

Rameshwar Lal Sanwarmal vs Commissioner Of Income-Tax, Assam on 5 December, 1979

Equivalent citations: 1980 AIR 372, 1980 SCR (2) 369, AIR 1980 SUPREME COURT 372, 1980 (2) SCC 371, AIR 1980 SUPREME COURT 373, 1980 TAX. L. R. 193, 1980 UJ(SC) 276, (1980) 1 SCJ 420, 1980 UPTC 408, (1980) 2 SCR 369 (SC), (1980) 3 TAXMAN 1, (1980) 14 CURTAXREP 372, (1980) 2 SCWR 68

Author: P.N. Bhagwati

Bench: P.N. Bhagwati, R.S. Pathak

PETITIONER:
RAMESHWAR LAL SANWARMAL

Vs.

RESPONDENT:
COMMISSIONER OF INCOME-TAX, ASSAM

DATE OF JUDGMENT 05/12/1979

BENCH:
BHAGWATI, P.N.

BENCH:
BHAGWATI, P.N.
PATHAK, R.S.

CITATION:
1980 AIR 372 1980 SCR (2) 369
1980 SCC (2) 371

ACT:

Indian Income Tax Act 1922-Section 2(Income) (e)-Scope of-Shares in a company registered in the name of Karta of HUF-Company advanced loans to business concerns of HUF-loans-if "deemed dividend".

HEADNOTE:

The assessee, a Hindu Undivided Family, owned certain shares in a private limited company in which the public were not substantially interested. Though the shares were beneficially owned by the Hindu Undivided Family, they stood registered in the name of its Karta. From out of its accumulated profits the company gave loans, in the assessment year 1956-57. to three business concerns which

were owned by The assessee. Section 2(6) (e) of the Indian Income Tax Act, 1922 provided that where a private company in which public were not substantially interested gave loans to its shareholders from out of its accumulated profits such loan would be treated as "deemed dividend" in the hands of the shareholders.

The Income Tax officer treated the loans as "deemed dividend" in the hands of the assessee on the ground that though the shares stood in the name of the Karta, the assessee being the beneficial owner, the conditions of section 2(6A)-(e) were satisfied. This view of the Income Tax officer was upheld by the Appellate Assistant Commissioner.

The Appellate Tribunal rejected the contentions of the assessee that the loans could not be taxed as "deemed dividend" in its hands because it was not the registered owner of the shares; and (2) assuming that they could be treated as "deemed dividend" they could be taxed only in the hands of the karta. The Tribunal referred six questions to the High Court.

Answering two out of the six questions, the High Court held that (1) the loans could not be treated as "deemed dividend" in the assessee's hands because the term shareholder used in the section meant only a person whose name is recorded in the company's register of shareholders and (2) even assuming that the loans were "deemed dividend" they could be taxed only in the hands of the registered shareholder (the Karta). The assessment made by the Income Tax officer was accordingly set aside.

In appeal to this Court, instead of questioning the correctness of the answers returned by the High Court the Revenue attacked only that part of the High Court's order which held that "deemed dividend" could be taxed only in the hands of the registered shareholder. Therefore the question before this Court was whether "deemed dividend" could be taxed in the hands of the beneficial owner of shares or could be brought to tax only in the hands of the registered shareholder. This Court answered that where shares are acquired with the funds of one person but are registered in the name of another it is the beneficial owner who should be taxed on the dividend on the shares and that this

370

principle applies equally to "deemed dividend" under the section. Even so, this Court discharged the answer given by the High Court in favour of the assessee and substituted an answer in favour of the Revenue.

Placing reliance on the decision of this Court in C.I.T. v. Sarathy Mudaliar (83 I.T.R. 170) where it was held that a loan advanced by a company to a beneficial owner did not fall within the mischief of section 2(6A)(e) the assessee contended that loans in this case could not be taxed as "deemed dividend" in its hands.

