

Inter corporate deposit taken from sister concern is taxable as deemed dividend. However, payment for purchase of machinery on behalf of taxpayer and issue of debentures are not taxable as deemed dividend

The Mumbai Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Jasubhai Engineering Pvt. Ltd.¹ (the taxpayer) dealt with the issue of taxability of the amounts received from sister concern towards inter-corporate loan, issue of debentures and payment made on behalf of the taxpayer for purchase of machinery, etc. as deemed dividend. The Tribunal held that inter corporate deposit taken from sister concern is to be treated as deemed dividend. However, payment made for purchase of machinery by a sister concern on behalf of the taxpayer is not in the nature of deemed dividend as it was a business transaction. Further payment received from sister concern for issue of debenture was not taxable as deemed dividend.

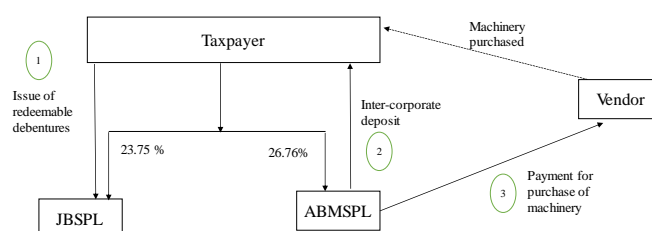
Facts of the case

The taxpayer is engaged in the business of manufacturing of engineering goods and is a shareholder in number of companies. During the assessment year²:

- The taxpayer has taken an inter-corporate deposit from ABMSPL³.
- ABMSPL also made payment of INR 1.723 million on behalf of the taxpayer for purchase of machinery in return for the manufacturing assets purchased by the taxpayer in FY 13-14.
- The taxpayer issued debentures to JBSPL⁴ and the same were subscribed. During the year debentures were redeemed by the taxpayer.

The Assessing Officer (AO) observed that ABMSPL and JBSPL were not companies in which public were substantially interested and the taxpayer was holding beneficial interest in these companies. Therefore, the AO made addition by invoking deemed dividend provisions. The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the order of the AO.

Diagram



Tribunal's decision

The taxpayer was having substantial interest in both the companies and deemed dividend provisions⁵ could be attracted in both the cases. The loan can be called by any name but ultimately the taxpayer has taken benefit/credit. It is settled law that deemed dividend provisions get attracted as soon as taxpayer takes benefit and it does not matter whether it was repaid within the same year. Therefore, any credit or advantage taken by the persons having substantial interest will attract the deemed dividend provision. The Tribunal relied on the decision of the Supreme Court in

⁵ Section 2(22)(e) of the Act

¹ ACIT v. Jasubhai Engineering Pvt Ltd (ITA No. 7519/Mum/2016, AY 2013-14) - Taxsutra.com

² Assessment Year 2013-14

³ The taxpayer was holding beneficial interest in ABMSPL

⁴ The taxpayer was holding beneficial interest in JBSPL

the case of Miss P. Sarda⁶ and held that even though the taxpayer claimed it as inter corporate deposit, the literal meaning would remain same as the short-term loan enjoyed by the taxpayer and hence the deemed dividend provision was attracted.

With regard to the payment for purchase of machinery on behalf of the taxpayer it was observed that ABMSPL had purchased similar machinery from the taxpayer in the subsequent assessment year and it was a back to back purchase of machinery. Therefore, it was a business transaction and deemed dividend provision cannot be attracted.

With regard to issue of debentures, the Tribunal observed that the transaction was of issue of securities, even though it was a private placement. Thus, it cannot be considered as a loan transaction. The deemed dividend provisions were attracted only when loan and advances taken in place of direct issue of dividends. The securities in the form of debentures were separate script having standalone capital liability, which cannot be equated with loan, which is a current liability.

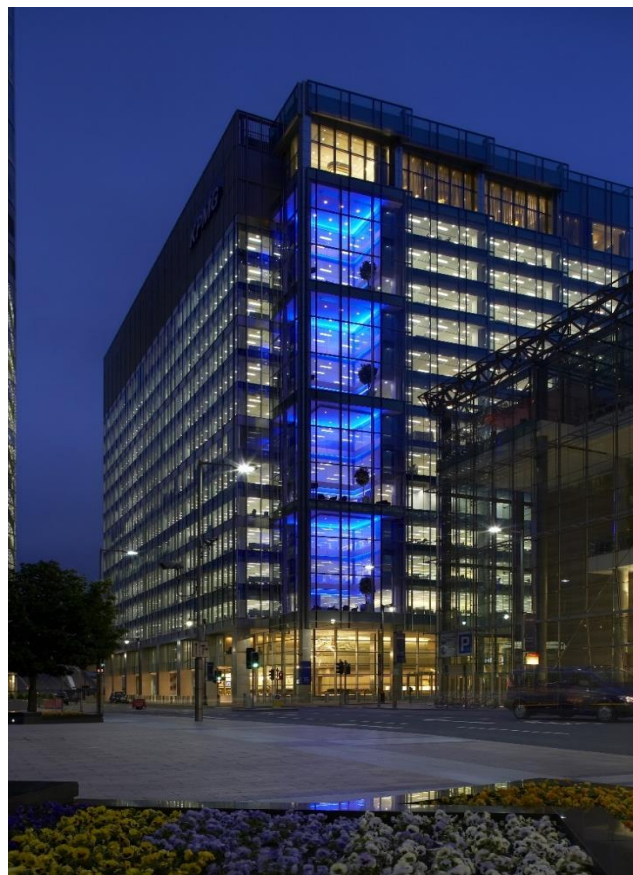
Our comments

The issue with respect to taxability of different forms of loans or advance given to a shareholder by a sister concern has been a matter of debate before the Courts/Tribunal.

The Courts/Tribunal in various cases⁷ have held that loans or advance received by a shareholder from its sister concern were in the nature of trade advance and it cannot be treated as deemed dividend under Section 2(22)(e) of the Act.

The Mumbai Tribunal in the case of KIIC Investment Company⁸ observed that an inter corporate deposit cannot be equated with a loan and therefore does not come under the purview of 'deemed dividend'.

The Tribunal in the present case has held that inter corporate deposit taken from a sister concern was to be treated as deemed dividend. However, the payment made for purchase of machinery by a sister concern on behalf of the taxpayer was not in the nature of deemed dividend as it was a business transaction. Further payment received from sister concern for issue of debenture was not taxable as dividend.



⁶ Miss P. Sarda v. CIT [1986] 29 ITR 444 (SC)

⁷ Bagmane Constructions Pvt. Ltd. v. CIT (ITA No. 473/2013, 474/2013, 475/2013, 476/2013), Asian Business Connections (P.) Ltd. v. DCIT [2019] 179 ITD 595 (Indore), CIT v. Raj Kumar [2009] 181 Taxmann 155 (Del), IFB Agro Industries Ltd. v. JCIT [2014] 42 Taxman.com 246 (Kol), DCIT v. Ernst & Young Pvt. Ltd. (ITA No.978/Kol/2011, CIT v. Atul Engineering Udyog (ITA No. 223 of 2011, AY 2006-07)

⁸ KIIC Investment Company v. DCIT (ITA NOS. 1381/MUM/2017) (Mum)

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