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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Reserved on: 01.02.2018
Pronounced on: 20.02.2018

\+ ITA 637/2004

COMMISSIONER OF INCOME TAX ..... Appellant
Through: Sh. Ruchir Bhatia, Sr. Standing Counsel for Revenue.

versus

M/S PRASIDH LEASING LTD. ..... Respondent
Through: Sh. Ajay Vohra, Sr. Advocate with Ms. Kavita Jha and Sh. Vaibhav Kulkarni, Advocates.

CORAM:
HON'BLE MR. JUSTICE S. RAVINDRA BHAT
HON'BLE MR. JUSTICE A. K. CHAWLA

S. RAVINDRA BHAT, J.

1. The following questions of law arise in this appeal:

"1. Whether the Tribunal was right in holding that the advance of a sum of ₹6.16 crores made by M/s Ginza Industries Ltd. to the assessee cannot be taxed as deemed· dividend without returning a finding that the lending of money was the substantial part of the business of the said company (M/s Ginza Industries Ltd);

2. Whether the Tribunal was right in holding that the Assessing Officer had wrongly made disallowance of ₹43.50 paid by the assessee to M/s Adani Associates towards guarantee commission fee;

2. In this appeal under Section 260A of the Income Tax Act, 1961 (hereafter referred to as "the Act"), the Revenue is aggrieved and challenges the order of the Income Tax Appellate Tribunal ("ITAT") which held that amount of ₹ 6.16 crores which the assessee received from M/s Ginza Industries Ltd. ("Ginza" hereafter) could not be taxable as deemed dividend under Section 2 (22) (e) of the Act. ITAT too held that the assessee was entitled to deduction of ₹ 43.50 lakhs paid as guarantee fee to M/s Adani Associates (hereinafter referred to "Adani") for advance received from Ginza.

3. The facts are that in the return of income filed by the assessee company on 30.11.1995 Ginza (with its registered office at 133, Canning Street, 3rd Floor, Room no. 17, Calcutta-700 001) was shown as sundry creditor in its balance sheet to which an amount of ₹ 17,40,20,000/- was due as at 30.03.1995. In this regard the assessee company was asked by order sheet entry dated 09.09.1997 to furnish the information with date, mode and purpose with which the credit of ₹ 17,40,20,000/- has been in the account of Ginza Industries Limited in the books of accounts of the assessee for each and every rupee. The assessee replied, stating that during the year, it had indulged in the business of sale and purchase of import licenses. It tied up with Ginza for procurement of License worth ₹ 50 crores approx. and had asked for advance of ₹ 20.00 crores for procurement of license. It was also stated that Adani stood as guarantor to Ginza, for the safe custody of the funds and in the Memo of their agreement Adani was to be paid 2.5% as guarantee commission by it (the assessee, Prasidh Leasing Ltd). The AO noticed, from the list of closing stock of shares for the Financial year 1994-95 filed with the return of

income that the assesse held 17,67,642 shares of Ginza. Therefore, the assessee company was asked to furnish the details of share holdings and whether any share holders and Directors were common. Subsequently, the assessee was asked to furnish particulars set out in a questionnaire.

4. A survey under Section 133A of the Act was conducted at Ginza's office premises at Kolkata, on 06.02.1998. One of the purposes for this survey was to ascertain if the interest free advance of ₹ 17.4 crores given to the assessee company by Ginza was covered under the definition of "Deemed Dividend" in terms of Section 2(22) of the Act. Summons were later issued to Ginza to furnish further particulars.

5. The AO, by his order brought to tax certain amounts. He held that the amount paid by Ginza fell within the description of the term "deemed dividend" under Section 2 (22) (e) and found as follows:

> *"In the case law cited above, it has been held that advances towards purchase are not covered under section 2(22)(e). But the fact in assessee's case is altogether different. These were no purchase made by Ginza Industries Ltd. from the assessee to show that purchase was the real motive for giving advances. The copy of agreement and correspondences between the parties shall be discussed subsequently. Right now it would be important to find out whether purchase of license was the real motive behind giving of advances.*
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> *If the advance was given really for purchase as the assessee says, what was the need to have a guarantee. In the normal business, where advances are given for purchases, the purchases are generally made and the party does not ask for a guarantee. Furthermore, the assessee had agreed to pay of commission to Adani Associates @ 2.5% of the net advances made which further substantiates that the motive for taking*

