

**IN THE INCOME TAX APPELLATE TRIBUNAL
"E" Bench, Mumbai**

**Before Shri Mahavir Singh, Judicial Member
and Shri G. Manjunatha, Accountant Member**

ITA Nos. 5549 & 5971/Mum/2014
(Assessment Years: 2010-11 & 2011-12)

A C I T - 7(2) Room No. 624, 6th Floor Aayakar Bhavan, M.K. Road Mumbai 400020	Vs.	M/s. Sunjewels International P. Ltd. Unit No. 116, SDF-IV, SEEPZ Andheri (E), Mumbai 400 096
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PAN – AADCS3647P

Appellant

Respondent

Appellant by: Shri R. Manjunatha Swamy
Respondent by: Shri Pramod Kumar Parida

Date of Hearing: 01.08.2018
Date of Pronouncement: 21.08.2018

ORDER

Per G. Manjunatha, AM

These two appeals filed by the Revenue are directed against separate but identical orders of the CIT(A)-13, Mumbai dated 20.06.2017 and 07.07.2017 for assessment years 2010-11 and 2011-12. Since the facts are identical, these appeals are heard together and are disposed off by this common order for the sake of convenience.

2. The Revenue has raised more or less common grounds of appeal for both the assessment years. For the sake of brevity grounds of appeal taken for A.Y. 2010-11 are extracted below: -

- “(i) The Learned CIT(A) has erred on facts and in law in deleting the disallowance made by the Assessing Officer on account of exemption under section 10AA of the Income Tax Act, 1961 without properly appreciating the factual and legal matrix of the case as clearly brought out by the Assessing Officer in the Assessment Order.*
- (ii) The Learned CIT(A) has erred on facts and in law in deleting the disallowance made by the Assessing Officer on account of exemption under section 10AA of the Income Tax Act, 1961,*

without properly appreciating the fact that business of assessee was merely a continuation of the old business and thereby violating the primary conditions of eligibility of exemption u/s. 10AA of the Act.

- (iii) *The Learned CIT(A) has erred on facts and in law in deleting the addition of ₹6,95,52,345/- u/s. 2(22)(e) r.w.s.56 of the Income Tax Act, 1961 without properly appreciating the factual and legal matrix as clearly brought out by the Assessing Officer.*
- (iv) *The Learned CIT(A) has erred on facts and in law in deleting the addition of ₹6,95,52,345/- u/s. 2(22)(e) r.w.s.56 of the Act, holding that the assessee was not shareholder of the lender company and by placing reliance upon the decision of Mumbai Tribunal in the case of ACIT vs Bhaumik Colours 92009) SOT (Mum SB) ignoring the intent of Legislation as envisaged in CBDT circular No 495 dated 22.09.1987.”*

3. The brief facts of the case extracted from ITA No. 5549/Mum/2014 are that the assessee company, which is engaged in the business of manufacture and export of studded jewellery, filed its return of income for A.Y. 2010-11 on 27.09.2010 declaring total income of ₹6,74,620/-. The assessee has claimed deduction under Section 10AA of the Income Tax Act, 1961 (hereinafter "the Act") in respect of profit derived from the unit located in SEZ. The assessee is a 100% exporter of diamond jewellery and established its unit in SEEPZ for manufacturing of studded gold and diamond jewellery. For its intended activity, assessee has taken approval from the Development Commissioner of SEZ vide its letter dated 05.07.2004. The case was selected for scrutiny and notice under Sections 143(2) and 142(1) of the Act were issued. In response to the notice, the Authorised Representative of the assessee appeared from time to time and filed various details as called for. The assessment was completed under Section 143(3) of the Act, on 31.01.2013 determining the total income at ₹12,85,84,750/- by making additions towards disallowance of deduction claimed under Section 10AA of the Act, on the grounds that assessee has set up new unit in SEZ by splitting/reconstruction of already existing unit. The AO also made addition towards deemed dividend under Section 2(22)(e) of the Act, in respect of loans received from M/s. KSN Trading Pvt. Ltd. and M/s. NSN Jewellers Ltd. on the ground that the assessee has received loans and advances from a company where the beneficial

ownership of shares in the assessee company and the lender company were held by common shareholders. Aggrieved by the assessment order the assessee preferred appeal before the CIT(A).

