C.I.T. ANDHRA PRADESH

v.

C. P. SARATHY MUDALIAR

October 12, 1971

[K. S. HEGDE AND H. R. KHANNA, JJ.]

Income-tax Act, 1922, *s.* 2(6*A*)(*e*)—*Dividend—H.U.F. holding shares in names of its members—HUF not registered as shareholder—Loans to HUF by company not dividend within meaning of s.* 2(6*A*)(*e*).

The assessee was a Hindu undivided family. Three members of the family namely, S and his two sons were shareholders in a private limited company which was not a company in which the public were substantially interested within the meaning of s. 23A of the Income-tax Act, 1922. In the account years relevant to the assessment years 1955-56, and 1956-57 the company advanced certain loans to the aforesaid Hindu undivided family. The question arose whether these loans could be considered as 'dividend' within the meaning of that expression in s. 2(6A)(e) of the Act. The Income-tax Appellate Tribunal found as a fact that the loans in question had been granted to the H.U.F. It further held that the loans advanced to the H.U.F. could not be considered as loans advanced to the 'shareholders' within the meaning of s. 2(6A)(e). The High Court in reference upheld the view taken by the Tribunal. In appeal to this Court by the Revenue,

HELD : It is well settled that an HUF cannot be a shareholder of a company. The shareholder of a company is the individual who is registered as the shareholder in the books of the company. The H.U.F., the assessee in the present case, was not registered as a shareholder in books of the company nor could it have been so registered. Hence, there was no gain-saying the fact that the H.U.F. was not the shareholder of the company. [1081 B—C]

Section 2(6A)(e) gives an artificial definition of 'dividend'. It does not take in dividend actually declared or received. The dividend taken note of by that provision is a deemed dividend and not a real dividend. The loan granted to a shareholder has to be returned to the company. It does not become the income of the shareholder. For certain purposes the legislature has deemed such a loan as 'dividend'. Hence s. 2(6A)(e) must necessarily receive a strict construction. When s. 2(6A)(e) speaks of 'shareholders' it refers to the registered shareholder and not to the beneficial owner. The HUF cannot be considered as a shareholder either under s. 2(6A)(e) or under s. 23A or s. 16(2) read with s. 18(5) of the Act. Hence a loan given to an HUF cannot be considered as a loan advanced to a 'shareholder' of a company [1081 D—E]

In the present case since no loans were advanced to the shareholders s. 2(6A)(e) was inapplicable. The appeal is dismissed. [1083 B]

Howrah Trading Co. Ltd. v. *C.I.T., Central Calcutta*, 36 I.T.R. 215 and *C.I.T., Bombay City II* v. *Shakuntala & Ors.*, 43 I.T.R. 352, relied on.

Kishanchand Lunidasing Bajaj v. *C.I.T., Bangalore*, 60 I.T.R. 500, distinguished.

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CIVIL APPELLATE JURISDICTION : Civil Appeals Nos. 2242 and 2243 of 1968.

Appeals by special leave from the judgment and order dated March 28, 1967 of the Andhra Pradesh High Court in Case Reference No. 2 of 1961.

B

B. Sen, R. N. Sachthey and *B. D. Sharma,* for the appellant (in both the appeals).

K. Jayaram, for the respondent (in both the appeals).

[The Income Tax Appellate Tribunal stated the case as follows :

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Statement of Case

"The assessee is a Hindu undivided family of which the karta is Sarathy and there are two adult members, Doraiswamy and Singaram. Sarathy holds 2,797 *shares, Doraiswamy* 100 *shares*

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and Singaram 100 *shares of a limited company by name 'The Chittoor Motor Transport Company (Private) Ltd.,' in which the public are not 'substantially interested within the meaning of section* 23*A. The Shares were acquired with the funds of the Hindu undivided family and, therefore, the shares were the property of the Hindu undivided family. There is no dispute about that. The dividend earned on these shares was thus also*

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the income of the Hindu undivided family and was being assessed accordingly. There was no dispute about that either. Sarathy was also the Managing Director of the aforesaid company and the Managing Director's remuneration too was treated and assessed as the income of the Hindu undivided family. There was no dispute about that also.

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In the two assessments made on the Hindu undivided family for the assessment years 1955-56 *and* 1956-57, *for which the relevant 'previous years' are the years ended* 31-3-1955 *and* 31-3-1956, *respectively, two sums of Rs.* 5,790/- *and Rs.* 39,085/- *were treated as its dividend income falling within*

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section 2(6*A*)(*e*) *of the Act in the respective years. The assessee disputed the inclusion on several grounds. Ultimately, the matter came up on appeal before the Tribunal. The three contentions before the Tribunal were :*

(*i*) *The provisions of Section* 2(6*A*)(*e*) *of the Act are ultra vires the Constitution.*

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(*ii*) *There, in fact, was no payment by the aforesaid company by way of advance or loan to the Hindu undivided family and*

(iii) *The deemed dividend could not be assessed as the income of the Hindu undivided family, the Hindu undivided family not being the shareholder to whom the payment of the advance or loan was made.*