advance for the assessee was not to supply the licenses to Ginza Industries Ltd. but to enjoy the benefit of interest free advance. The reason is that the assessee, if the agreement is considered to be genuine, acknowledged that it stood benefited right at the moment when advance was given. The assessee was to pay to Adani Associates a commission of 2.5% on net of advance which meant that the assessee admitted having been benefited just by virtue of receiving the advance to such an extent that it could pay a commission @ 2.5% out of its own resources. Now, if the advance was really for purchases to be made for Ginza Industries Ltd. and the assessee had no vested interest in the amount of advance itself, why would it agree to pay the commission. If purchases were not made, as it happened assessee could not have gained anything if Ginza Industries Ltd. had recalled its advance at a short notice of 3 days. Instead it would have lost a few lacs of rupees on account of commission to Adani Associates. The anomalies and contradiction do not end here. There are a number of such contradiction & which are discussed below. 1. The assessee vide its letter dated 03.03.98 submitted, "the market of advance licenses is such that spot payment and something advance payments are required to block the desired deal. Therefore, M/s Ginza Industries Ltd. were asked by the assessee company to supply to it an advance, which may range up to Rs. 20 crores.

It would be interesting to see how the assessee had used or parked its funds obtained as advance from Ginza Industries Ltd. It purchased shares of different companies to the tune of Rs. 8 crores. It gave a loan of 6.4 crores approx. to Adani Finance & Investment Corporation Ltd. It also advanced load to another 5-6 persons. Now on one hand the assessee says that the business is such that one needs to make spot or advance payments to block the deal. There is also a provision in the agreement whereby Ginza Industries Ltd. could call back the

advance within 3 days. Now, the common sense would fell that all these are not possible at the same time. The money from advance is parked in investments in shares and loans and advances to parties in Ahmedabad (Adani Finance) and Calcutta (e.g. - Easter Housing Udyog, Marygold Estates etc.). The assessee could be required to mobilize these funds within 3 days, if Ginza Industries Ltd. recalled it or within a day if it was required to block deals in purchase of licenses. Would it be possible for the assessee to sell off its shares and call all its advances back in a day or two.

The answer is no. the payments from sale of shares could take at least a 'week' depending on settlement period in stock exchanges and it is not always possible to sell shares through private placement especially if it is not pre-planned. Moreover, no person takes a loan on interest which it may beasked to repay in 2-3 days. So, the companies or persons to whom the assessee advanced the loans did not obviously take the loan on such an ad hoc basis. They must have taken the loan for some period and even in case of an emergency could not be expected to pay back in a matter of 2-3 days.

Any person who has so much liquidity that it can pay back the loans within such a short period would not require a loan at all. Only banks are expected to have such liquidity. Furthermore, the rate of interest charged on these loans and advances was approx. @ 12% per annum which clearly shows that the loans were taken for medium to long term. Nobody pays or take interest @12% on loans and advances which can be called back within a short notice as short as 2-3 days. All this goes on to show that the assessee company had invested the funds with at least a medium term perspective. This shows that the assessee could not have and did not have the intention to purchase the shares."

6. The CIT (Appeals) whom the assessee approached, allowed the plea that the amount could not have been treated as "deemed dividend" holding as follows:

> *"it is very clear that the moneys given by M/s Ginza Industries Ltd. to the appellant company were given for the procurement of licence as per the tripartite agreement dated 1.9.94. The AO has tried to make much of the fact that no licence was ultimately procured by the appellant company for Ginza and as such this vitiates the entire agreements. This arguments, to my mind, is misplaced. If no deal was struck at a competitive rate acceptable to Ginza it doesn't mean that the purpose for t which the moneys were advanced can be called in question. The procurement of licences is a matter of performance and would depend on so many factor, many of which would be beyond the control of the appellant company, such as market sentiments and unsettled conditions. The learned AR has raised a valid point that as result of unstable condition in the lincene market the parties were asking for higher rates and higher advances, which M/s Ginza Industries Ltd. in the absence of the funds that it would have secured as a result of the planned public issue, could not come up with and, therefore, the deal had to be called off. It is like an exporter traveling abroad in search of contracts/orders and just because he fails to secure any contract/ order the travelling expense being called in question. The purpose behind a transaction and the results thereof do not often go hand in hand. If that were not so all human endeavors would lead to success but the story of real life is different. In this case that intention in important and it is very clear form the tripartite agreement and other evidence on record that the purpose for moneys given by M/s Ginza Industries Ltd. to the appellant company was to procure advance licences. Failure to actually clinch any such deal does not in any way detract from the purpose. 2.11(9) Keeping in view the facts and*

circumstance of the case, as brought out in the preceding sub paragraphs, the contention of the learned AR of the appellant company that the issue is squarely covered in favour of the appellant by the Hon'ble Bombay High Court decision in the case of Nagindas M. Kapadia, 177 ITR 393, deserves to be upheld. In the said judgement is has beheld that advance towards purchases cannot be brought in the ambit of Section 2(22)(e). Therefore, it is clear that the AO erred in taxing Rs. 6,16,00,000/- as deemed dividend u/s 2(22)(e) of the Act. The appellant company is entitled to a relief of Rs. 6,16,00,000/-."