The Revenue on the other hand contended that (1) since in the earlier case of Rameswarlal Sanwamal (82 I.T.R. 628) this Court had answered the reference in favour of the Revenue and that decision was final the later decision in Sarathy Mudaliar's case would not be available to the assessee; (2) although the present question was not specifically considered by this Court on the earlier occasion it must be held to have been impliedly decided against the assessee and (3) that the decision in Sarathy Mudaliar's case was incorrect and should be referred to a larger bench.

^

HELD: The arguments of the Revenue are fallacious. When the Revenue came in appeal to this Court in the earlier case of Rameswarlal Sanwamal it challenged only the second part of the High Court's decision ignoring the first part. The result was that the first part of the High Court's decision that loans advanced to The business concerns of a beneficial owner of shares could not be regarded as 'deemed dividend' in his hands and that the loans in the sent case did not fall within the meaning of section 2(6A)(e) remained intact and unaffected by the decision of this Court. This Court could not have answered the first question against the assessee without over-ruling the first part of the High Court's decision. However, through inadvertence, this Court set aside the High Court's answer without considering whether this part of tile decision was right or wrong. When no contention was raised on behalf of the Revenue that even if the assessee was not a registered shareholder loans advanced to its business concerns would be "deemed dividend" in its hands and there was no occasion for this Court to consider the question, from the mere fact that an answer was given in favour of the Revenue, it cannot be said that this contention was impliedly decided in its favour. [376 C-H]

2. The proper Way of looking at the decision of this Court in Rameswarlal Sanwamal would be to regard the answer given in favour of the Revenue to be confined only to the aspect considered and decided by this Court, namely, that "deemed dividend" did not stand on any different footing from actual dividend and just as actual dividend is liable to be taxed in the hands of the beneficial owner of the shares. so too "deemed dividend" must be held liable to be taxed ill the hands of the beneficial owner. This Court did not consider whether a loan to a beneficial owner could be regarded as "deemed dividend". Therefore, this aspect of the question still remained to be answered and it was open to the assessee to contend that the loans advanced to its business concerns could not be regarded as "deemed dividend" within the meaning of the section since the assessee was not a registered shareholder. [377 A-D]

3 (1) The decision of this Court in Sarathy Mudaliar's case laid down the law correctly and there is no need to refer the case to a larger bench. The

371

question whether a loan advanced to beneficial owner of shares would be liable to be regarded as "deemed dividend" was neither raised nor considered by this Court in Rameswarlal Sanwarmal's case but came up for consideration for the first time in Sarathy Mudaliar's case only. There is thus no conflict between the two decisions, [77 E-1]

(b) It is only where a loan is advanced by a company to a registered shareholder the other conditions set out in the section are satisfied that the amount of the loan would be liable to be regarded as "deemed dividend". The amount of loan would not fall within The mischief of the section if it is granted to a beneficial owner of the shares. [378 E-F]

In the instant case the loans were advanced not to the registered shareholder but to the business concerns of the beneficial owner. Hence they could not be regarded loans advanced to a shareholder of the company within the meaning of the section. [378 H

JUDGMENT:

CIVIL APPELLATE JURISDICTION: Civil Appeal No. 133 or 1979.

Appeal by Special Leave from the Judgment and order dated 13-6-1972 of the Assam High Court in Income Tax Reference No. 2/64.

H. M. Verma and N. R. Choudhary for the Appellant. S.C. Manchanda, S.P. Nayar and Miss A. Subhashini for the Respondent.

The Judgment of the Court was delivered by BHAGWATI, J.-This appeal by special leave raises a question of law relating to the interpretation of section 2(6A) (e) of the Indian Income-Tax Act, 1922. The question is in fact concluded by a decision of this Court in Commissioner of Income-tax v. C.P. Sarathy Mudaliar but, it has been argued on behalf of the Revenue that this decision is in conflict with an earlier decision given by this Court in Commissioner of Income-tax v. Rameswarlal Sanwarmal and hence the question should be referred to a larger Bench. We shall presently consider these two decisions, but we may point out straight-away that, in our opinion, there is no conflict between these two decisions and the question is completely covered by the decision in Commissioner of Income-tax- v. C. P. Sarathy Mudaliar (supra)). The facts giving rise to the appeal are not in dispute and we may briefly state the same in order to appreciate how the question arises for determination.

