

Advt. exp. couldn't be disallowed just because hoardings were placed at place where co. had no selling outlets

Summary – The Pune ITAT in a recent case of Rajmal Lakhichand, (the Assessee) held that Current year business profits should not be considered as part of accumulated profits for purpose of section 2(22)(e)

Where assessee had not charged interest on advance given to seven parties contending that they were not traceable or in financial difficulties, but not a single evidence was furnished in support of its claim, disallowance under section 36(1)(iii) was to be made

Where assessee had not received any tax free income during assessment year under appeal no disallowance under section 14A read with rule 8D was called for

Expenditure incurred on advertisement for promoting its business could not be disallowed on ground that assessee had put up advertisement hoardings in places where it had no selling outlets

While arriving at business income, deduction of section 40(b) is to be given first and then if at all there remains positive income, brought forward losses are to be set off

Facts

- The assessee was a flagship concern of a Rajmal group. It was a beneficial shareholder in the group companies through its partner (Ishwarlal). It had received advance from group companies.
- The Assessing Officer opined that all advances from group companies fell under purview of deemed dividend under section 2(22)(e).
- The assessee had made two fold submissions against invoking of provisions of section 2(22)(e) that the assessee was a partnership firm and, thus, could not be a registered shareholder in the group companies. The second contention of assessee was that the provisions of section 2(22)(e) were not attracted as debit balances standing in the name of assessee was on account of business transactions.

Held

- Section 2(22)(e) get attracted not only in the case of registered shareholder but also in the case of concern in which such shareholder is a member or a partner having substantial interest. In the present case the assessee-firm was holding share in group companies through one partner, who is having 40 per cent share in the assessee-firm. Hence, Ishwarlal has substantial interest in the

assessee-firm. The assessee is a beneficial shareholder of group companies and is amenable to provisions of section 2(22)(e).

- In view of *Explanation 3* to section 2(22)(e) the provisions of section 2(22)(e) would be applicable to the assessee-firm.
- The second limb of argument of assessee is that the advances received by assessee are in the normal course of business and are trade advances. The term 'loans and advances' has not been defined under the provisions of Act. Therefore, they have to be understood in the commercial sense. It is true that all advances received from group companies cannot be treated as deemed dividend within the meaning of section 2(22)(e).
- In the instant case, the assessee has received advances from group companies which are being carried forward year after year. During the financial year there are substantial purchases and sales of gold, bullion and ornaments between the group concerns. However, a distinguishing feature of the transactions is that there has been substantial opening and closing debit balances. As per details furnished by assessee the opening balances, sales, purchases and closing balances of assessee firm in the books of closely held private companies clearly indicates that closing balances in the case of group companies is much more than the opening balances. In other words during the financial year the assessee has received further advances from group companies. It is an undisputed fact that the debit balances at the end of the year has swollen in assessee's accounts in the books of group concerns. The settled legal position *qua* the provisions of section 2(22)(e) is that the transactions in the current accounts are outside the purview of section 2(22)(e). However, this is a peculiar case where the advances received by the assessee from the group concerns are substantially higher. It is repeatedly submitted by the assessee during the assessment/appellate proceedings that the payments received by the assessee from the group concerns constitutes trade advances on current account. The authorities below having considered the submissions of the assessee but have not rebutted the claim of the assessee in order to treat the excess payments received by the assessee as non-trade advances and not on current account. This is the case where certain questions are left unanswered which are vital for adjudication of the issue under consideration. The key question is whether the excess funds received by the assessee constitute trade advance or otherwise.
- The question as to why group companies paid advances much higher than the transactions, *i.e.*, on account of purchases and sales is also unanswered. Ancillary to the same, there is requirement for the Assessing Officer to probe the treatment of such advances in the earlier and subsequent assessment years, whether, the provisions of section 2(22)(e) were invoked on similar set of facts, *i.e.*, excess payments received by the assessee? Both the sides have failed to provide information on this aspect.
- The exclusion of advance business transactions by way of trade advances from the purview of section 2(22)(e) are required to be examined, if the advances so given are substantially higher than the normal business requirements. In other words, if the payments received by the assessee is say Rs. 100, in what circumstances the assessee receives Rs. 200, should that be construed as business

advances and extend the benefits to the assessee without invoking the provisions of section 2(22)(e) which are otherwise interpreted by applying the principles of literal interpretation.

- The provisions of section 2(22)(e) constitutes deemed provisions. Thus, the provisions need to be interpreted strictly. The initial onus is on the Assessing Officer to demonstrate that the excess payments received by the assessee from the group concerns constitute non-trade advances and not on account of current account to record the business transactions between or among the group concerns. Merely rejecting the explanation of the assessee is not sufficient to invoke the provisions of section 2(22)(e). The Assessing Officer is under statutory obligation to demonstrate the use of excess funds or advances received by the assessee on account of non-business purposes.
- The assessee has submitted that if at all provisions of section 2(22)(e) are to be invoked, the current year business profits should not be considered as part of accumulated profits for the purpose of section 2(22)(e). There is merit in this submission of assessee that accumulated profits for the purpose of section 2(22)(e) do not include current year's business profit, since it accrues only at the end of year. Further, loan or advance treated as deemed income up to date of fresh loan is to be reduced from accumulated profits.
- In view of the facts of the case, this issue needs revisit to the file of Assessing Officer. The Assessing Officer shall decide the issue *de novo* in the light of above observations after affording opportunity of hearing to the assessee, in accordance with law.