

**IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCHES "A", BANGALORE**

Before Shri Chandra Poojari, AM & Shri George George K, JM

ITA No.2644/Bang/2019 : Asst.Year 2014-2015

M/s.Davanam Constructions Private Limited, No.148 Surveyor Street, Basavanagudi Bengaluru - 560 004. PAN : AABCD3880H.	v.	The Assistant Commissioner of Income-tax, Circle 2(1)(2) Bengaluru.
(Appellant)		(Respondent)

Appellant by : Sri.Nitish Ranjan, CA
Respondent by : Sri.Sankar Ganesh K, JCIT-DR

Date of Hearing : 19.05.2022	Date of Pronouncement : 27.05.2022
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ORDER

Per George George K, JM :

This appeal at the instance of the assessee is directed against CIT(A)'s order dated 30.10.2019. The relevant assessment year is 2014-2015.

2. The grounds raised read as follows:-

"1. The order of the CIT(A) is opposed to law, facts and circumstances of the case.

2. The order is passed in haste, without providing sufficient and reasonable opportunity of being heard.

3. The order is passed against the principle of natural justice and thus liable to be quashed.

4. The learned Assessing Officer has erroneously invoked the provisions of section 2(22)(e) and making the impugned addition and the ld.CIT(A) has erred in upholding the same.

5. The ld.CIT(A) and the ld.AO has failed to comprehend the fact that the appellant had received the impugned amount of Rs.2,00,75,000/- from M/s.Kausthubha Project Pvt. Ltd.

towards advance for the project at Okalipuram and the same was received solely on the grounds of commercial expediency.

6. *Notwithstanding the above, the ld.CIT(A) has failed to appreciate the fact that the impugned issues are beyond the scope of the "Limited Scrutiny" thereby rendering it void ab initio under section 143 of the Act.*

7. *Without prejudice to the above, it is noteworthy that the amount to be brought to tax in the impugned situation shall not exceed the amount received during the assessment year in question, which in the instant case is Rs.85,75,000/-. Therefore, the ld.AO has made the impugned addition in a haste, without the application of mind."*

3. The brief facts of the case are as follows:

The assessee is a company carrying on its business as builder and developer of properties. For the assessment year 2014-2015, the return of income was filed on 30.09.2014 declaring a loss of Rs.2,21,95,569. The assessment was selected for scrutiny by issuance of notice u/s 143(2) of the I.T.Act. The assessment u/s 143(3) of the I.T.Act was completed vide order dated 16.12.2016 determining a net loss of Rs.8,01,457. One of the additions made in the assessment completed u/s 143(3) of the I.T.Act was u/s 2(22)(e) of the I.T.Act amounting to Rs.2,00,75,000. The A.O. held that the payment is made by a closely held company, i.e., M/s.Kausthubha Project Private Limited (KPPL), to the assessee and assessee is a shareholder having substantial interest in the payers company (The assessee is having 74.5% share in KPPL). Further, it was observed by the A.O. that KPPL had accumulated profits to the extent of Rs.4,95,79,456 as on 31.03.2013 while a payment to the extent of Rs.2,00,75,000 was to the assessee. Therefore, it was

concluded by the A.O. that provisions of section 2(22)(e) of the I.T.Act is applicable.

4. Aggrieved by the order of the assessment u/s 143(3) of the I.T.Act, the assessee filed an appeal before the first appellate authority. It was submitted that since the case was selected for limited scrutiny, the A.O. has gone beyond the scope of limited scrutiny assessment and has made addition u/s 2(22)(e) of the I.T.Act, without the approval of the competent authority.

5. As regards the addition on merits made u/s 2(22)(e) of the I.T.Act, the assessee submitted that the amount received from KPPL amounting to Rs.2,00,75,000 was towards advance for purchase of a property in the proposed project at Oklipuram, being jointly developed by the assessee and M/s.Pacific Heights. It was submitted that the same has been disclosed in the audited balance sheet as on 31.03.2014. It was contended that the amount advanced are purely commercial in nature. In this context, the learned AR relied on various judicial pronouncements, which are reproduced at para 5 of the impugned order of the CIT(A). The assessee also raised an alternate contention that if at all the addition is to be made u/s 2(22)(e) of the I.T.Act, the amount received during the financial year, i.e., Rs.85,75,000 only ought to be considered and not the amount received in the earlier year.