7. The ITAT confirmed the conclusions of the CIT (A) and held as follows:

> *"13. After going through the facts, provisions of law and finding of the Assessing Officer as well as of the CIT(Appeals), we find that there is no dispute that the assessee company is a shareholder having more than 10% equity and that anadvance was given to the assessee. The content ion 0 f the assessee was that the amount advanced was in the course of business and hence cannot be treated as deemed dividend U/S 2(22)(e). We further noted that even the Assessing Office raccepts in his order somewhere that if it were in the course of business, no deemed dividend could have resulted. However, the AO held that there was no business transactions and all the transactions entered into by assessee with M/s Ginza, along with other companies from whom the import licences were to be purchased, were involved just to save itself from the clutches of section 2(22)(c). In our considered view. The CIT(Appeals) has dealt with this objection at great length as he has considered all the aspects of taking advance from MIs Ginza Industries for the purpose of supply of import licences, as the assessee was not dealing with import licences at that point of time, therefore, he*

contacted one M/s Vimal Overseas and payment of handsome amount i.e., of Rs. 8 crore was paid to this party directly to M/s Ginza. Confirmation from M/s Vimal Overseas was filed. The said confirmation of Vimal Overseas is placed on record, whereby it was recorded

"This is to certify that the advance received [To M/s Prasidh Leasing Limited/M/s Ginza Industries Limited during the financial year 1994-95 as per the statement of account enclosed with this letter was only for the supply of Import Export Licences to them. "
forVimal Overseas
Dated: 28.5.98
Place: Delhi.
Sd/ Authorized Signatory"

14. We further noted that the CIT (Appeals) ascertained the factual position by calling the details directly from M/s Adani Associates, who is a leading company and found that M/s Adani Associates was approached to be a Guarantor between assessee and MIs Ginza, as it was acceptable to both. As a guarantor M/s Adani Associates were to be paid 2.5% commission of the amount received in advance on account of purchase of import licence for M/s Ginza and accordingly a sum of Rs. 43,50,000/- was payable to M/s Adani Associates. It was further seen by the CIT(Appeals) that M/s Adani has shown this amount as their income. The statement of the parties from whom the import licences were to be purchased for M/s Ginza Industries were also examined and found that the amount was given directly by M/s Ginza Industries to the assessee for purchase of import licenses. M/s Ginza Industries was to bring a public issue and for that a detailed report was prepared. A copy of that was prepared and the same is placed at pages 14 to

32 of the paperbook and in paragraph 32 of the notes at page 23 (Internal page 11 of the report) it has been clearly mentioned that:

"Loans & Advances contains an advance of approx. Rs. 20 crores to Delhi based exporters, who will provide regular advance licenses for duty free import of Polyester Yarn at a concessional rate to the Company. In the event of the deal not materializing, the party is to return the amount with int. @ 21 % p.a. before 28th February, 1995. This deal was entered into so as to park the Company's surplus funds of a good return."

14.1 From this evidence it is clearly established that MIs Ginza Industries, who was preparing for bringing a public issue, has shown the advances given to assessee for the purpose of purchase of import licences. Therefore, from these details it cannot be said that there was any motive on part of the assessee or MIs Ginza Industries to cover up the matter for saving the assessee from the clutches of section 2(22)(e). Undisputedly, M/s Ginza Industries is a limited company and no director or shareholder are common in assessee company and of MIs Ginza Industries. M/s Adani Associates is also a public limited company and have no common shareholder or director. The work of the assessee as well as of M/s Ginza Industries and Adani Associates are totally different. The management is different and objects are also different. The shares were purchased by the assessee company by observing that M/s Ginza IS an important company, whose public issue was coming in near future, therefore, they purchased shares from M/s Ginza directly and also from the market. The statement of Managing Director of M/s Ginza were recorded by the Assessing Officer and he had categorically stated that the advance was given to the assessee for the purpose of purchase

of import license It is important to note here that when first installment of advance was to Vimal Overseas, at that point of time no shares of M/s Ginza Industries were purchased by assessee company. More than Rs. 20 crores were advanced by M/s Ginza Industries and the management of M/s Ginza Industries and the management of assessee company were different. Therefore, it cannot be said that M/s Ginza Industries wants to save the' assessee from the clutches of section 2(22)(e) by giving a colour of business transaction. A sum of Rs. 20 crore is not a small amount and there was 110 purpose other than the business expediency for giving such a huge advance to the assessee. Once the transaction were not materialized, as M/s Ginza failed to bring the public issue, therefore thereafter the total amount was returned to M/s Ginza. If by any reason the business transaction could not been materialized, then it cannot be said that there was any other motive other than business expediency.

