
(2013) 04 GUJ CK 0052

Gujarat High Court

Case No: Tax Appeal No. 936 of 2012

Commissioner of
Income Tax

APPELLANT

Vs

Krupeshbhai N. Patel

RESPONDENT

Date of Decision: April 29, 2013

Acts Referred:

- Companies Act, 1956 - Section 108, 153
- Income Tax Act, 1961 - Section 2(22)(e)

Citation: (2013) 359 ITR 504 : (2013) 216 TAXMAN 61

Hon'ble Judges: S.G. Gokani, J; Akil Abdul Hamid Kureshi, J

Bench: Division Bench

Advocate: Mauna M. Bhatt, for the Appellant; Manish J. Shah, for the Respondent

Judgement

@JUDGMENTTAG-ORDER

1. Revenue is in appeal against the judgment of the Income Tax Appellate Tribunal dated 29.06.2012 raising following questions for our-Consideration:

(A) Whether the Appellate Tribunal has substantially erred on facts and in law in deleting the addition of Rs. 27,66,022/- made on account of deemed dividend, u/s. 2(22)(e) of the Act?

(B) Whether the order of the Appellate Tribunal is not perverse inasmuch as it failed to take cognizance of the fact that at the time of search action, the assessee failed to disclose the existence of any trust and the assessee, in the statement recorded by DDIT(Inv), Baroda on 19.03.2009 even agreed to pay taxes on the deemed dividend u/s. 2(22)(e) of the IT Act?

Though two separate questions have been framed, issue is single namely of the decision of the Assessing Officer to tax a certain income in the hands of the respondent-assessee

as a deemed dividend u/s 2(22)(e) of the income tax Act, 1961 ("the Act" for short).

2. For the assessment year 2006-07, the Assessing Officer inquired with the assessee regarding the assessee's shareholding in a company namely M/s. Amod Stampings Pvt. Ltd. (hereinafter to be referred to as "the said company"). It appears that during course of a search operation carried out by the department, it was noticed that the said company had given loans to various members including the assessee having shareholding, and voting powers exceeding 10%. The assessee was, during the search operation, confronted with such shareholding pattern and the loans advanced. Assessee wrote a letter dated 19.03.2009 agreeing to accept a sum of Rs. 881.71 lakhs as deemed dividend u/s 2(22)(e) of the Act. During the course of the assessment proceedings, however, it was asserted before the Assessing Officer that a trust was created on 16.01.2005, in which, the respondent-assessee and other family members had settled an aggregate of 5.12 lakhs of equity shares of the said company held by them. It was the case of the assessee that he did not hold any beneficial interest in the shares on the said company having more than 10% of the total voting power. He, therefore, contended that Section 2(22)(e) of the Act had no application.

3. The Assessing Officer, however, gave detailed reasons to reject such a stand. He was of the opinion that neither the shares of the said company were transferred nor any dividend was passed on to the trust. These facts led to a conclusion that the trust was not in existence at all.

4. Assessee carried the matter in appeal. CIT(A) dismissed such appeal primarily on the following grounds:

(viii) Admittedly,

(a) the trust does not have any bank account.

(b) Trust does not have any income whatsoever other than the shares of M/s. Amod Stampings Pvt. Ltd. settled in its favour as per the Trust-Deed dated 18.11.2005.

(c) No return of income has been filed, as there is no income of the Trust.

(d) no dividend is also received by the Trust since M/s. Amod Stampings Pvt. Ltd. has not declared any dividend.

(e) The trust is not registered with any other authority as it is not required.

(f) However, Trust deed is executed on 16.11.2005 on the stamp paper of valid denomination and is notarized.

(g) The objective of the trust is to meet the education and medical costs of the children of the family.

(h) The shares settled in favour of the Trust are still in the name of the trustees including the appellant and they are holding it as Trustees.

5. Assessee thereupon approached the Tribunal. The Tribunal, by the impugned judgment, allowed such appeal making following observations:

11.1 In the light of the above legal discussion, we have examined the facts of the case. The area of dispute is the existence of a "declaration of trust claimed to be executed on 6/11/2005. Undisputedly, search was conducted on 11/02/2009. Revenue's main objection is that on the date of search the said document was not recovered. However, the vehement contention of the assessee is that this documents has duly been executed on a stamp paper of Rs. 100/- on 16/11/2005. Further, it has also been strongly contested that the said document was duly notarized by a notary, who has authenticated its execution. Rather it was alleged that no attempt was made by the Revenue to negate the validity of the said document, Revenue Department could have examined the veracity of the said document by investigating the records of the stamp vendor, as also the said notary. A legal document which is executed in the presence of a duly authorised person, i.e. notary, an appointed legal entity by Government of India, has to be acknowledged and to be accepted as true and correct unless and until proved otherwise. From the side of the assessee, it was strongly contested that to corroborate such declaration, reliance is also placed on the minutes of the meeting of the Board of Directors of M/s. Amod Stampings Pvt. Ltd. held on 22/12/2005, wherein it was resolved as under-

Resolved further that the copy of the said resolution be submitted to the Bank.