6. The CIT(A), however, rejected the contentions of the assessee. The CIT(A) held that the assessee could not establish that it has a regular business connection with

Kausthubha Project Private Limited and how the impugned transaction would amount to trade advance or any commercial expediency involved in it. As regards the alternative contention of the assessee, the CIT(A) held that section 2(22)(e) of the I.T.Act does not specify that payment should be received in the same financial year relevant to the assessment year under consideration. The CIT(A), however, did not adjudicate the assessee's contention that the A.O. has erred in going beyond the scope of limited scrutiny assessment to make addition u/s 2(22)(e) of the I.T.Act.

7. Aggrieved by the order of the first appellate authority, the assessee has filed this appeal before the Tribunal. The assessee has filed two sets of paper book (one comprising of 68 pages and the other comprising of 101 pages). Enclosed in the paper book are the financial statement of the assessee for the relevant assessment year, financial statement of Kausthubha Project Private Limited, JDA agreement entered between the assessee and Pacific Heights (JDA dated 06.11.2014), agreement to sale dated 14.02.2012 between the assessee and M/s.Kausthabha Projects Private Limited, the case laws relied on, etc.

8. The learned Departmental Representative strongly supported the orders of the Income Tax Authorities.

9. We have heard rival submissions and perused the material on record. The first contention of the assessee is that the A.O. has erred in going beyond the "limited scrutiny" assessment and making an addition u/s 2(22)(e) of the

I.T.Act, without prior approval from the competent authority. This contention of the assessee is to be rejected, since we find that the PCIT vide letter dated 06.12.2016 had granted approval to the A.O. for converting the “limited scrutiny” assessment to a “complete scrutiny” assessment. A copy of the notice issued u/s 143(2) of the I.T.Act and the approval letter dated 06.12.2016 of the PCIT are placed on record. Therefore, ground 6 is rejected.

9.1 As regards the contention of the assessee on merits of the addition, it is necessary to examine the relevant section, namely, section 2(22)(e) of the I.T.Act, which reads as follow:-

2(22) "dividend" includes—

- (a) any distribution by a company of accumulated profits, whether capitalised or not, if such distribution entails the release by the company to its shareholders of all or any part of the assets of the company ;
- (b) any distribution to its shareholders by a company of debentures, debenture-stock, or deposit certificates in any form, whether with or without interest, and any distribution to its preference shareholders of shares by way of bonus, to the extent to which the company possesses accumulated profits, whether capitalised or not ;
- (c) any distribution made to the shareholders of a company on its liquidation, to the extent to which the distribution is attributable to the accumulated profits of the company immediately before its liquidation, whether capitalised or not ;
- (d) any distribution to its shareholders by a company on the reduction of its capital, to the extent to which the company possesses accumulated profits which arose after the end of the previous year ending next before the 1st day of April, 1933, whether such accumulated profits have been capitalised or not ;
- (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—

- (i) a distribution made in accordance with sub-clause (c) or sub-clause (d) in respect of any share issued for full cash consideration, where the holder of the share is not entitled in the event of liquidation to participate in the surplus assets ;
- (ia) a distribution made in accordance with sub-clause (c) or sub-clause (d) in so far as such distribution is attributable to the capitalised profits of the company representing bonus shares allotted to its equity shareholders after the 31st day of March, 1964, and before the 1st day of April, 1965;
- (ii) any advance or loan made to a shareholder or the said concern by a company in the ordinary course of its business, where the lending of money is a substantial part of the business of the company ;
- (iii) any dividend paid by a company which is set off by the company against the whole or any part of any sum previously paid by it and treated as a dividend within the meaning of sub-clause (e), to the extent to which it is so set off;
- (iv) any payment made by a company on purchase of its own shares from a shareholder in accordance with the provisions of section 77A^{14a} of the Companies Act, 1956 (1 of 1956);
- (v) any distribution of shares pursuant to a demerger by the resulting company to the shareholders of the demerged company (whether or not there is a reduction of capital in the demerged company).

Explanation 1.—The expression "accumulated profits", wherever it occurs in this clause, shall not include capital gains arising before the 1st day of April, 1946, or after the 31st day of March, 1948, and before the 1st day of April, 1956.

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 2A.—In the case of an amalgamated company, the accumulated profits, whether capitalised or not, or loss, as the case may be, shall be increased by the accumulated profits, whether capitalised or not, of the amalgamating company on the date of amalgamation.

