

Diamond Jewellers. This proprietorship concern was converted into a Private Limited Company under the name and style of M/s Radhe Sham Jain Diamond Jewellers Pvt Ltd. on 9.2.2008. The assessee i.e. Shri Radhe Sham Jain was allotted 50% shares and therefore, was a substantial share holder of the said company. During assessment proceedings the AO noticed that the assessee had withdrawn a sum of Rs. 1,81,10,000/- from the said company. On enquiry it was explained that the amount of Rs. 1.50 crores was originally withdrawn by the assessee from capital account in the proprietorship concern, however, the cheque remained un-cleared because the business was taken over by the company. Later on this cheque was returned by Shri Radhe Sham Jain i.e. the assessee to the company and the company had credited the same on 15.3.2008 and all the money has been withdrawn later on only. However, the AO did not find force in the submissions because entry regarding cheque of Rs. 1.50 crores could not be verified from the bank statement. It was further stated that a sum of Rs. 12,34,430.60 was opening credit balance in the capital balance of Shri Radhe Sham Jain which was transferred as credit to his account by the company. In this respect the AO was of the view that this sum was meant for the issue of shares, therefore, the same could not be considered as credit. In this background, he held that sum of Rs. 1,81,10,000/- is to be treated as deemed dividend u/s 2(22)(e) of the Act.

4 Before the Id. CIT(A) the submissions made before the AO were reiterated.

5 The Id. CIT(A) found force in the submissions and observed that a sum of Rs. 1.50 crores was basically on

account of capital of the assessee originally in the hands of the proprietorship concern against which the cheque was issued. Since later on the cheque was returned to the company and the said company has issued the cheque and therefore, withdrawal by the assessee from the company to this extent could not be treated as loan. However, he further noted that on 29.3.2008 that there was a debit balance amounting to Rs. 11,75,565/-. and therefore, to this extent provisions of section 2(22)(e) were applicable. However, he further noted that since accumulated profits were only Rs. 34,858/- therefore, only a sum of Rs. 34,858/- can be treated as deemed dividend. Accordingly he reduced the addition on account of deemed dividend to Rs. 34,858/-.

6 Before us, the Id. DR for the revenue carried us through the assessment order and pointed out that amount of Rs. 1.50 crores was only an adjustment entry as observed by the AO because this could not be verified from the bank statement. He also submitted that the AO was right in observing that a sum of Rs. 12,34,430/- shown as opening balance was towards subscription by the assessee and therefore, credit could not be taken for the same. Thus action of the AO was justified.

7 On the other hand, the Id. counsel of the assessee referred to balance sheet of proprietorship concern, M/s Jain Diamond Jewellers and the capital account of the assessee in the said proprietorship concern. He pointed out that opening balance of capital was Rs. 1,64,34,402/- and the various transactions took place during the year. On 8.2.2008 there was a credit balance of Rs. 1,59,39,810/- and the assessee had withdrawn a capital of Rs. 1.50 crores on that date through a

cheque. The closing balance as on 9.2.2008 was only Rs. 12,34,430/- which was transferred to the company. These figures are reflected in the balance sheet. Since the cheque for Rs. 1.50 crores could not be presented to the bank because of conversion of the proprietorship concern into a Private Limited Company, the sum was shown as liability under the head "cheque issued – OBC". Later on this cheque was returned to the company which was credited by the company to the assessee's account on 15.3.2008 and the money has been withdrawn by the assessee only after the date. Thus at no point of time, there was a debit balance and debit balance arose only on 29.3.2008 amounting to Rs. 11,75,569/-. However, accumulated profits of the company was only Rs. 34,858/- as reflected in the balance sheet of the company. Thus the CIT(A) has correctly applied the provisions of section 2(22)(e) of the Act only to the extent of Rs. 34,858/-. He also referred to ground No. 2 and submitted that Revenue has wrongly taken the ground that accumulated profits could not be taken only at Rs. 34,858/- whereas reserve and surplus account in the balance sheet shows a figure of Rs.11,17,80,000/-. He contended that reserve and surplus account amounting to Rs. 11,17,80,000/- consist of only share premium account which cannot be treated as accumulated profits. In this regard he relied on the decision of Delhi Bench of the Tribunal in DCIT V. MAIPO INDIA LTD. 116 TTJ (Del) 791. He pointed out that the decision has been followed by Mumbai Bench of the Tribunal in case of Ketan B Mehra V ACIT in ITA No. 1939 to 1943/Mum/2010 (Copy of the order enclosed).

8 We have heard the rival submissions carefully in the light of the material on record as well as the decisions cited by the parties. Section 2(22)(e) reads as under:-

“any payment 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) [made after the 31st day of May, 1987, by way of advance or loan to a shareholder, 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**”

The plain reading of above provision clearly shows that the payment by the company in which public is not substantially interested by way of advance or loan to a shareholder who is holding shares not less than 10%, is to be treated as deemed dividend. It is further noted that such deemed dividend can be there only to the extent of accumulated profits.