15. In view of all these facts and circumstances and in view of the detailed reasoning given by the CIT(Appeals) in his order, which could not be controverted by the learned D.R, we are of the considered view that CIT(Appeals) was justified in holding that the transactions entered into by the assessee with M/s Ginza; for business consideration. The findings of the CIT(Appeals) are findings of fact, as the CIT(Appeals) has dealt with each and every objection of the Assessing Officer and then arrived at a conclusion that the transactions entered by assessee with M/s Ginza were', for business consideration. Once it is established that the transactions

16. We have confirmed the finding of the CIT (Appeals) that this was a business transaction. therefore, we are not inclined to consider the alternate submission of both sides in regard to

accumulative profits of Mis Ginza Industries for the purpose of section 2(22)(e).”

8. The revenue argues that the ITAT failed to notice that no import licences were purchased and sold to Ginza. In fact there was no transaction whatsoever between the assessee and M/s Ginza. It is submitted that the alleged agreement between assessee and M/ s Ginza was vague, ambiguous and did not specify the rate/discount on purchase of import licenses. Giving interest free advance of ₹ 20 crores under such an agreement cannot be regarded as a genuine business transaction.

9. It is argued that M/s Ginza did not need import licenses for self-consumption. The so-called project was at a drawing stage and merely a proposal. It did not materialize. It is rather odd and strange for M/s Ginza to enter into an agreement for purchase of import licences and agree to make payment in advance of ₹ 20 crores, when the alleged project, for which these were to be required, was being visualized and uncertain. It is argued that the impugned order erroneously relied upon the draft prospectus/document in terms of which Ginza had given loan/advance of approximately ₹ 20 crores to the assessee to provide regular advance licences for duty free imports of polyester yarn at concessional rates and in the event of the deal not materializing, the assessee was to return the amount 'with interest @ 21% per annum before 28th February 1995. It is argued that in terms of the alleged agreement dated 1.9.1994, the assessee was not liable to pay any interest and substantial amounts were paid by M/s Ginza to the assessee even in the month of March 1995 though the deal had not materialized.

10. It is argued that the agreement, dated 01.09.1994 was merely a cover up and camouflage for giving loans and advances to the assessee by Ginza to get over provisions of Section 2 (22) (e) of the Act. ₹20 Crores was not a small amount, therefore justification for giving the same should have been given. The onus was upon the assessee to justify and prove that it was a genuine business transaction.

11. The Revenue argues furthermore that the ratio of the decision in *Navnit Lal. C. Jhaveri v. K.K. Sen* 1965 (56) ITR 198 squarely applies. It is submitted that the object of introducing Section 2(22)(e) of the Income Tax Act, 1961 was to curb the tendency of passing-off what would be "dividends" as loans or other advantages to shareholders. Learned counsel also relied upon *Tarulata Shyam v. CIT* 1977 (108) ITR 345, (where the court had held that the position reflected in the books at the end of the year is not conclusive and that if funds are actually given by the company to its shareholder, which answers the description under the provision, it would be treated as "deemed dividend") to say that similarly loans camouflaged as trading advances fall within the mischief of "deemed dividend" provision. Lastly, he also relied upon the judgment of this Court in *CIT v. Sunil Chopra* 242 CTR (Del) 498, where the true nature of a transaction, discerned by the AO was upheld and the ITAT's reasoning set aside.

12. Sh. Ajay Vohra learned senior counsel appearing for the assessee contended that the ITAT – and the appellate Commissioner recorded correct findings which do not need to be distributed. It was submitted that the sum of ₹ 6.16 crores was given by Ginza to the assessee for legitimate

and genuine purpose, i.e. for procuring import licenses. Though the AO recorded statements made on behalf of Ginza through its officials, the crucial part (omitted by him but considered by the lower appellate authorities) was that the company intended to set-up a manufacturing facility and also intended to trade in import licenses. The assessee had expertise and knowledge in the field of dealing with such licenses. No doubt, the manufacturing facility proposed by Ginza was not set-up in the assessment year or even later but the fact remained that it had geared up all its resources to do so.