The first two of these contentions were rejected by the Tribunal. The first contention, in fact, was expressly given up at the time of the hearing of the appeals. As regards the second, the Tribunal found as a fact that the payment of the advance or loan was to the Hindu undivided family and there was no basis for the claim that the advance or loan was really to another person viz. THE VEGETOLS, Ltd., a limited company to whom the amount was ultimately said to have been lent by the Hindu undivided family. As regards the third contention, relying on the interpretation given to the expression 'shareholder' by the Bombay High Court in the case of S. C. Cambatta, (1946) 14 *I.T.R.* 748, *the Tribunal held that since the Hindu undivided family was not itself and also could not be the registered shareholder of the company, but it was the individual members who as such were the registered shareholders, the advance or loan to the Hindu undivided family, which was not a registered shareholder, could not be treated as the dividend income of the Hindu undivided family. Although in the Bombay case the provisions of Section* 23A, *wherein also there is a provision for treating the deemed dividend as the income of the shareholder, were being considered and in the instant case the provisions of section* 2(6A)(e) *were to be considered, the Tribunal held that the ratio of the Bombay case equally applied, as in both the sections, it was the artificial income that was sought to be taxed and the provisions of the law had, therefore, to be strictly construed. The reasoning of the Tribunal will be found in paragraph* 3 *of its common order dated* 18-1-1960. *A copy on the Tribunal's order is Annexure 'A' hereto and forms part of the case.*

5. *The question of law that, in our opinion, arises is :*

"Whether, on the facts and in the circumstances of the case, the amounts of Rs. 5,790/- *and Rs.* 39,085/- *could be deemed to be the dividend income of the Hindu undivided family in the respective assessment years ?"*

The Judgment of the Court was delivered by

Hegde, J. This is an appeal by special leave from a decision of the Andhra Pradesh High Court. The question of law referred to the High Court under section 66(1) of the Indian Income-tax Act, 1922, (to be hereinafter referred to as "the Act") is "whether on the facts and in the circumstances of the case, the

A amounts of Rs. 5,790/- and Rs. 39,085/- could be deemed to be the dividend income of the Hindu undivided family in the respective assessment years?"

The assessee in this case is a Hindu undivided family. From the case stated it is not possible to state definitely as to how many B coparceners were there in that family. But we gather from the case stated that the three of the members of that family, *viz.* Doraiswamy, Singaram and Sarathy were shareholders in a private limited company by name "The Chittoor Motor Transport Co. (Private) Ltd." Doraiswamy and Singaram held 100 shares each in that company; Sarathy held 2,797 shares. The Tribunal found C that these shares were acquired from out of the family funds. It appears that in the account years relevant to the assessment years 1955-56 and 1956-57 the Chittor Motor Transport Co. (Private) Ltd. advanced certain loans to the Hindu undivided family of which Doraiswamy, Singaram and Sarathy wer coparceners The question arose whether those loans can be considered as "divi-D dend" within the meaning of that expression in section 2(6A) (e) of the Act. The Tribunal found as a fact that the loan in question had been granted to the H.U.F. The assessee contended that the same was taken for making an advance to the Vegetols Ltd. The Tribunal did not examine the correctness of that contention. It was contended on behalf of the Revenue before the Tribunal that the loan in question was advanced to the share-E holders of the company. The Tribunal repelled that contention. It came to the conclusion that though the shares were acquired from out of the family funds in law the shareholders were Doraiswamy, Singaram and Sarathy and not their H.U.F. Hence, the loan advanced to the H.U.F. cannot be considered as loans advanced to the "shareholders" within the meaning of section F 2(6A)(e).

Before the High Court the counsel for the Revenue gave up the contention that the loans in question were advanced to the "shareholders" of the company. On the other hand, he contended that those loans had been advanced on behalf of or for the individual benefit of the shareholders. The High Court did not G accept that contention. It held that as no such case had been taken up before the Tribunal it was not possible to go into that contention. The facts found by the Tribunal did not afford any basis for that contention. In the result, the High Court answered the question referred to it in favour of the assessee.

H Before us Mr. B. Sen, the learned counsel for the Revenue, took up two contentions. His first contention was that the loans advanced were those advanced to the shaleholders of the company. Secondly, he contended that, at any rate, it must be held

that those loans were advanced on behalf of or for the individual benefit of the shareholders. He submitted that the counsel for the Revenue gave up the first contention before the High Court because of certain decisions of this Court and, according to him, those cases cannot be held to have been correctly decided in view of a later decision of this Court.

We shall now proceed to examine the two contentions advanced by Mr. Sen. For doing so, we have to read section 2(6A). That section says :

"2. (6A) 'dividend' includes—

(e) any payment by a company, not being a company in which the public are substantially interested within the meaning of section 23A, of any sum (whether as representing a part of the assets of the company or otherwise) by way of advance or loan to a shareholder or any payment by any such company on behalf or for the individual benefit of a shareholder, to the extent to which the company in either case possesses accumulated profits;

Before a payment can be considered as dividend under section 2(6A)(e) the following conditions will have to be satisfied :—

1. It must be a payment by a company not being a company in which the public are substantially interested within the meaning of section 23A of any sum whether as representing a part of the assets of the company or otherwise by way of advance or loan.

