VERENDRA KALRA & CO
CHARTERED ACCOUNTANTS

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HC dismisses Revenue's appeal qua TP-adjustment for management fees sans substantial question of law; Follows earlier order

Facts

The revenue against the order passed by the ld. Tribunal has raised the following substantial questions of law as to whether the ld. Tribunal has erred in law in:

- Determining the payment under the head of management support service at Arm's Length Price when the provision of Section 92C and r.w.r. 10B & Rule 10C allows for "Reliable and accurate adjustment" to account for difference between intonated transaction and comparable uncontrolled transactions?
- Allowing the depreciation on Intellectual property rights u/s 32, considering Intellectual property Rights as technical known now?
- Treating the provision of obsolescence of inventory or ascertained liability where are no cogent material is unavailable to sustainable the valuation of inventory?
- In granting relief to the assessee to the tune of INR 5.04 crores on account of additions pertaining to "Adjustment in Transfer Pricing in respect of International Transactions",
- In granting relief to the assessee to the tune of INR 0.34 crores on account of additions pertaining to "Depreciation on Intellectual property Assets",
- In granting relief to the assessee to the tune of INR 0.11 crores on account of additions pertaining to "Provision on obsolescence of inventory"

Source: HC, Calcutta in PCIT vs Landis Gyr vide [TS-260-HC-2023(CAL)-TP] on May 09, 2023

Ruling

- HC for (i) and (iv) upheld the order passed by the ld. Tribunal on the ground that the revenue has not been able to point out any distinctive feature for us to take a departure from the consistent manner in which the relief was granted and therefore the issues were decided in favour of the assessee.
- For substantial questions of law (ii) and (v), HC has upheld the order of the Tribunal answering the appeal in favour of the assessee for AY 2007-08 and 2008-09. HC stated that, in the absence of any distinguishing feature pointed out by the Revenue before us, the order impugned passed by the Tribunal on those issues does not call for interference.
- With regard to substantial questions of law (iii) and (vi), HC again upheld the decision of the ld. Tribunal placing reliance on the decision of the **Hon'ble Delhi High Court in CIT vs. Hotline Teletube & Components Ltd.** HC also upheld the facts of the case and found from the workings that the assessee has clearly mentioned the item code, description of item available in the inventories, date of last transaction, quantity, rate per unit and the value together with the time periods from the date of sale to decide the relevant provision percentage. HC upheld the findings of the Tribunal having examined that no substantial questions of law arise for consideration in the present case.

TPO to pass fresh order uninfluenced by Tribunal's observations on manner of ALP determination

Facts

The Revenue has filed this appeal, aggrieved by the order passed by the ld. Tribunal on 17-08-16 allowing the assessee's appeal and remanding the case back to the Transfer Pricing Officer (TPO) for the AY 2009-10. The only grievance raised by the ld. counsel of the assessee is that while remanding the case back to the TPO, the ld. Tribunal should not have made observations on the merits of the Transfer Pricing adjustment which has to be considered by the TPO upon such remand. The counsel of the assessee also held that in the first round of litigation itself and he had taken a particular stand in the matter and therefore, the Tribunal has made such impugned observation while remanding the case back to the TPO.

Source: HC, Madras in PCIT vs Motonic India Automotive Pvt. Ltd. vide [TS-1266-HC-2019(MAD)-TP] on May 26, 2023

Ruling

- HC held that while remitting the matter back to the TPO, the Tribunal should not have curtailed the discretion to be exercised by the TPO, in accordance with law. The Tribunal was well within the powers to allow the new additional grounds raised by the assessee before it, but when the matter was being remitted back to the TPO, the directions of mandatory nature as to how to make adjustments only in a particular manner, etc. would frustrate the very purpose of remand.
- HC further stated that it is clear that though the issue relating to Customs Duty Adjustment, Air Freight Adjustment and the TPO for determining the Arm's Length Price (ALP) in the case of the assessee, the Tribunal has, in fact, fixed how such adjustments have to be made or not to be made. This hardly leaves any discretion to deal with these issues afresh with the TPO, since the TPO, being the lower Authority, would be bound by the observations and findings of the Tribunal. The very purpose of remand for enquiry by the TPO into these three issues has not been fulfilled. Therefore, the present appeal of the Revenue and while upholding the remand order passed by the Tribunal, observe that the TPO will pass such fresh order in pursuance of the remand directions, uninfluenced by the observations of the Tribunal, on the merits of the case. It goes without saying that the Assessee will be again given the due opportunity of hearing to make out its case before the TPO and fresh orders may be passed, after providing reasonable opportunity of hearing. The appeal of the Revenue was thus allowed.

ITAT following Watermarke ruling upholds Revenue's benchmarking of interest on FCCDs @ LIBOR+ 200 bps