4. Before the CIT(A), the assessee filed elaborate written submissions on both the issues which has been reproduced by the learned CIT(A) in his order at pages 3 to 9. The sum and substance of the arguments of the assessee before the learned CIT(A) was that the AO was erred in denying deduction under Section 10AA of the Act, in respect of profit derived from unit located in SEZ without appreciating the fact that the assessee has obtained necessary approval from the competent authority. Therefore it is incorrect on the part of the AO to deny the benefit by holding that the assessee has set up its business by splitting/reconstruction of already existing business. Similarly, in respect of addition made towards disallowance of deemed dividend under Section 2(22)(e) of the Act, the assessee submitted that it has received intercorporate loans from two of its money lending concerns in the normal course of business and the AO has incorrectly appraised the facts to make addition under Section 2(22)(e) of the Act.

5. The CIT(A), after considering the submissions of the assessee, deleted the addition made by the AO towards disallowance of deduction claimed under Section 10AA of the Act, by following his predecessor's order in assessee's own case for assessment years 2007-08 and 2008-09 by holding that the assessee has fulfilled all conditions specified under Section 10AA of the Act, to claim the benefit of deduction, therefore the AO was incorrect in disallowing deduction claimed under the said section without appreciating the fact that setting up a new business in a different name does not amount to splitting/reconstruction of already existing business. In so far as addition made towards deemed dividend under Section 2(22)(e) of the Act, the CIT(A) held that the issue has been considered by the Hon'ble Bombay High Court in the case of Universal Medicare Pvt. Ltd. vs. CIT 190 Taxman 144 wherein under similar set of facts held that intercorporate loans received in normal course of business

would not come under the purview of section 2(22)(e) of the Act. The facts of the assessee's case are identical to the facts considered by the Hon'ble Jurisdictional High Court. Therefore by following the ratio laid down by the Hon'ble High Court deleted the addition made by the AO. Aggrieved by the order of the CIT(A) Revenue is in appeal before us.

6. The first issue came up for our consideration is deduction claimed under Section 10AA of the Act, in respect of profit derived from unit located in SEZ. The learned A.R., at the time of hearing, submitted that the issue is squarely covered in favour of the assessee by the decision of the ITAT Mumbai in assessee's own case in ITA Nos. 5401 to 5403/Mum/2013 for assessment years 2007-08 to 2009-10, wherein under similar set of facts the ITAT has deleted the addition made by the AO towards deduction claimed under Section 10AA of the Act. The learned D.R. for the Revenue fairly accepted that the issue is covered in favour of the assessee by the decision of the ITAT for earlier years.

7. We have heard the rival contentions and considered the material available on record. The issue of deduction claimed under Section 10AA of the Act, is no longer res integra. The Coordinate Bench of ITAT in assessee's own case has considered similar issue in the light of section 10AA of the Act, and after considering the facts held that the assessee has established an independent unit in the SEZ at Andheri to carry out manufacture and export of plain and studded golden and silver jewellery and started commercial production from A.Y. 2006-07 onwards. The relevant portion of the order of the ITAT is extracted below: -

"5. We have heard the rival submissions and perused the material before us. We find that the assessee had established as an independent unit in the Special Economic Zone (SEZ) SEEPZ at Andheri (E) to carry out manufacture and export of plain and studded gold and silver jewellery, that it started its commercial production w.e.f. June 2005 i.e. AY.2006-07, that by virtue of being established as an unit in SEZ it became eligible for the grant of deduction u/s. 10AA of the Act, that there was loss in the first year and loss was accepted u/s. 143(3), that the AO considered the issue as to whether the assessee was at all eligible for the benefit u/s 10AA, that the AO

made detailed inquiry while completing scrutiny assessment in that regard, hat in the next Asst. Year 2007-08, the AO further enquired about the eligibility for availing the benefit u/s. 10AA, that the assessee had suitably replied point by point to the queries raised by the AO, that in subsequent assessment years 2010-11 and 2011-12, it was allowed its claim u/s. 143(3). For the three AY.s. 2007-08 to 2009-10 he denied the assessee benefit of 10AA. We find that the basis for denying the deduction was that the AO was of the opinion that the unit was established by restructuring or splitting of old unit. We further find that he has not elaborated as to how had he reached at the above conclusion. Secondly, he has not taken into consideration the new machinery purchased by the assessee during the year. We have gone through the bills of machinery purchased by the assessee during the year under consideration. From the bills forming part of the paper book, it is clear that the assessee had purchased machinery of substantive value and therefore without any evidence we are not ready to agree with the AO that the assessee had used old machinery to establish the new unit. We find that the issue of eligibility of exemption u/s. 10AA was already deliberated upon by the AO in the earlier AY, therefore, without bringing on record the new facts distinguishing same with the facts of last AY., the AO should not have taken a diagonally opposite stand. Considering the peculiar facts and circumstances of the case, we are of the opinion that the order of the FAA does not suffer from any infirmity. So, upholding the same, we decide effective ground of appeal against the AO.”

