TRANSFER PRICING

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Dell International Services India Private Limited v/s JCIT, LTU IT(TP)A No.130/Bang/2014

Dell International Services India Pvt Ltd (" assessee"), a private limited company was engaged in the business of development and export of computer software and Information Technology Enabled Services. For AY 2009-2010, assessee paid royalty @3% on sales to third party customers. The assessee selected Transaction Net Margin Method ("TNMM") as the Most Appropriate Method ("MAM") and computed its margin at 33.37% on operating cost (which included royalty payment) in respect of its software development segment. The assessee carried out search for third party comparables using Prowess and Capitaline Database and applying certain qualitative and quantitative filters, arrived at 24 companies in the comparable list with the arithmetical mean profit of 21.84%. Accordingly, the profit margin earned by the assessee at 33.37% on operating cost was treated as arm's length.

Based on a TPO reference by the AO, The TPO held that no independent party would pay royalty under similar circumstances. Therefore, the TPO determined the ALP of the international transaction in respect of "royalty" as Nil by applying test which he felt were relevant in determining the ALP of intra-group services. Separately, with reference to the transaction of outstanding receivables from AE, the TPO treated the debts outstanding for a period of more than six months in respect of transaction with assessee's AEs as a deemed loan and applied CUP method to benchmark the transaction on adhoc basis.

DRP concurred and affirmed the 'NIL' ALP of royalty payment under CUP method and for outstanding receivables, directed the AO / TPO to remitted verification of the working capital adjusted margins of the assessee from which the outstanding receivables emanated and if the same were found to be at ALP then directed no separate adjustments for the interest on outstanding receivable.

Bangalore ITAT held that the royalty payment under aggregated benchmarking vide TNMM is at an ALP. ITAT noted that "Thus, when the segment level profit margins are accepted by the TPO, it is impermissible to isolate the royalty payment and 'Separately evaluate the ALP of the same." ITAT considered TNMM as MAM for the instant case of assessee. ITAT observed that TNMM required establishing comparability at a broad functional level, requiring comparison between net margins from AE transactions with similar non –AE transactions and therefore removed the limitations of other methods (since the comparison was made at the net profit level). ITAT further held that TNMM was the only method where comparison was possible (wherein, for differences in the transactions, reasonable adjustments to the comparable transaction could be made). On aggregation of royalty under TNMM, ITAT, while placing reliance on the decisions of Hon'ble Delhi HCs in Sony Ericsson Mobile Communications India and Maruti Suzuki India, noted that the said HC decision was also relied on by the co-ordinate bench in the case of Toyota Kirloskar Motor, wherein, approach of benchmarking on aggregated basis was upheld.

With respect to interest on outstanding receivables, ITAT noted that interest was not charged on both AE and non-AE sales. ITAT further observed that Hon'ble Rajasthan HC in the case of Sharda Spuntex P had upheld non charging of interest on AE debts when said practice was not observed w.r.t non-AE debtors. ITAT while holding outstanding receivables from AE to be an 'international transaction', opined the same to be closely linked to sales to AE. It therefore remitted for verification the working capital adjusted margins of assessee for making adjustment, if any, for interest on outstanding receivables for assessee.