The assessee is the Hindu Undivided Family of M/s. Rameswarlal Sanwarmal consisting of S. M. Saharia as manager and karta and his wife and a minor son. The assessment year with which we are concerned in the appeal is 1956-57, the relevant accounting year being the year ending Ramanavami Sambat 2012, that is, 18th April, 1956. During this assessment year, the assessee was the beneficial owner of certain shares in a private limited company called Shyam Sunder Tea Co. (P) Limited.

These shares though beneficially owned by the assessee stood in the name of S.M. Saharia in the register of shareholders of the Company. The assessee also owned 3 business concerns, namely, Nilmony Shop, Saharia & Co. and Saharia Industrial Corporation. The Company advanced loans to these 3 business concerns during the relevant assessment year and since it was a company in which public were not substantially interested, a question arose in the assessment of the assessee to income-tax, whether the loans advanced to these 3 business concerns could be regarded as "deemed dividend" of the assessee under section 2(6A)(e) of the Act? The Income-tax officer took the view that the loans advanced to the 3 business concerns were attributable to the accumulated profits of the company to the extent of Rs. 4,48,045 and since the assessee which owned the 3 business concerns was the beneficial owner of the shares standing in the name of S. M. Saharia, the conditions of section 2(6A)

(e) were satisfied and the loans were liable to be regarded as "deemed dividend" taxable in the hands of the assessee under section 2(6A) (e). The assessee preferred an appeal against the order of assessment but the Appellate Assistant Commissioner agreed with the view taken by the Income-tax officer and held that since S. M. Saharia held shares in the company as representing the assessee and the loans were advanced to the three business concerns belonging to the assessee out of the accumulated profits of the company, the Income-tax officer was justified in treating the loans as "deemed dividend" under section 2(6A) (e); and taxing them in the hands of the assessee. The matter was carried in further appeal to the Tribunal and several arguments were advanced on behalf of the assessee resisting the applicability of section 2(6A) (e), but of them, there are two which are material for our purpose and they are: first, that since the assessee was not a registered holder of shares in the company, the loans advanced to the three business concerns of the assessee could not be regarded as loans advanced to a share-holder so as to attract the applicability of section 2(6A) (e); and secondly, even if the loans could be treated as "deemed dividend" under section 2(6A) (e), they could be taxed only in the hands of S. M. Saharia, the registered shareholder and not : in the hands of the, assessee. Both these arguments were negatived by the Tribunal and so also were the other subordinate arguments and the appeal was rejected and the assessment confirmed. This led to a reference application by the assessee and on the application, five A. questions of law were referred by the Tribunal to the High Court. There were, in fact, six questions but for the purpose of the present appeal, it is not necessary to refer to the first question, since it related to the assessment year 1955-56 and it raised a point of limitation which was ultimately decided in favour of the assessee and there is no dispute about it. The other five questions related to the taxability of the loans advanced to the three business concerns of the assessee as "deemed dividend" under section 2(6A)(e) and each of these questions brought in issue different aspect of taxability. It is the first of these questions which is material and we may re- produce it as follows:

"Whether on the facts and in the circumstances of the case, and on a true interpretation of the terms of section 2(6A) (e) of the Income-tax Act, 1922, the Tribunal was right in holding that the amounts of Rs. 2,21,702 (gross) and Rs. 3,43,505 (net) were taxable as dividends in the hands of the applicant H.U.F. for the assessment year 1955-56 and 1956-57 respectively, when the shares were registered in the name of Sri S. M. Saharia, the karta of the family ?"

This question referred to both the assessment years 1955-56 and 1956-57, but we are not concerned in this appeal with the controversy relating to the assessment year 1955-56 and hence we shall confine ourselves only to the assessment year 1956-57.