13. Learned senior counsel highlighted that the approach adopted by the CIT(A) and ITAT accord with the principles enunciated by several decisions which is that merely because amount is given by a company to its shareholder, it would not fulfill the character of a deemed dividend. Whilst the AO is justified in examining the issue, he has to also take into account commercial realities such as that quite often amounts are given in the usual course of proceedings towards procurement of services or purchases made. Often times, there is delay in the fulfillment of the contract, i.e. supplies to be made or the services to be rendered. *Ipso facto*, this would not convert a genuine transaction into a suspect one attracting deemed dividend clause. Learned counsel relied upon the judgment of this Court in *CIT v. Creative Dyeing and Printing Private Limited* 2009 318 ITR 476; *CIT v. Atul Engineering Udyog* 2015 228 Taxmann 295 (All) and *CIT v. Nagindas. M. Kapadia*1997 (177) ITR 393. He also relied upon the circular issued by the CBDT which clarified that amounts advanced by a company through a concern and adjusted

against dues for job work done or by a company to its shareholder to install plant or machinery at its premises; amounts given as floating security deposit by a company to its sister concern or shareholder for use of electricity generators etc. were of trading transactions. The Circular stated that *"it is, a settled position that trade advances, which are in the nature of commercial transactions would not fall within the ambit of the word 'advance' in section 2(22)(e) of the Act. Accordingly, henceforth, appeals may not be filed on this ground by Officers of the Department....."*.

14. It was submitted that as far as the second question with respect to the disallowance of ₹ 443.50 lakhs to M/s. Adani Associates is concerned, the concurrent findings are based upon appreciation of evidence by lower appellate authorities. Learned senior counsel particularly relied upon the observations of the CIT(A) who had recorded that the payment of guarantee fee in fact reinforced the genuineness of the transaction, i.e. advance given to the assessee by Ginza. It was submitted that the AO needlessly rejected the explanation given by the assessee in this regard.

Analysis and findings.

<u>Reg Point no.1.</u>

15. Section 2(22)(e) of the Income Tax Act, 1961 reads as follows:

> *"**2.** In this Act, unless the context otherwise requires,—*
>
> XXXX XXXX XXXX
>
> *(22) dividend" includes—*

XXXX XXXX XXXX

(e) any payment[9] *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)* [10]*[made after the 31st day of May, 1987, by way of advance or loan*[9] *to a shareholder*[9]*, 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*[11] *;"*

16. The challenge, to a *para materia* provision, (i.e. 2(6A) of the repealed Act of 1922) was repelled by the Supreme Court in *Navnit (supra)*. In *Navnit (supra)*, the Supreme Court noted that there could be three kinds of payments, i.e. payments made to the shareholder by a company by way of advance or loan; (b) payments made on behalf of the assessee and (c) payments made for the benefit of the assessee. The Court then analyzed the *para materia* provision and said that 5 conditions are to be met for its applicability; firstly that the company should be one in which the public is not substantially interested within the meaning of the expression in law, in the year in which loan is advanced. Secondly, the buyer should be a shareholder at the date when the loan was advanced regardless of the extent of shareholding. Thirdly, the loan to the shareholder by the company can be deemed to be dividend only to the

extent to which it is shown that the company possessed accumulated profit at the date of the loan; fourthly, the loan should not be advanced by the company in its ordinary course of business and lastly that the loan should remain outstanding at the instance of the shareholder's previous year in relation to the concerned assessment year. The Supreme Court also clarified the fourth condition by importantly holding that in other words, this provision would not apply to cases where the company which advances the loan to its shareholder carries on the business of money lending itself;

17. In the present case, the assessee held shares in Ginza. However, the extent of shareholding was not in terms of the statutorily prescribed limits. It reached that level on 11.11.1994; by then Ginza had advanced ₹ 12,31,50,000/- (which was concededly not taken into account by the AO). Undisputedly, Ginza was not a company in which the public was not substantially interested because Floral Commercial Pvt. Ltd. held more than 50% of its shares as on 31.03.1994. That concern is itself a private company. During 1994-95, shares were sold by Floral Commercial Pvt. Ltd. and others, which resulted in the company's status as remaining unaltered in which the public was not substantially interested. The assessee's total holdings amounted to 17,67,642 shares. On 11.11.1994, a direct allotment of 6,77,000 shares was made in favour of the assessee. It was then that it became interested in Ginza in excess of 10%; its shareholding increased to more than 10%. The AO's order in this case was based upon extensive and painstaking enquiry. He found that the assessee used the amount – which Ginza had given it to procure

import licenses, by purchasing shares and giving further advances of ₹6.4 crores to various entities at 12% per annum. The AO inferred that this circumstance undermined the assessee's contention that Ginza advanced the amount of ₹ 6.16 crores to it in the ordinary course of business and observed as follows:

