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Inter-corporate deposits are distinct from 'loans' or 'advances' and cannot be taxed as deemed dividend under section 2(22)(e) of the Income-tax Act.

Facts

Bombay Oil industries Limited ("BOI"), the assessee, had obtained unsecured loans from various companies. The Assessing officer ("AO") invoked the provisions of section 2(22)(e) of the Income-tax Act ("ITA") and sought to tax these amounts as 'deemed dividend'.

BOI raised the following contentions before the AO:

- it had accepted these inter-corporate deposits ("ICD") as a means of alternative finance and such ICDs cannot be treated as 'loans' or 'advances' under section 2(22)(e) of the ITA;
- As per section 2(22)(e) of the Act, the scope of 'dividend' excludes any advance or loan made to a shareholder by a company in the ordinary course of its business. As the ICDs were provided to it by the companies in the ordinary course of their business, these cannot be treated as 'dividend'.

The AO rejected the contentions of BOI and treated the ICDs as deemed dividend under section 2(22)(e) of the ITA. The Commissioner (Appeals), based on the details provided by BOI, held that lending of money was not a substantial part of the business of the lender companies and is therefore not covered by the exception clause of section 2(22)(e). The Commissioner (Appeals) accordingly upheld the view taken by the AO.

On appeal to the Mumbai Tribunal ("ITAT"), BOI reiterated the facts and submissions made with the AO and Commissioner (Appeals) and also relied upon various judicial precedents to bring out the distinction between 'loans' or 'advances' and deposits. It also contended that the provisions of section 2(22)(e) contain a deeming fiction which has to be strictly interpreted within the framework of the particular section.

Observations / Ruling of the ITAT

- Requisite condition for invoking section 2(22)(e) of the ITA is that the payment

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must be by way of 'loans' or 'advances'.

- Section 2(22)(e) enacts a deeming fiction whereby the scope of the word 'dividend' has been enlarged to bring within its ambit certain specified payments made by a company. Such a deeming fiction cannot be given a meaning wider than what it purports to do.
- The lower authorities have not controverted the claim of BOI that the amounts received from the companies were ICDs.
- The distinction between 'deposits' and 'loans' has been recognised by various judicial precedents.

Based on the above observations, ITAT held that there is a clear distinction between deposits and 'loans' or 'advances' and hence, ICDs do not fall within the purview of deemed dividend under section 2(22)(e) of the ITA.

Conclusion

This ruling acts as another precedent to shareholders holding prescribed proportion of shares in their closely held companies and who have obtained deposits from such companies directly or through a specified concern.

Source: Bombay Oil Industries Ltd. v. Deputy Commissioner of Income-tax, ITA No. 2985/2005 (Mumbai Bench)

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