Now two distinct aspects were comprised in this question and both were argued before the High Court. One was whether the loans advanced to the three business concerns of the assessee could be regarded as "deemed dividend" within the meaning of section 2(6A) (e) and the other was whether these loans, even if regarded as "deemed dividend" could be taxed in the hands of the assessee. The High Court decided both these aspects of the question in favour of the assessee and held that the word "share-holder" in section 2(6A) (e) meant registered share-holder or in other words, a shareholder whose name is recorded in the Register of the company as the holder of the shares and since the advance in the present case was made to the assessee which was not a registered share-holder, it could not be regarded as "deemed dividend" within the meaning of section 2(6A) (e) and that even if it be assumed that the advance was liable to be regarded as "deemed dividend" under section 2(6A) (e), it could be taxed as dividend income only of the registered share-holder and not Only of the assessee. This view taken by the High Court rendered it unnecessary to decide the other four questions and the High Court accordingly declined to consider them. The result of this decisions was that the assessment made by the Revenue Authorities was set aside in so far as it included the loans advanced by the company to the three business concerns of the assessee as deemed dividend and taxed it in the hands of the assessee.

The Revenue, being aggrieved by the decision of the High Court, preferred an appeal after obtaining special leave of this Court. Now it seems that through some inadvertence which is difficult to understand, the Revenue attacked only that part of the order of the High Court which held that the "deemed dividend" could be assessed to tax only in the hands of S.M. Saharia, the registered share-holder and no in the hands of the assessee which was merely the beneficial owner of the shares. Neither in the statement of case filed on its behalf nor in the course of the arguments the Revenue assailed the correctness of the view taken by the High Court that since the assessee was not a registered share holder, loans advanced to the assessee could not be regarded as "deemed dividend" under section 2(6) (e). The result was that the only question that came to be considered by this Court was whether the "deemed dividend under section 2(6A)(e) could be taxed in the hands of the beneficial owner of the shares or it could be brought to tax only in the assessment of the registered share-holder and the view taken was that where the shares acquired with the funds of one person are held ill the name of another, it is the former who is assessable to tax on the dividend on those shares and this principle would apply equally on the 'deemed dividend' under section 2(6A)(e). This Court did not consider whether the loans granted to the three business concerns o the assessee could at all be regarded as 'deemed dividend' within the meaning of section 2(6A)(e) when the assessee was not a registered share-holder and the decision of the High Court to the effect that the assessee not being a registered share-holder, the loan advanced to it advanced not be regarded as 'deemed dividend' under section 2(6A)(e) remained undisturbed. Now obviously, so long as the decision of the High Court on this point was not over-ruled, the question whether the amount of the loans was taxable as "deemed dividend" in the hands of the assessee could not be answered in favour of the Revenue. But sometimes even Homer nods and through same unfortunate inadvertence for which the counsel appearing on behalf of the assessee in that case must accept full responsibility, this

Court discharged the answer given by the High Court in favour of the assessee and in its place substituted an answer, in favour of the Revenue. This decision of the Court is reported in Commissioner of Income-tax v. Rameshwar Lal Sanwarlal (supra).

Since the first question relating to the assessment year 1956-57 was answered by this Court in favour of the Revenue, the Reference went to the High Court for consideration of the remaining questions that had not been answered by the High Court. It appears that at the hearing of the Reference the first two out of the remaining four questions were not pressed on behalf of the assessee and only the last two questions were argued before the High Court. Both these questions were considered by the High Court and they were answered in favour of the Revenue and against the assessee. The assessee thereupon preferred the present appeal after obtaining special leave from this Court.