> *"It would be interesting to see how the assessee had used or parked its funds obtained as advance from Ginza Industries Ltd. It purchased shares of different companies to the tune of Rs.8 crores. It gave a loan of Rs.6.4 crores approx to Adani Finance & Investment Corporation Ltd. It also advanced loan to another 5-6 persons. Now on one hand the assessee says that the business is such that one needs to make spot or advance payments to block the deal. There is also a provision in the agreement whereby Ginza Industries Ltd. could call back the advance within 3 days. Now, the common sense would tell that all these are not possible at the same time. The money from advance is parked in investments in shares and loans and advances to parties in Ahmedabad (Adani Finance) and Calcutta (e.g. – Easter Housing Udyog, Marygold Estates etc.). The assessee could be required to mobilize these funds within 3 days, if Ginza Industries Ltd. recalled it or within a day if it was required to block deals in purchase of licenses. Would it be possible for the assessee to sell off its shares and call all its advances back in a day or two. The answer is no. The payments from sale of shares could take at least a 'week' depending on settlement period in stock exchanges and it is not always possible to sell shares through private placement especially it if is not pre-planned. Moreover, no person takes a loan on interest which it may be asked to repay in 2-3 days. So, the companies or persons to whom the assessee advanced the loans did not obviously take the loan on such an ad hoc basis. They*

must have taken the loan for some period and even in case of an emergency could not be expected to pay back in a matter of 2-3 days. Any person who has so much liquidity that it can pay back the loans within such a short period would not require a loan at all. Only banks are expected to have such liquidity. Furthermore, the rate of interest charged on these loans and advances were approx. @ 12% per annum which clearly shows that the loans were taken for medium to long term. Nobody pays or take interest @ 12% on loans and advances which can be called back within a short notice as short as 2-3 days. All this goes on to show that the assessee company had invested the funds with at least a medium term perspective. This shows that the assessee could not have and did not have the intention to purchase the said advance licenses for Ginza Industries Ltd."

18. The statement of the Managing Director of Ginza – the company was recorded. He stated that Ginza intended to purchase import licenses to the tune of ₹ 70-80 crores some of which were for its own use (worth ₹ 30-40 crores) and the rest was to be used for trading. According to the statement the assessee had offered to obtain license which was to be 10-15% lower than the market rates and eventually the rates offered by it were not beneficial even though better than the prevailing market rates. The AO also held – after considering the statements made on behalf of Ginza by its MD and eliciting further details from the assessee that Ginza claimed that it was intending to launch projects like yarn, steel and chemicals which never took off. Ginza was into production of items that needed domestic inputs. It was also held that Ginza MD upon being asked whether materials had been procured: in 1994-95 *"or subsequently steel, yarns or chemicals against any import licences, his answer was 'no'. In fact the total import of Ginza from FY 1991-92 till FY 1996-97 has only*

been for a value of Rs. 20 lakhs. All of this goes on to indicate that Ginza was never in a position to procure any import items against licences inhouse."

19. The AO also held on the other hand the answer of Sh. Setiha, who dealt with licences on behalf of the company was also of an evasive nature and his failure to comply to the queries dated 18.03.1998 to establish existence of employees competent to dealt with licenses, as stated by him, also proves that Ginza did not have any intention or scope by way of knowledge or expertise to deal with the premium market for buying and selling advance licenses.

20. The CIT(A) completely brushed aside the AO's determination/findings and in fact made light of them by stating that whether or not any license was ultimately procured by the assessee for Ginza was not relevant and was in fact "misplaced". The CIT(A) was of the opinion that absence of procurement of licenses because of lack of competitive rates acceptable to Ginza could not have led to the inference that the transaction fell within the description of Section 2(22)(e); and that procurement of licenses is a matter of performance and it depended on many factors most of which would be beyond the control of the assessee. The ITAT endorsed this finding, also adding that Ginza had prepared itself to bring-up the issue and had shown as advances given to the assessee for the specific performance of advance licenses. It held that the assessee's motives or that of Ginza would have been doubted. The ITAT was also impressed by the fact that there were no common directors of Ginza in the assessee company and that even Adani Associates which

had underwritten the amounts subject to payment of commission was also a public company.