2. (a) It must be an advance or loan to a shareholder, or

2. (b) a payment by the company on behalf or for the individual benefit of the shareholder, and

3. to the extent to which the company in either case possesses accumulated profits.

There is no dispute that first and the last conditions are satisfied in the present case. The question is whether conditions Nos. 2 and 3 are satisfied. We shall first take up condition No. 2(b). No contention appears to have been taken before the Tribunal that the loans in question were given by the company on behalf of the shareholders or for their individual benefit. That being so, the Tribunal did not go into that question. In fact, as can be gathered from the case stated, the contention of the assessee before the Tribunal was that the loan in question was borrowed for the benefit of another company. But the Tribunal did not go into that question. Under these circumstances, the High

A Court in our opinion, was right in not going into that question because on the facts found by the Tribunal it was not possible to decide that contention.

The only surviving question is whether a loan advanced by a B company to a H.U.F., which is the real owner of the shares, can be considered as a loan advanced to its shareholder. It is well settled that an H.U.F. cannot be a shareholder of a company. The shareholder of a company is the individual who is registered as the shareholder in the books of the company. The H.U.F., the assessee in this case, was not registered as a shareholder in books of the company nor could it have been so registered. Hence, C there is no gain-saying the fact that the H.U.F. was not the shareholder of the company. Mr. Sen did not contend otherwise.

Section 2(6A)(e) gives an artificial definition of "dividend". D It does not take in dividend actually declared or received. The dividend taken note of by that provision is a deemed dividend and not a real dividend. The loan granted to a shareholder has to be returned to the company. It does not become the income of the shareholder. For certain purposes, the legislature has deemed such a loan as "dividend". Hence, section 2(6A) (e) must E necessarily receive a strict construction. When section 2(6A) (e) speaks of "shareholder", it refers to the registered shareholder and not the beneficial owner. The H.U.F. cannot be considered as a shareholder either under section 2(6A) (e) or under section 23A or under section 16(2) read with section 18(5) of the Act. Hence a loan given to an H.U.F. cannot be considered as a loan advanced to a "shareholder" of a company.

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Our conclusion in this regard receives support from the decisions of this Court. In *Howrah Trading Co. Ltd.* v. *Commissioner of Income-tax, Central, Calcutta,* (36 I.T.R. 215) this Court had to examine the case of a person who had purchased shares of a company under a blank transfer but in whose name G the shares had not been registered in the books of the company. The question was whether he could be considered as a "shareholder" in respect of such shares for the purpose of section 18(5) of the Act, because of his equitable right to the dividend on such shares and therefore entitled to have that dividend grossed up under section 16(2) by addition of income tax paid by the com- H pany in respect of those shares and claim credit for the tax deducted at the source. This Court held that he cannot be considered as a "shareholder", the reason being that he had not been registered as a shareholder.

In *Commissioner of Income tax, Bombay City II*, v. *Shakuntala & ors.* (43 I.T.R. p. 352) a Hindu undivided family which was the beneficiary of certain shares in a company in which the public were not substantially interested held those shares in the names of different members of the family. The Income Tax Officer applied the provisions of section 23A of the Act (before its amendment in 1955) and passed an order that undistributed portion of the distributable income of the company shall be deemed to be distributed, and the amount appropriate to the shares of the family were sought to be concluded in the income of the family. In that case again this Court ruled that the word "shareholder" in section 23A meant the shareholder registered in books of the company and the amount appropriate to the shares had to be included in the incomes of the members of the family, in whose names the shares stood in the register of the company; and as the Hindu undivided family was not a registered shareholder of the company, that amount could not be considered as the income of the family under section 23A.

From the above decisions it is clear that when the Act speaks of the "shareholder" it refers to the registered shareholder.

Mr. Sen contended that the above two decisions cannot be considered to have laid down the law correctly in view of the decision of this Court in *Kishanchand Lunidasing Bajaj* v. *Commissioner of Income tax, Bangalore,* (60 I.T.R. p. 500). Therein the question was whether a H.U.F. could be charged to tax in respect of dividends received by some of the coparceners of that family in respect of shares held by them, those shares having been purchased from out of the family funds. This court ruled that the dividends paid to the shareholder was the income of the family and that being so, the same was assessable in the hands of the Hindu undivided family. We see no conflict between this decision and the decisions earlier referred to. In the case of actual receipt of dividends there is a receipt of income. That income is received on behalf of the family. Hence, the same was assessable in the hands of the family. In the case of deemed dividends under section 2(6A)(e) the family does not get any income at all. The dividend referred to by that provision is only a deemed dividend and not a real dividend. Hence, no

A income is either received by the family or accrued to it. Therefore, the only person who is deemed to have received that income can be assessed in respect of that income.

Coming to the facts of the present case the loans advanced to shareholders alone can be deemed as dividends. No loans
B had been advanced to shareholders as seen earlier. Hence, the shareholders did not get any income. Hence section 2(6A) (e) became inapplicable.

For the reasons mentioned above these appeals fail and the same are dismissed with costs.

G.C. *Appeals dismissed*