9 In case before us, there is no doubt that M/s Radhe Sham Jain Diamond Jewellers (P) Ltd is a company in which public is not substantially interested and the assessee i.e. Shri Radhe Sham Jain is holding more than 10% shares. However, the question is whether the said company has given any advance or loan to the assessee or not? The company was incorporated by way of conversion of proprietorship business of Jain Diamond Jewellers on 9.2.2008. Perusal of the balance sheet of the proprietorship concern on 9.2.2008 (See paper book page 1). Clearly shows that there was a capital balance of Rs. 12,34,430/-. There was also a liability on account of cheque issued – OBC to the extent of Rs. 1.50 crores. Perusal of the copy of the capital account of the assessee in the proprietary

concern at page 11 to 13 clearly shows that there was opening capital balance of Rs. 1,64,34,402/-. There are various transactions done in the capital account till 8.2.2008 and there was a credit balance of Rs. 1,59,39,810/- on that date. Against which payment of Rs. 1.50 crores was made by the proprietorship concern to the assessee i.e. Shri Radhe Sham Jain on 8.2.2008. This cheque was not encashed and shown as liability in the balance sheet. Because of the conversion of proprietary concern into a Private Limited company the cheque could not be encashed later on and the same was returned to the Private Limited Company which has been credited by the company to the assessee's account on 15.3.2008. Thus it is clear that this amount belonged to the assessee on account of capital in the proprietorship concern and because the cheque could not be encashed, therefore, the money belonged to the assessee which has credited by the company. The so called cheque on account of loan or advance which have been issued by the Company have been issued only after 15.3.2008. The AO has mainly stressed on the fact that this seems to be adjustment entry. We are of the opinion that the AO has failed to appreciate that because of the conversion of the proprietorship concern, the cheque could only be encashed by the assessee. The cheque has been shown as liability in the balance sheet of proprietorship concern and was later on returned by the assessee to the Private Limited company. Since all the assets have been taken over by the Private Limited company, the said company owned assessee this amount of Rs. 1.50 crores which was credited to his account on 15.3.2008. Because of non encashment of the cheque the same is not reflected in the bank

statement. This fact has been correctly appreciated by the Id. CIT(A).

10 The Id. CIT(A) has further correctly noted that there was definitely a debit balance amounting to Rs. 11,75,569/- on 29.3.2008 in the name of the assessee in the books of the Private Limited company. However, he has correctly restricted the addition to Rs. 34,858/- i.e. to the extent of accumulated profits. There is no force in the ground of the Revenue that accumulated profits are Rs. 11,17,80,000/-. Schedule 'A' at page 17 of the paper book very clearly show that this amount is on account of share premium account and net profit is only Rs. 34,858/-. Delhi Bench of the Tribunal in case of DCIT V. MAIPO INDIA LTD. 116 TTJ (Del) 791 has clearly observed that share premium account could not be taken into consideration as part of the accumulated profits. Head note reads as under:-

“Dividend – Deemed dividend u/s 2(22)(e) – Accumulated Profits – Assessee company received a sum of Rs. 25,42,772/- in the nature of loans and advances from company GCPL, in which assessee-company held 40 per cent shares – Assessee repaid a sum of Rs. 14,31,000/- towards the end of the year and the balance of Rs. 11,11,772/- was treated by AO as deemed dividend – CIT(A) on appeal, found that out of reserves and surplus account of GCPL, Rs. 1.90 crores represented share premium and Rs. 1,85,821/- was on account of balance in profit and loss account which was treated as deemed dividend – Justified – There being a statutory bar u/s 78 of the Companies Act, 1956 on the share premium account being used for distribution of dividend, the deeming provisions of section 2(22)(e) cannot apply – Section 78(1) of the Companies Act, 1956 says that any payment out of the share premium account, except for purposes authorized by sub-section (2) will be treated as reduction of share capital attracting the provisions of the Companies Act in relation thereto – The expression “whether capitalized or not” can have application only where the profits are capable of being capitalized and not where the receipt in question forms part of the share capital of the company under the provisions of the Companies Act – In view of the provisions of the Companies Act, share premium cannot be stated to be commercial profits – Amount of Rs. 1,85,821/- alone out of

the amount of Rs. 25,42,772/- can be assessed as deemed dividend u/s 2(22)(e).”

The above view has been taken particularly following the decision of Hon'ble Supreme Court in case of P.K. Badiani V CIT, 105 ITR 642. In that decision it was clearly observed that accumulated profits would mean profit in the commercial sense and not assessable taxable profits. In that case development rebate reserve created by the company by charging profit and loss account was held to be accumulated profits though the same was liable to be deducted as rebate. Following this ratio it is clear that share premium account would not partake the nature of commercial profits and therefore, by no stretch of imagination, this can be called accumulated profits. Therefore, in case before us accumulated profits can be taken only at Rs. 34,858/- and the Id. CIT(A) has correctly confirmed the addition deemed dividend u/s 2(22)(e) of the Act to the extent of Rs. 34,858/- which has not been challenged by the assessee. In these circumstances we find nothing wrong in the order of the Id. CIT(A) and the same is confirmed.

11 In the result, appeal of the Revenue is dismissed.

Order pronounced on .09.2012

Sd/-
(SUSHMA CHOWLA)
JUDICIAL MEMBER

Sd/-
(T.R. SOOD)
ACCOUNTANT MEMBER

Dated : .09. 2012

SURESH

Copy to: The Appellant/The Respondent/The CIT/The CIT(A)/The DR