8. In this view of the matter and consistent with view taken by the Coordinate Bench, we are of the considered view that the AO was incorrect in denying the benefit of deduction claimed under Section 10AA of the Act. The CIT(A), after considering the facts, has rightly deleted the addition made by the AO. We do not find any error or infirmity in the order of the CIT(A), hence we inclined to uphold the findings of the CIT(A) and reject the ground taken by the Revenue.

9. The next issue that came up for considering is the addition made towards deemed dividend under Section 2(22)(e) of the Act. The facts with regard to the impugned dispute are that during the year under consideration the assessee has received unsecured loans from M/s. KSN Trading P. Ltd. and M/s. NSN Jewellers Ltd. The AO observed that the loans received by the assessee from the above two companies hit by the provisions of Section 2(22)(e) of the Act, as M/s. Sunjewels India Pvt. Ltd. is a common shareholder in assessee company as well as NSN Jewellers

Pvt. Ltd. and KSN Trading Pvt. Ltd. The lenders of loan is having beneficial ownership of more than 10% of shares, therefore the loans and advances received from KSN Trading Pvt. Ltd. and NSN Jewellers Pvt. Ltd. comes within the purview of provisions of Section 2(22)(e) of the Act.

10. The learned A.R. for the assessee submitted that the learned AO was erred in making addition toward loans and advances received from KSN Trading Pvt. Ltd. and NSN Jewellers Pvt. Ltd. under Section 2(22)(e) of the Act without appreciating the fact that these loans are intercorporate loans taken during the normal course of business of the assessee and hence are not hit by the provisions of Section 2(22)(e) of the Act. The learned A.R. further submitted that once the loans are taken in the normal course of money lending business the provisions of Section 2(22)(e) of the Act are not attracted but the AO without appreciating this fact has made addition only on the ground that the assessee is having beneficial shareholding in the two lender companies. The lender companies are involved in money lending business activity, therefore this transaction come within the ambit of Explanation provided to Section 2(22)(e) of the Act. In this regard relied upon various judicial precedents, including the decision of the Hon'ble Bombay High Court in the case of CIT vs. Universal Medicare Ltd. (2010) 324 ITR 263. The assessee also relied upon the decision of the ITAT Special Bench in the case of ACIT vs. Bhaumik Colour Pvt. Ltd. (2009) 313 ITR (AT) 146.

11. The learned D.R., on the other hand, submitted that the learned CIT(A) was erred in deleting the addition made by the AO without appreciating the fact that provisions of Section 2(22)(e) of the Act, will hit to any loans and advances taken from a company where one of the shareholders is holding more than 10% beneficial interest. Therefore it is incorrect on the part of the CIT(A) to take a view that only registered shareholder takes loan from a company then provisions of Section 2(22)(e) will come into operation. The learned D.R. referring to the decision of the Hon'ble Supreme Court in the case of Gopal & Sons (HUF) vs. CIT (2017) 391 ITR 1 submitted that the Hon'ble Supreme Court has put an end to

the controversy and held that even a beneficial shareholder holding substantial interest in a company or firm which receives loans and advances from other company then provisions of Section 2(22)(e) of the Act will come into operation and loans and advances to the extent of accumulated profit of the company shall be treated as deemed dividend under Section 2(22)(e) of the Act.

12. We have heard both the parties and perused the material available on record. The facts with regard to common shareholding in assessee company as well as lender company is not disputed by the assessee. M/s. Sunjewels India Pvt. Ltd is holding more than 88.80% shareholding in assessee company as well as 99% shares in two lender companies. It is also an undisputed fact that the assessee has received unsecured loans and advances from KSN Trading Pvt. Ltd. and SNS Jewellers Pvt. Ltd. The two lender companies are having accumulated profit as on the date of loans and advances given to the assessee company. The AO has treated loans and advances received from the two lender companies as deemed dividend under Section 2(22)(e) of the Act to the extent of accumulated profit of lender companies or loans and advances received by the assessee whichever is less and accordingly made addition of ₹6,95,52,345/-. It is the claim of the assessee that the loans and advances received from the above two companies are normal business transactions in the nature of intercorporate loans and hence the AO was erred in applying the provisions of Section 2(22)(e) of the Act. The assessee has also taken a plea that only the registered shareholder who is having beneficial holding of shares in a company from which loans and advances received will come under the provisions of Section 2(22)(e) of the Act, but not the beneficial owner of the equity shares in the said companies.