21. The decision of this Court in *Sunil Chopra (supra)* is illuminating. There, the assessee had received advances substantially, worth ₹ 1.4 crores from each company in which he held more than 10% shares. The public were not substantially interested in these companies. The AO held that the amount was deemed dividend. Except for grating relief to the extent of ₹ 38.81 lakhs, the CIT(A) held the balance amounts to be deemed dividends. The ITAT reversed these findings holding that the assessee's business involved brokerage from real estate and they were for investment in the real estate. The ITAT's findings were reversed by this Court on the basis of the following reasoning:

> *"8. From the order of the Tribunal, it may be seen that it has only commented upon the finding recorded by the AO. Before proceeding further to see the reasoning of the Tribunal, we may note the background of the proceedings before the AO. The AO recorded that during the course of assessment proceedings, the assessee in reply to show cause notice furnished his response. With regard to the amount of Rs.34,75,780/- received from M/s National Capital Region Electronics Pvt. Ltd., the assessee stated that the said amount was received against sale of property in terms of agreement dated 18th September, 2003. Here it may be noted that the companies are closely-held companies in which the only Directors are none other than the family members of the assessee. The AO recorded the said agreement to be sham and rightly so, inasmuch as the agreement was executed on 18th September, 2003 and the handing over of the property was to be done before 31st December, 2008. In any case, this property was still being*

reflected in the balance sheet of the assessee as on 31st March, 2005, even though the agreement was entered on 18th September, 2003. The CIT(A) also disbelieved the claim of the assessee on this count. The Tribunal in this regard has recorded that the assessee was claiming this advance for investment in his books of accounts and the AO has not disputed this. Apparently, this was a perverse recording by the Tribunal inasmuch as it has been seen that AO and CIT(A) have categorically recorded this transaction as colourable device. It is unbelievable that an agreement was executed on 18th September, 2003 and the payment was made, but the possession of the property was to be handed over after more than five years. Even the property continued to be reflected in the balance sheet of the assessee after two years of the agreement. Similarly, in respect of Rs.27,90,125/- shown as loan/advance from M/s TSM Polymers Pvt. Ltd., the assessee had replied to the AO that this was received against sale of property under the terms of the agreement dated 18th September, 2003. With regard to this entry also, the Tribunal made a sweeping observation that the assessee was claiming these as advance for investment in his books of accounts and this aspect was not disputed by the AO. He also observed that the business of the assessee is earning brokerage from the business of real estate and this demonstrated that he had taken the money in the line of his business. The observation of the Tribunal that the AO had not brought any contrary material on record was equally perverse and against the facts recorded by the AO. In this regard also, it may be noted that though the agreement was executed on 18th September, 2003 for the sale of the property, but the property continued to be reflected in the balance sheet of the assessee as on 31st March, 2005. The AO rightly recorded both these aspects to be not covered by the exception to deemed dividend as contemplated under Section 2(22)(e).

> *Consequently, he rightly held these transactions as sham and treated them as deemed dividend of the assessee under Section 2(22)(e)."*

22. The Board circular and the line of reasoning adopted by the various High Courts, including this Court relied upon by the assessee in this case undoubtedly indicate that the trading transactions or advances would fall outside the mischief of sums that are to be treated as deemed dividends. To this extent, there can be no dispute. Nevertheless, as to whether amounts advanced by a company to a company in which the public does not have any substantial shareholding or in which the public is not interested to a shareholder, to an entity or individual holding shares in excess of 10% amounts to a trading transaction or falls within the aspect and, therefore, deemed commercial, there can be no bright line test. The Revenue has to conduct a fact-based inquiry each time such contention is urged by the assessee. The facts and circumstances of this case show that Ginza advanced substantial amounts (which were confined by the AO to only ₹ 6.16 crores since that was the extent of payment made by Ginza after the assessee characterized the *Rubicon* threshold of 10% as a shareholder in it from out of its available surplus). The AO's decision, that the profit available for distribution for the concerned AY (including accumulated profit for FY 1993-94) were to the tune of ₹ 17.4 crores from 08.09.1994 and approximately ₹ 18.16 crores from 20.09.1994. This finding, in the considered view of this Court is significant; it has remained undisturbed; neither the CIT(A) nor the ITAT have adversely commented on it or even reversed it.