There is only one contention advanced on behalf of the assessee in support of the appeal, namely, that the amounts of the loans advanced to the three business concerns of the assessee could not be regarded as 'deemed dividend' within the meaning of section 2(6A)(e) since the assessee was not a registered share-holder of the company. This contention was sought to be supported by the decision of this Court in Commissioner of Income-tax v. C.P. Sarathy Mudaliar (supra). Now there can be no doubt that the decision of this Court in C.I.T. v. C.P. Sarathy Mudaliar (supra) lays down that it is only where a loan is advanced by a company to a registered share-holder out of its accumulated profits that it would be liable to be regarded as 'deemed dividend' under sec. 2(6A)(e) and a loan to a beneficial owner of the share does not come within the mischief of that section and if this decision represents the correct law on the subject, the amounts of loans advanced to the three business concerns of the assessee would not possibly be brought within the net of taxation as 'deemed dividend'. But the argument urged on behalf of the Revenue was that it was not open to the assessee to raise this contention based on the decision in Commissioner of Income-tax v. C. P. Sarathy Mudaliar (supra), since it was covered by the first question which had already been answered in favour of the Revenue by this Court. The Revenue conceded that this contention was not specifically raised before the Court when the first question came to be considered but it must be held to have been impliedly decided against the assessee, since the first question could not be answered in favour of the Revenue on any other hypothesis. This argument of the Revenue does appear to be very plausible at first blush, but if it is scrutinised closely it will be apparent that it is fallacious and cannot be accepted. The most important circumstance which it ignores is that when the Reference was first heard by the High Court, the first question was decided in favour of the assessee on two counts, one was that since the assessee was not a registered share-holder of the company, the loans advanced to the three business concerns of the assessee could not be regarded as 'deemed dividend' within the meaning of section 2(6A) (e) and the other was that even if they could be treated as 'deemed dividend' under section 2(5A) (e), they could be taxed only in the hands of S. M. Saharya, the registered share-holder and not in the hands of the assessee who was merely a beneficial owner of the shares. When the Revenue preferred an appeal against the judgment of the High Court, the Revenue should have assailed the decision of the High Court in both its limbs, but through some inadvertence which is difficult to understand, the Revenue challenged by the second limb of the decision ignoring completely the first. The result was that the decision of the High Court that the amounts of loans advanced to the three business concerns of the assessee did not fall within the definition of 'deemed dividend' in section 2(6A)(e) remained intact and unaffected by the decision of

this Court in the appeal. Now, it is true that this Court could not have answered the first question against the assessee without over-ruling this part of the decision or the High Court, but through some unfortunate error, this Court set aside the answer given by the High Court in favour of the assessee without considering whether this part of the decision of the High Court was right or wrong. When no contention was raised on behalf of the Revenue before this Court that the decision of the High Court on this point was wrong and that even though the assessee was not a registered shareholder, the amounts of loans advanced to the three business concerns of the assessee were still liable to be regarded as "deemed dividend" under section 2(6A) (e) and no such contention formed the subject-matter of discussion before this Court and this Court had, therefore, no occasion to consider this question, it is difficult to see how it can be said merely from the answer given by this Court in favour of the Revenue that this contention was impliedly decided in favour of the Revenue. It would be straining logic to an absurd limit to say that though this contention was not raised, not argued, not discussed and not decided, yet it must be held to have been impliedly decided because through an error committed by this Court, an answer was given in favour of the Revenue in ignorance of the true position. It would also not be right to hold that merely because this Court erroneously answered the first question against the assessee without considering whether the view taken by the High Court on this point was incorrect, the assessee must be precluded from raising the contention that the assessee not being a registered shareholder, the amounts of loans advanced to the three business concerns of the assessee did not fall within the definition of "deemed dividend" under section 2(6A)(e). Why should the assessee, which had the decision of the High Court of this point in its favour and which decision was not assailed by the Revenue in the appeal and which remained undisturbed by this Court, be prejudiced on account of an obvious error committed by the court. The proper way of looking at the decision of this Court would be to regard the answer given in favour of the Revenue to be confined only to the aspect considered and decided by this Court. The only aspect considered by this Court was whether the "deemed dividend" under section 2(6A) (e) could be taxed in the hands of the beneficial owner of the shares or it could be assessed to only in the hands of the registered shareholder, and this Court held that "deemed dividend" did not stand on any different footing from actual dividend and just as actual dividend was liable to be taxed in the hands of the beneficial owner of the shares, so also "deemed dividend" must be held liable to be taxed in the assessment of the beneficial owner. This Court did not decide the question whether a loan advanced to a beneficial owner of the shares can be regarded as "deemed dividend" within the meaning of section 2(6A) (e) and the answer given by this Court in favour of the Revenue cannot be said to extend to this aspect of the question. We would, therefore, hold that the first question still remains to be answered so far as this aspect of the question is concerned and it is open to the assessee to contend that the amounts of loans advanced to the three business concerns of the assessee could not be regarded as "deemed dividend" under section-, 2(6A)(e), since the assessee was not a registered shareholder.