03. Settlement of Shares Held by N.S. Patel Family's Children Trust.

The Chairman placed before the board information received from the three shareholders of the Company being Smt. Lalitaben N. Patel, Shri Navinbhai N. Patel and Shri Krupeshbhai N. Patel about settlement of 5,12,000 equity shares of Rs. 10 each fully paid up held by them in favour of M/s. N. S. Patel Family's Children Trust. The said persons have informed that they would be continuing to hold these shares, but beneficial interest in these shares would be those of the trust so settled and its beneficiaries.

11.2 Our attention has also been drawn on the terms through which the settlors have settled the shares in favour of the beneficiaries vide N.S. Patel Family's Children Trust-DECLARATION OF TRUST dated 16th day of November-2005 as follows-

Whereas

(i) the Settlors are members of the family of Late Shri Narharibhai Somabhai Patel and are presently shareholders of one company by the name of M/s. Amod Stampings Private Limited, a Company formed and registered under the provisions of the Companies Act, 1956 and having its register office at Gujarat Spun Pipe Compound, P.O. Samiala, Padra Road, Vadodara 391 410 ("the Company");

(ii) the Settlers are desirous of ensuring that the children of the family, who are presently pursuing education or are proposing to settle in business, do not have any scarcity of funds for their future pursuits, primarily being education or commencing new business;

(iii) the Settlers have decided, for natural love and affection, to settle some of the shares of the Company upon a trust for the benefit of the children of the family to be governed by the provisions of this Declaration of the Trust;

Terms and Conditions of Settlement

1. In consideration of natural love and affection, the Settlers do hereby settle the following equity shares held by the respective shareholders for the benefit of the Beneficiaries as described in this Declaration:

The shares of the Company are equity shares of Rs. 10 each fully paid up and the same are referred as the "Settled Assets".

2. The Settlers shall act as the First Trustees, unless and until other persons are appointed as the Trustees in accordance with the Declaration and the respective Settlor shall continue to hold the part of the Settled Assets in their name, but shall not have any beneficial interest in the said asset shall stand vested in the beneficiaries in accordance with this Declaration;

11.3 After the search, Dy. Commissioner of Investigation has also enquired about this issue and vide submission dated 22/04/2009, the assessee has furnished the complete details of the said declaration. In respect of few other queries, explanation of the assessee was that in the absence of any other transaction or earning or NIL income, there was no necessity to open a bank account. Further, about the registration of the shares, it was explained that as per section 153 of the Companies Act, 1956, a company is not permitted to include the name of the Trust in the register because trusts are not required to be entered in the register. Due to this reason, the name which was earlier noted as shareholders remained the same, however through a Board meeting it was resolved to acknowledge the change in the vesting of the shares. Under the totality of the circumstances of the case and the evidence on record, we are of the view that a deeming provision has to be applied strictly, so that a fiction so created by a Statute should not cover within its ambits more than what is subscribed. A deeming provision is, therefore, to be applied restrictively, so that its application must not enlarge the scope of presumption. Rather, it has been held in the case of [L.B. Sugar Factory and Oil Mills \(P\) Ltd., Pilibhit Vs. Commissioner of Income Tax , U.P., Lucknow](#), that no authority can presume something which is not envisaged in the Act. A documentary evidence is thus nothing but affirmation of the existence of a fact and, therefore, merely on preponderance of probabilities such a documentary evidence should not be rejected. We, therefore, conclude that in the absence of any contrary material specially when we are dealing with a fiction created by a Statute, a fictional income, i.e. deemed dividend need not be taxed

in the hands of the assessee on an unestablished hypothecation. We hereby direct to delete the addition. Ground is allowed.

6. Learned counsel, Mr. Bhatt for the revenue vehemently contended that the Assessing Officer as well as the CIT(A) had examined the material on record and come to just a conclusion that the creation of the trust was not genuine. Even if the trust was created, as held, mere so-called transfer of the shares had never been acted upon. He highlighted several aspects of the matter, particularly, those projected by the CIT(A) in the appellate order to contend that the creation of the trust at best was an artificial device to avoid tax liability.