13. Having heard both the sides, we find that the controversy has been resolved by the Hon'ble Supreme Court in the case of Gopal & Sons (HUF) (sura). Even a beneficial shareholder holding substantial interest in the lender company will also come within the provisions of Section 2(22)(e) of the Act. Even if a company is not a registered shareholder in lending

company, once the payment is received by a firm or company who is shareholder in lending company has substantial interest, the payment made to such company shall construed as deemed dividend in the hands of the company or firm as per Explanation (3) to Section 2(22)(e) of the Act. The relevant portion of the order is extracted below: -

“Section 2(22)(e) creates a fiction, thereby bringing any amount paid otherwise than as a dividend into the net of dividend under certain circumstances. It gives an artificial definition of ‘dividend’. It does not take into account that dividend which is actually declared or received. The dividend taken note of by this provision is a deemed dividend and not a real dividend. Loan or payment made by the company to its shareholder is actually not a dividend. In fact, such a loan to a shareholder has to be returned by the shareholder of the company. It does not become income of the shareholder. Notwithstanding the same, for certain purposes, the Legislature has deemed such a loan or payment as ‘dividend’ and made it taxable at the hands of the said shareholder. It is, therefore, not in dispute that such a provision which is a deemed provision and fictionally creates certain kinds of receipts as dividends, is to be given strict interpretation. It follows that unless all the conditions contained in the said provision are fulfilled, the receipt cannot be deemed as dividends. Further, in case of doubt or where two views are possible, benefit shall accrue in favour of the assessee. [Para 12]

In the instant case, the payment in question is made to the assessee which is a HUF. Shares are held by Karta of this HUF. The said Karta is, undoubtedly, the member of HUF. He also has substantial interest in the assessee/HUF, being its Karta. It was not disputed that he was entitled to not less than 20 per cent of the income of HUF. In view of the aforesaid position, provisions of section 2(22)(e) get attracted and it is not even necessary to determine as to whether HUF can, in law, be beneficial shareholder or registered shareholder in a company. [Para 16]

It is also found as a fact, from the audited annual return of the company filed with ROC that the money towards shareholding in the company was given by the assessee/HUF. Though, the share certificates were issued in the name of the Karta, Gopal Kumar Sanei, but in the annual returns, it is the HUF which was shown as registered and beneficial shareholder. In any case, it cannot be doubted that it is the beneficial shareholder. Even if it is presumed that it is not a registered shareholder, as per the provisions of section 2(22)(e), once the payment is received by the HUF and shareholder (Karta, in this case) is a member of the said HUF and he has substantial interest in the HUF, the payment made to the HUF shall constitute deemed dividend within the meaning of clause (e) of section 2(22). This is the effect of Explanation 3 to the said section. Therefore,

it is no gainsaying that since HUF itself is not the registered shareholder, the provisions of deemed dividend are not attracted. [Para 17]"

14. In this case the undisputed fact is that common shareholders having substantial share holding in assessee company as well as lender companies. Therefore we are of the view that the loans and advances received by the assessee from the two companies comes within the ambit of provisions of Section 2(22)(e) of the Act. The CIT(A), without appreciating the facts, deleted the addition made by the AO towards deemed dividend under Section 2(22)(e) of the Act. Hence we reverse the findings of the learned CIT(A) and upheld the addition made by the AO towards deemed dividend under Section 2(22)(e) of the Act.

15. In the result, the appeal filed by the Revenue is partly allowed.

16. The facts and issues in ITA No. 5971/Mum/2014 are identical to the issues already considered by us in the preceding paragraphs in ITA No. 5549/Mum/2014. The reasons given by us in the preceding paragraphs were mutatis mutandis apply to this appeal also. Therefore for the same reasons we partly allow the appeal filed by the Revenue.

17. In the result, the appeals filed by the Revenue for both the assessment years are partly allowed.

Order pronounced in the open court on 21st August, 2018.

Sd/-
(Mahavir Singh)
Judicial Member

Sd/-
(G. Manjunatha)
Accountant Member

Mumbai, Dated: 21st August, 2018

Copy to:

- 1. The Appellant*
- 2. The Respondent*
- 3. The CIT(A) -13, Mumbai*
- 4. The CIT - 7, Mumbai*
- 5. The DR, "E" Bench, ITAT, Mumbai*

By Order

//True Copy//

*Assistant Registrar
ITAT, Mumbai Benches, Mumbai*

n.p.