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 ;

9.2 The aforementioned provision shows that a payment would acquire the attributes of a dividend within the meaning of the said provision if the following conditions are fulfilled:-

(i) The company making the payment is one in which public are not substantially interested.

(ii) Money should be paid by the company to a shareholder holding not less than ten per cent (10%) of the voting power of the said company. It would make no difference if the payment was out of the assets of the company or otherwise.

(iii) The money should be paid either by way of an advance or loan or it may be "any payment" which the company may make on behalf of or for the individual benefit of any shareholder or also to any concern in which such shareholder is a member or a partner and in which he is substantially interested.

(iv) And lastly, the limiting factor being that these payments must be, to the extent of accumulated profits, possessed by such a company.

9.3 Thus, it is apparent that the provisions of the Section 2(22)(e) of the Act seeks to tax the loans and advances made to shareholders by a closely held company as deemed dividends in the hands of the shareholders. This is intended to prevent tax evasion in situations where closely held companies distribute accumulated profit as loans or advances which are not chargeable to tax under the Act, instead of distributing it as dividends which is chargeable to tax under the Act. Further it is also evident from the said section that one of the sub-clause in section 2(22)(e) provides that where

loans or advance are given to the registered shareholder for the business purposes of the payer company and also lending of money is a substantial part of its business, then such payment will not be-treated as deemed dividend.

9.4 The limited contention of the learned AR is that the advance received from M/s.Kausthubha Project Private Limited (KPPL) by the assessee is in the nature of trade advance against the flat being built and it is submitted that the said amount falls within the exclusion as laid down under clause (ii) of section 2(22)(e) of the I.T.Act, and therefore, the same cannot be considered as deemed dividend under the said section.

9.5 Let us examine the contention of the assessee based on the facts on record. The assessee holds 74.5% share of KPPL, a company in which public are not substantially interested and the accumulated profits as on 31.03.2013 of KPPL far exceeded the advances to assessee. Therefore, in the normal course, the provision of section 2(22)(e) of the I.T.Act would be attracted. However, the further question is whether exclusion as laid down under clause (ii) of section 2(22)(e) of the I.T.Act is applicable. The assessee submitted that it had entered into an agreement dated 14.02.2012 with KPPL for a sale of property which is a flat to be built in Okalipuram for a sum of Rs.2,25,00,000 (agreement for sale produced at pages 82 to 89 of the paper book-1). According to the assessee, as per the terms of the sale agreement, it received a sum of Rs.2,13,75,000 as advance against such property on various

dates between 14.02.2012 and 13.06.2013, as detailed below:-

Sl. No.	Date	Bank	Mode	Amount (Rs.)
1	14.02.2012	HDFC Bank	Cheque (Cheque No.572496)	24,60,000
2.	17.03.2012	HDFC Bank	Cheque (Cheque No.572492)	24,60,000
3.	16.05.2012	SBI	Online	18,00,000
4.	16.05.2012	SBI	Online	12,80,000
5.	20.06.2012	SBI	Online	12,00,000
6.	20.06.2012	SBI	Online	12,60,000
7.	28.02.2013	HDFC Bank	Cheque (Cheque No.686540)	23,40,000
8.	13.06.2013	SBI	Online	85,75,000

9.6 It is interesting to note that the flat which the assessee is seeking to sell is not in existence at the time of receipt of advance from KPPL (first advance on 14.02.2012). The assessee has a parcel of land at Okalipuram. The assessee had entered into JDA only on 06.11.2014 with M/s. Pacific Heights for development of the said land into a multistoried apartment complex. One residential unit in Pacific Heights is sought to be sold to KPPL vide agreement for sale entered between the assessee and KPPL on 14.02.2012. As mentioned earlier, the first date of advance from KPPL to the assessee is on 14.02.2012, i.e., much prior to the JDA which was executed on 06.11.2014. Therefore, on the facts of the present case, the sale of a residential flat to KPPL is a story set up to circumvent the provisions of section 2(22)(e) of the I.T.Act. The assessee has not produced any evidence / material to show that the agreement to sell of a flat to KPPL has actually

fructified in a sale deed. Therefore, on the facts of the instant case, the amount received by the assessee from KPPL is nothing but deemed dividend liable to the taxed u/s 2(22)(e) of the I.T.Act. It is ordered accordingly.