It is also obvious from what we have said above that there is no conflict between the decisions of this Court in *C.I.T. v. Rameswarlal Sanwamal* and *C.I.T. v. C.P. Sarathy Mudaliar* (supra). The question whether, on a proper construction of section 2(6A) (e), a loan advance to a beneficial owner of the shares would be liable to be regarded as "deemed dividend" was not raised or argued before this Court in *C.I.T. v. Rameswarlal Sanwamal* and this Court was not called upon to decide it and hence there is no discussion about it in the judgment of this Court nor is there any decision on it. It is only

in the subsequent decision in C.I.T. v. C. P. Sarathy Mudaliar (supra) that this question came up for the first time before this Court for consideration and this Court held that when sec. 2(6A)

(e) speaks of a "shareholder" it refers to the registered shareholder and not to the beneficial owner and hence a loan granted to a beneficial owner of the shares who is not a registered shareholder cannot be regarded as a loan advanced to a "shareholder" of the company so as to be within the mischief of section 2(6A)(e). There is thus no conflict at all between the decisions in C.I.T. v. C. P. Sarathy Mudaliar (supra) and C.I.T. v. Rameswarlal Sanwarlal. In fact, Mr. Justice Hegde was, a common Member of the Bench in both the cases and the subsequent decision in C.I.T. v. C. P. Sarathy Mudaliar was given within less than a month after the decision in C.I.T. v. Rameswarlal Sanwarmal. It is impossible to believe that Mr. Justice Hegde was oblivious of the decision in C.I.T. v. Rameswarlal Sanwarmal when he delivered the judgment in C.I.T. v. C. P. Sarathy Mudaliar.

The Revenue lastly contended that the decision in C.I.T. v. C.P. Sarathy Mudaliar is incorrect and we must refer the present case to a larger Bench. Now it is obvious that before we can be persuaded to accede to this request, we must be satisfied that the decision in Commissioner of Income Tax v. C. P. Sarathy Mudaliar is wrong. But having given our most anxious consideration, we find ourselves unable to disagree with the view taken in that decision. What section 2(6A) (e) is designed to strike at is advance or loan to a "shareholder" and the word "shareholder" can mean only a registered shareholder. It is difficult to see how a beneficial owner of shares whose name does not appear in the register of shareholders of the company can be said to be a "shareholder". He may be beneficially entitled to the shares but he is certainly not a "shareholder". It is only the person whose name is entered in the register of shareholders of the company as the holder of the shares who can be said to be a shareholder qua the company, and not the person beneficially entitled to the shares. It is the former who is a "shareholder" within the matrix and scheme of the company law and not the latter. We are, therefore, of the view that it is only where a loan is advanced by the company to a registered shareholder and the other conditions set out in section 2(6A) (e) are satisfied that the amount of the loan would be liable to be regarded as 'deemed dividend' within the meaning of section 2(6A) (e). The amount of the loan would not fall within the mischief of this section if it is granted to a beneficial owner of the shares who is not the registered shareholder. The decision in C.I.T. v. C. P. Sarathy Mudaliar does, in our opinion, lay down the correct interpretation of section 2(6A) (e).

Now in the present case it was common ground that the loans were advanced to the three business concerns of the assessee which was a Hindu Undivided Family and this Hindu Undivided Family was not the registered holder of any shares in the company but it was the beneficial owner of certain shares which stood in the name of the Manager and Karta, Shri S. M. Saharya. The loans were thus advanced to the beneficial owner of the shares and not to the registered shareholder and hence they could not be regarded as loans advanced to a "shareholder" of the company within the meaning of section 2(6A) (e). Section 2(6A) (e) was accordingly not attracted and the amounts of the loans could not be taxed as deemed dividends in the hands of the assessee. We accordingly answer the first question A in favour of the assessee so far as this aspect is concerned. In view of this answer to the first question, it is not necessary to consider the other two questions decided by the High Court on remand. The learned counsel appearing on behalf of the assesses, in fact, did not press them.

There will be no order as to costs of the appeal. B.B.A..