7. Counsel submitted that when the Assessing Officer and CIT(A) had examined these aspects at considerable length, the Tribunal could not have reversed such decisions without fully considering all material facts.

8. Counsel further submitted that if, as admitted by the assessee, the shares could not have been transferred, the assessee would continue to be the registered as well as the beneficial owner of the shares. The requirement of Section 2(22)(e) would thus be fulfilled and the effect thereof must be allowed to operate.

9. On the other hand, learned counsel Mr. J.P. Shah for the respondent-assessee opposed the appeal contending that looking to the materials on record when the Tribunal has come to certain findings of facts, no question of law could be stated to have arisen. He submitted that the assessee had never conceded to surrender such income for tax. He drew our attention to the communication dated 19.03.2009 in this respect.

10. Section 2(22)(e) of the Act makes a deeming provision for treating any payment by a company under certain circumstances as a dividend such provision reads as under:

(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 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 (hereinafter 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;

11. What is envisaged u/s 2(22)(e) of the Act is any payment by a company not being a company in which public are substantially invested any sum, by way of advance or loan to shareholder who happens to be a person who is a beneficial owner of shares holding not

less than 10% of the voting power or to any concerned in which such shareholder is a member or a partner in which he has a substantial interest. Thus, the payment by a company by way of advance or loan should be to a shareholder, who is the beneficial owner of the shares holding not less than 10% share of the voting power. In the present case, our inquiry does not include the percentage of the voting power since this issue is not under controversy. The question is in the present circumstances, the Tribunal could have validly come to the conclusion that the assessee was not hit by Section 2(22)(e) of the Act. In that context, we need to appreciate the Tribunal's conclusions on the basis of the requirements of the said section of the advance or loans made by the company to its shareholder and a person who was beneficial owner of the shares. To our mind, these two aspects cannot be separated and rightly therefore gave its due weight-age by the Tribunal. Learned counsel, Mr. Bhatt did contend that when the shares were not transferred in the name of the trust, the assessee continued to be the shareholder and also must be seen to have retained its beneficial ownership of the shares. To this aspect, we do not agree. If it was otherwise demonstrated that the total interest in the shares was divested and settled in a trust, the later requirement of Section 2(22)(e) namely that of the assessee being a beneficial owner of the share, would not be satisfied. Our attention was drawn to Sections 108 and 153 of the Companies Act but which, in our opinion, would apply in different situations. Section 108 of the Companies Act pertains to registration of shares and requirement to be fulfilled. Section 153 provides that a trust shall not be entered on the registration of the members or of debenture holders.

12. With this background, we may appreciate the Tribunal's decision. As noted, the revenue authorities had formed an opinion that the creation of trust was not genuine. This was primarily on the basis that no trust-deed was found at the time of search. Even the assessee agreed to pay tax on such deemed dividend. The trust-deed was not registered or acted upon by creating a bank account or carrying on any activity by the trust. The Tribunal, on the other hand, was influenced by the other factors namely that the trust deed was created on a stamp paper in the year 2005 i.e. nearly four years before the date of the search; that the same was duly notarized. The department did not carry out any inquiries with the notary public to establish the non-genuineness of the trust deed. The Tribunal also took into account other facts, such as that the Companies Act would not permit transfer of the shares in the name of the trust; that there was no dividend declared by the Company and that the Trust, therefore, did not receive any income so as either to open a bank account or to file a return. Equally importantly the mere fact that the trust-deed was not found at the time of search and that later on the assessee agreed to surrender tax on such dividend income did not convince the Tribunal. We have ourselves perused the said letter dated 19.03.2009. In such letter the assessee had stated that he had agreed to take such a stand to avoid any litigation. He however held a belief that the said income was not chargeable to tax as a deemed dividend. Creation of a trust and settlement of the shares in such trust were also mentioned in such communication. It was stated that the authority had expressed the opinion that since there was no financial transaction in the name of the trust and that the trust was not registered, it would not be

possible to accept that the shares were settled in the said trust. It was for these reasons that the income was being surrendered.

13. In our opinion, the entire issue is based on appreciation of materials on record. Upon consideration of various factors if the Tribunal came to the conclusion that the trust was genuine and that the view of the revenue authorities that the same was never acted upon was not correct, such findings cannot be stated to be perverse so as to give rise to a question of law. The Tax appeal is therefore, dismissed.