9.7 As regards the alternative contention of the assessee that the amount received in the current year alone can be brought to tax, we find that the Bangalore Bench of the ITAT in the case of Assetz Infrastructure Pvt. Ltd. v. DCIT in ITA No.563/Bang/2019 (order dated 23.03.2022) has held as follows:-

“7. The next contention of the Ld. A.R. is that the Ledger account of subsidiary company is having “opening credit balance of Rs.2,86,92,744/- as on 01-04-2013 should be reduced from the accumulated profits. Elaborating the same, the Ld A.R submitted that the AO could have assessed loans received in the earlier years as deemed dividend in those years itself. Hence, the opening balance cited above should be reduced from the accumulated profit for the purpose of determining the deemed dividend u/s 2(22)(e) of the Act. In support of this contention, the Ld. A.R. placed his reliance on the decision rendered by Hon’ble Supreme Court in the case of CIT vs. G Narasimhan (1999)236 ITR 327 and also the decision rendered by Visakhapatnam Bench of ITAT in the case of P. Satya Prasad Vs. ITO (2013) 31 Taxmann.com 267. The Hon’ble Supreme Court in the above said case has held that when a loan given by a company to a shareholder is treated as deemed dividend u/s 2(22)(e) of the Act, it has to be treated as payment made from out of the accumulated profits of the company and hence the same should be adjusted against accumulated profits. It was further held that whenever accumulated profits of the company are required to be determined, such an adjustment will have to be made. The above said principle was followed by the Visakhapatnam bench of Tribunal in the case of P. Satya Prasad (supra).

8. We heard Ld. D.R. on this issue and perused the record. We notice that the Visakhapatnam bench in the case of P. Satya Prasad (supra) had followed the decision rendered by Cochin bench of Tribunal in the case of Gordhan Das Khimji (1985) 11 ITD 158, wherein it was held that the deemed dividend assessable in any of the earlier years has to be reduced from the accumulated profits even it was not assessed in that year. The discussion made by the Tribunal in the case of P Satya Prasad (supra) are extracted below:-

“14. The contention of the assessee is that the amount of deemed dividend, which should have been assessed in any of the earlier years, should also be reduced from the accumulated profit even if it was not assessed as deemed dividend in that year. For this proposition, the Ld A.R has placed reliance on the decision rendered by the Cochin bench of Tribunal in the case of Gordhandas Khimji (supra) and also the decision rendered by the Delhi bench of Tribunal in the case of A.R. Chadha & Co India (P.) Ltd. (supra). The Ld CIT(A), as stated earlier, refused to follow the said decisions on the ground that the department is going to gain anything by postponing the taxability of deemed dividend. Further, the Learned CIT(A) has observed that the Cochin bench did not consider Explanation 2 to sec. 2(22)(e) of the Act. We have already noticed that the Ahmedabad bench of the Tribunal has explained about the area of operation of Explanation 2 to sec. 2(22)(e) of the Act and we have also concurred with the view that the accumulated profit does not include current years profit from business. Accordingly, in our view, the Explanation 2 to sec. 2(22)(e) shall not alter the taxability of the dividend in the right year of assessment.

15. The Hon'ble Supreme Court has held in the case of Miss P. Sarada (supra), that the legal fiction embodied in sec. 2(22)(e) comes into play as soon as monies were paid by a company. The very same view was expressed by the Apex Court in the case of Smt. Tarulata Shyam v. CIT [1977] 108 ITR 345. The Cochin bench of Tribunal in the case of Gordhandas Khimji (supra) considered the decision of Hon'ble Supreme Court in the case of Tarulata Shyam (supra) and has expressed the view that the deemed dividend assessable in any of the earlier years has to be reduced from the accumulated profits, even if it was not assessed in that year. The relevant observations made by the Cochin bench are extracted below:-

"11. In Smt. Tarulata Shyam's case (supra), it was held by the Supreme Court that the statutory fiction created by s. 2(6A)(e) would come into operation at the time of payment of advance or loan to a shareholder and tax is attracted to the loan or advance to the extent to which the company possesses accumulated profits the moment the loan or advance is received, and even if the loan or advance ceases to be outstanding at the end of the previous year, it can still be deemed to be 'dividend' if the conditions of the section are satisfied. It was also observed that the language of the section is clear and unambiguous and that there is no scope of importing into the statute words which are not there and that once it is shown that the case of the assessee comes within the letter of the law, he must be taxed, however great the hardship may appear to the judicial mind to be. ...