Facts

The assessee is a foreign company incorporated in Cyprus and is engaged in the business of real estate and development. The assessee e-filed its original return of income for AY 2014-15 declaring income of INR 16.72 crores and subsequently, a revised return was filed declaring a refund of INR 5.48 crores. Subsequently, the case was selected for scrutiny and accordingly, notice u/s 142(1) dated 07-06-16 was issued and duly served. Thereafter, notices u/s 142(1) were also duly issued and served after which the case was referred to the TPO for determination of Arm's Length Price (ALP) and the TPO on examination of international transactions rejected the Transfer Pricing analysis but did not propose for any adjustment of income as the same has been proposed in case of WRPL on the same transaction to benchmark the interest paid/payable on FCCD's denominated in INR at LIBOR plus 200 basis points. A copy of TPO order of WRL was forwarded to the appellant and notice was issue by the AO asking to show cause as to why excess interest income of INR 13.98 crores be not taxed at 40% plus surcharge relying on article 11(7) of India-Cyprus DTAA. The assessee contended since the FCCD's are in the nature of equity instruments and are denominated in INR and interest on the same is payable in INR, the same has to be benchmarked at the currency specific interest rate benchmark of SBI PLR. However, the AO had adopted LIBOR plus 200 basis points as more appropriate to determine the arm's length price, rejecting the SBI PLR plus 300 basis points adopted by the appellant. Finally, the AO had taxed the excess interest of INR 13.98 crores at 40% and ALP of INR 2.74 crores is taxed at DTAA rate of 10% and passed assessment order u/s 143(3) r.w.s 144C. Feeling aggrieved with the final assessment order, assessee carried the matter before ld. CIT(A), who granted partial relief to the assessee. Feeling aggrieved with the order of ld. CIT(A), both the assessee and Revenue are now in appeal before the ITAT.

Ruling

ITAT stated that admittedly, the interest as computed by the AO pursuant to the application of applying LIBOR + 200 points was confirmed by the Tribunal in the case of Watermarke Residency Limited. Now the issue is that whether only 10% of the gross amount of the interest is required to be taxed in the hands of the assessee and the remaining interest amount cannot be taxed as per clause 7 of Article 11 of the DTAA or not? In this aspect, the ld. Tribunal held that the conjoint reading of Clauses 2 and 7 of Article 11 of DTAA made it abundantly clear that interest paid over and above the interest mentioned in clause 7 of Article 11 of DTAA, shall be chargeable at Income Tax rate as applicable in Contracting State namely, India, as mentioned in Article 11(7) of DTAA. In furtherance to this, ITAT stated that, we do not find any error in the order passed by the lower authorities. During the course of argument, the ld. AR had vaguely argued that excess amount of the interest paid/received by the assessee shall be chargeable under the head “Income from business” and thereafter, it may be taxed under the other provisions of DTAA. In our view, the Assessing Officer/ld. CIT(A) cannot be changed the characteristics of “head of income” when the assessee itself has admitted that the amount received by it was in the nature of interest only and hence, it would be improper either on the part of the AO or the assessee to change or recharacterize the amount received by it as “business income” within the meaning of DTAA. Once the assessee itself admits that the amounts received by it on the FCCDs were in the nature of “Interest income”, then the same cannot be converted into “income from business” and therefore, the submissions of the ld. AR are without any basis and hence, the same are rejected. Accordingly, the appeal of the assessee was dismissed.

Source: ITAT, Hyderabad in Fairfield Developments Limited vs DCIT vide [TS-256-ITAT-2023(HYD)-TP] on May 05, 2023

Exchange rate on date of shipment and not agreement to be considered for adjustment qua freight charges payment

Facts

The return of income for the AY 2009-10 was filed by the assessee company on 30-09-09 declaring total income of INR 13.82 crores. Considering the international transactions carried out by the assessee with its AEs amounting to more than INR 15 crores, the Ld. AO made a reference u/s 92CA(1) to the ld. TPO after obtaining the prior approval of the ld. CIT. The ld. TPO observed that during the year under consideration, the assessee had taken ships on voyage charter from Tolani Shipping (Singapore) Pvt. Ltd, an Associated Enterprise (AE). The Voyage rates which assessee had paid to the AE was comparatively favorable with the then prevailing market fixtures that have been concluded by TRANSCHART, New Delhi, which is the chartering wing of the Ministry of Surface Transport, Govt. of India. The assessee also furnished the copies of confirmation received from the relevant broker for the relevant market transaction which indicated coal freight rate prevailing at the time of entering into an agreement with the AE.

The ld. TPO observed that assessee had incurred a loss of INR 21.40 per MT on handling of cargo from Australia to India. Moreover, the ld. TPO adopted the metric tonnes mentioned in the agreement and the exchange rate of USD to Indian rupees prevailing on the date of agreement to determine the freight charges payable by the assessee. The ld. TPO, however, did not agree with the contentions of the assessee and proceeded to make a transfer pricing adjustment of INR 11.77 crores towards ALP adjustment on account of payment for freight without considering demurrage and brokerage charges thereon. Aggrieved by this, the assessee is in appeal before the ld. Tribunal.

Ruling

ITAT held that for the purpose of benchmarking the international transactions, actual quantity i.e. the subject matter of shipment should be considered together with the exchange rate prevailing on the date of shipment. The purpose of transfer pricing regulation in Chapter X is only to ensure that on the date of relevant international transaction, whether the transaction had been carried out by the assessee with the AE at arm's length. The quantity to be shipped as mentioned in the agreement and exchange rate prevailing on the date of agreement is only a promise or a contract entered into between assessee and other parties. That promise gets fructified/materialized only when actual shipment is made. Hence, the benchmarking of the said international transaction should be done on the date of actual shipment of the goods by applying the exchange rate of conversion of USD into Indian rupees prevailing on the date of the said transaction and not on the date of agreement. In our considered opinion, the interpretation of provisions of Chapter X in this manner alone would be just and fair and serve the intended purpose of the said Chapter. When this is done, there will be no scope of any ALP adjustment in respect of freight charges paid by the assessee as is evident from the aforesaid table. Hence, the ld. AO/TPO was directed to delete the ALP adjustment made in the sum of INR 11.77 crores. Accordingly, the grounds raised by the assessee were allowed.

Source: ITAT, Mumbai in Tolani Shipping Co. Ltd vs DCIT vide ITA No. 1755/Mum/2014 on May 29, 2023

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