23. The second significant aspect in this Court's opinion is that Ginza was not trading in import licences or even advance licences. Yet it wished to purchase license *inter alia* stating that it needed them for importing steel, yarn and other equipment necessary to set-up a project. A closer look would reveal that its imports never took place. Ginza's stand was that it wished to trade substantially to the extent of around ₹40 crores in import licences and that the assessee had in overall procured licenses at a competitive rate of 10-15 % less than the prevailing market rate. Even if all these facts were assumed to be correct, two important aspects are undeniable – first that one of the objects of procuring import license, i.e. self importation of equipment and for self consumption was never fulfilled. No significant imports were made. Secondly, in fact hardly any import licenses were procured (although the ITAT returned a finding with respect to payments made directly to Vimal Enterprises.), in fact an amount of ₹ 8 crores was paid directly by Ginza to Vimal. The last significant aspect is that even though the assessee claimed that Ginza could recall its amounts within three days in terms of the agreement, it had committed itself to long term lending and investment. Substantial amounts were advanced to commercial entities at 12%, including ₹ 6.4 crores advanced to Adani Exports. The assessee also invested ₹ 8 crores by purchasing shares.

24. These facts analyzed meticulously by the AO, in this Court's opinion, were completely overlooked by the lower appellate authorities who virtually made short work of the findings recorded with respect to the applicability of Section 2(22)(e). All indications were that the

assessee was sanguine and assured about the nature of the amount given by Ginza, i.e. that it could use it for its own purposes– as it did by advancing substantial amounts at commercial rates of interest) which could not be conceivably attributable to short term deposits and also for the purpose of yielding income, i.e. by investing with the object of trading in shares.

25. In these circumstances, both the lower authorities, in the opinion of the Court overlooked that the real intent of Ginza in advancing the sums it did to the assessee was to share its profit by way of deemed dividend. The sum of ₹ 6.16 crores clearly fell within the description of "deemed dividend" under Section 2(22)(e) of the Act like in the case of *Sunil Chopra (supra).* For these reasons, the first question is answered in favour of revenue and against the assessee.

Regarding Question no.2

26. This question relates to the disallowance made in respect of ₹43.5 lakhs claimed by the assessee as commission. On this aspect, this Court notices that the entire tripartite agreement between the assessee, Ginza and Adani was rejected, because its basis, including the assurance of a commission to the extent of ₹43.5 lakhs payable to Adani, was held to be false. The AO was of the opinion that the agreement was of a self–serving nature and meant for purposes other than of business intended. The AO took into account the fact that even though the amounts could be recalled within three days, in fact they were lying with the assessee for long periods and never advanced for the purpose of purchase of licenses. The

guarantee commission supposed to have been paid was intended to further the object of Section 2(22)(e). The AO concluded as follows:

> *"From the above discussion, it has also been clearly established that the tripartite agreement has been created to suit the self interest and the consequent payment of 43.5 lacs has been shown to have been made as a cover up exercise and hence cannot be taken as the payment made for the purposes of business. This issue had also been discussed in the show cause notice dated 23.3.1998 which has been discussed earlier in the order. The claimed payment of 43.5 lacs made to Adani Associates as guarantee commission is therefore being disallowed because the same has not been for the purpose of business not for self serving moreover to create a cover up for escaping the provision of Section 2(22)(e) of the Income Tax Act, 1961, resulting in an addition of Rs.43.5 lacs."*

Subsequently the AO proceeded to discuss the issue further and ultimately brought to tax the said amount of ₹ 43.5 lakhs.

27. The CIT (A) and the ITAT deleted the disallowance holding that the original transaction of advance was genuine and a trading one and furthermore that the commission was paid through payment channels in terms of the tripartite agreements. It was also observed that there was no interrelationship between the assessee and Adani or for that matter the other company with which the license arrangements were sought to be entered into directly.

28. This Court is of the opinion that since the commission payment was premised upon the assessee's claim about the genuineness of the underlying transaction, i.e. that it was an advance, the findings on

Question No.1 logically would result in the second question too being answered in the revenue's favour.

29. The AO's findings are based upon facts. In the opinion of the Court, the facts also pointed to a significant detail that seems to have escaped the notice of lower appellate authorities, i.e. that after obtaining substantial sums, the assessee even made over a substantial part of it – ₹6.14 crores to Adani to whom it paid ₹43.5 lakhs as commission for the standing guarantor. The latter payment in the light of the transactions previously discussed strain ones' credibility and does not accord with prudent commercial practice. For these reasons the Court is of the opinion that the findings of the lower authorities are based upon a mis-appreciation of circumstances and are, therefore, unreasonable, and are premised on an erroneous appreciation of the facts and the law. The disallowance of ₹43.5 lakhs was just and warranted.

30. The second question of law is too answered in favour of revenue and against the assessee. In view of the findings in favour of the revenue, the appeal has to succeed. It is accordingly allowed. There shall be no order as to costs.

S. RAVINDRA BHAT, J

A. K. CHAWLA, J

FEBRUARY 20, 2018