13. None of the discussions referred to above are directly on the point. But the line of discussion in those decisions gives some indication with

regard to the correct position. We are unable to hold that loans and advances will become deemed dividends only when the Department chooses to treat the same as such and brings the same to tax as dividend. The section is not worded as an enabling section by which the Department can treat the loans and advances as deemed dividends. The section does not say that the amount will become deemed dividend only if it has been assessed as such. On the other hand, the provision is a clause in the inclusive definition, by which advances and loans are constituted as dividends. The moment an advance or loan satisfying the conditions of the section is made, it would become a dividend and it is immaterial whether the department has assessed the same as dividend or not. The decisions referred to above indicate that the deemed dividend has to be worked out on the basis of the conditions obtaining at the time when the loans or advances are made. In the case of Smt. Tarulata Shyam (supra), the Supreme Court observed that the statutory fiction created by the section would come into operation at the time of the payment of advance or loan. Similarly, the observations in the case of P.K. Badani (supra) (76 ITR 369) (Bom) would indicate that the accumulated profits should be reduced by the amount of loan or advance, immediately on making such loan or advance. Only if this is done, the subsequent loans or advances can be tested by verifying the accumulated profits on the dates on which they are made. As pointed out in the decision referred above, the repayments of the advances or loans will have no effect either on the advances or loan treated as dividend or on the accumulated profits as reduced by such advance or loan. As such, it does not seem to be neither practicable nor proper to postpone the whole process of ascertaining the accumulated profits till the Department chooses to treat a particular advance as deemed dividend. If the contention of the Department is accepted, then if the ITO ignores the advances in earlier years and then goes down on the assessee in an assessment year in which he has drawn substantial advances, it will amount to allowing the Department to take advantage of its omissions to assess the earlier loans and advances as deemed dividends and to allow such omissions to bloat the accumulated profits, so that the whole of the large advances taken in the last assessment year are converted into deemed dividends. As rightly pointed out by the CIT(A), the advances or loans in the earlier assessment years should be treated as dividend which the Department omitted to assess. If so, it follows that the accumulated profits should be reduced by the earlier loans or advances in spite of the fact that they were not assessed to tax as deemed dividends by the Department."

It is a well settled proposition of law that an income pertaining to a particular assessment year can be assessed in that year only. For example, the income pertaining to the assessment year 2005-06 can be assessed only in that year, i.e., the said income cannot be assessed in any other assessment year, even if the tax authorities wish to do so. Hence, the assessee cannot be compelled to pay tax on the income which was omitted

to be assessed in an earlier year, by assessing the said income in any other assessment year. Accordingly, we are inclined to follow the decision rendered by the Cochin bench in the case referred supra. Accordingly, the loan given by the company in the immediately preceding year, i.e., assessment year 2006-07, should have been assessed as deemed dividend in accordance with the provisions of sec. 2(22)(e) in that year. The deemed dividend so assessable in that year is liable to be deducted from the amount of "accumulated profits" for the purpose of computing the deemed dividend during the year under consideration.""

Accordingly we accept the contention of the assessee that the deemed dividend, if any, assessable in any of the years is required to be reduced from the accumulated profits, even if it was not assessed so by the AO in any of the earlier years.

9. In the instant case, the opening credit balance available in the subsidiary company's ledger account was Rs.2,86,92,744/-. As per the principle discussed above, the deemed dividend, if any, assessable/assessed in any of the earlier years is required to be reduced from the "accumulated profits" for the purpose of determining the accumulated profits in relation to the loan amount received from the subsidiary company during the year under consideration. However, we are of the view that the details of amount of deemed dividend, if any, assessable/assessed are required to be determined/verified by the AO."

9.8 In the light of the above order of the ITAT in the case of Assets Infrastructure Pvt. Ltd. v. DCIT (supra), we direct the A.O. to examine the alternative plea and take a decision in accordance with law.

10. In the result, the appeal filed by the assessee is partly allowed for statistical purposes.

Order pronounced on this 27th day of May, 2022.

Sd/-
(Chandra Poojari)
ACCOUNTANT MEMBER

Sd/-
(George George K)
JUDICIAL MEMBER

Bangalore; Dated : 27th May, 2022.
Devadas G*

Copy to :

1. The Appellant.
2. The Respondent.
3. The CIT(A)-2, Bangalore.
4. The Pr.CIT-2, Bangalore.
5. The DR, ITAT, Bengaluru.
6. Guard File.

Asst.Registrar/ITAT, Bangalore