jural relationship of debtor and creditor between the assessee and the company.

In the latter case, the Division Bench observed as follows (page 24) :

But, in the case on hand, there is no payment of loan as such and the call amounts due by the assessee were treated as having been paid up by making a credit entry in favour of the assessee-family. It is difficult to treat this as the actual payment by way of a loan. We are, therefore, of the view that the sum of Rs. 1,65,000 cannot be treated as payment by way of loan by the company to the assessee-family and that, therefore, section 2(6A)(e) could not be invoked.

8. The facts of the present case are closer to the facts of the case in *G.R. Govindarajulu Naidu and Another Vs. Commissioner of Income Tax*, and we are, therefore, inclined to follow the observation of the Division Bench mentioned above.

9. That apart, the provision of law, namely, section 2(22)(e), which we have already extracted above, says that by a fiction dividend is made to include any payment by a company, etc. Therefore, it is difficult for us to introduce another fiction in respect of the words "payment by the company" by construing even a transfer entry as amounting to payment. In other words, when section 2(22)(e) itself introduces a fiction, it is improper for us to introduce another fiction and construe a payment as equivalent to a constructive payment. In this view of the matter, we are not inclined to accept the arguments advanced on behalf of the Revenue and following the decision in *G.R. Govindarajulu Naidu and Another Vs. Commissioner of Income Tax*, we answer the reference in the affirmative and against the Revenue.