The Institute of Chartered Accountants of India - WIRC

CASE LAWS AND CASE STUDIES RELATING TO TRANSFER PRICING

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ABBREVATIONS

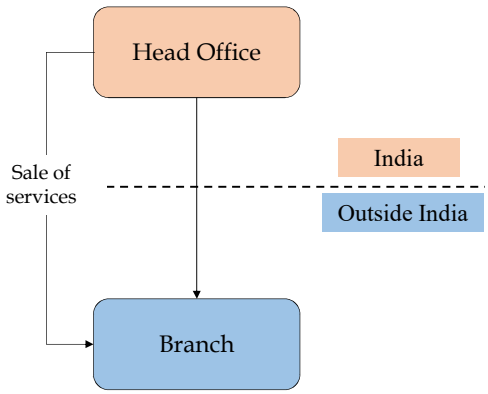
ABBRV	PARTICULARS
AE	Associated Enterprise
ALP	Arm's Length Price
DTAA	Double Taxation Avoidance Agreement
HO	Head Office
IPR	Intellectual Property Rights
IT Rules	Income Tax Rules, 1962
The Act	Income Tax Act, 1961

ABBRV	PARTICULARS
PE	Permanent Establishment
OECD TP Guidelines	OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations – July 2017 Edition
TP	Transfer Pricing
UN TP Manual	United Nations Practical Manual on Transfer Pricing for Developing Countries - 2017 Edition

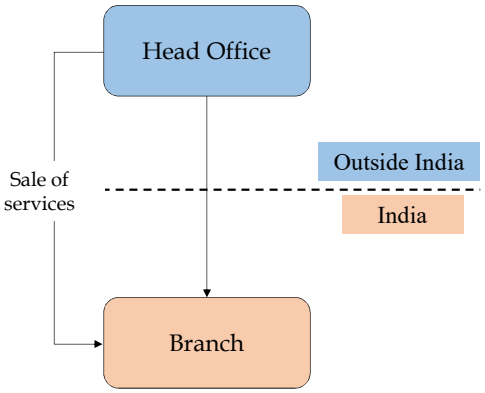
CASE STUDY 1 – HEAD OFFICE & BRANCH TRANSACTIONS

CASE STUDY

Scenario 1: Foreign Branch of an Indian Entity



Scenario 2: Indian Branch of a Foreign Entity



ANALYSIS

Section 92B(1) – **International transaction**

*"a transaction between two or more **associated enterprises**, either or both of whom are non-residents, in the nature of purchase, sale or lease ……"*

Section 92A(1) – **Associated Enterprise**

*"AE in relation to another enterprise, means **an enterprise** which participates….in the management or control or capital of the other enterprise……"*

Section 92F(iii) – **Enterprise**

"enterprise means a person (including a permanent establishment of such person) who is, or has been, or is proposed to be, engaged in any activity...."

ANALYSIS (cont'd…)

❑ Relationship between HO and Branch

Branch is *NOT* distinct from HO

- Elder Exim vs. DCIT [2017] (ITA No. 5385/Mum/2014) (Mum.);
- Sumitomo Mitsui Banking Corpn. vs. DDIT (IT) [2012] (19 taxmann.com 364) (Mum.) (SB);
- Semantic Space Technologies Ltd vs. DCIT [2012] (ITA No.824/Hyd/2010) (Hyd Trib.);
- Aithent Technologies (P.) Ltd. vs. DCIT [2016] (74 taxmann.com 214) (Delhi Trib.);

Distinct Entities

- Definition of 'enterprise' [section 92F(iii)] – 'person' **includes** a 'PE of a person'

CAN BRANCH AND HO BE CONSIDERED AS DISTINCT ENTITIES???

- Dresdner Bank AG vs. ACIT [2006] (108 ITD 375) (Mum.) – Branch hypothetically treated as independent entity to compute profits attributable to the Branch

ANALYSIS (cont'd…)

If HO and Branch are considered as **distinct entities**

↓

Branch derives its residential status from its HO

Foreign Branch of Indian Company

- **Status of Foreign Branch = Resident** as HO is resident in India;
- Transaction between two residents;
- Not an international transaction (section 92B) as none of the parties are non-residents;
- Global income of Indian Company (HO) is taxable in India – Hence, **tax neutral;**
- Aithent Technologies (P.) Ltd. *(supra)* – TP provisions not applicable

Indian Branch of Foreign Company

- **Status of Indian Branch = Non-Resident** as HO is non-resident;
- Transaction between two non-residents;
- Qualifies as an international transaction (section 92B) as both the parties are non-residents;
- Dresdner Bank AG *(supra)* – TP provisions apply to transactions between Foreign Company and Indian Branch

ANALYSIS (cont'd…)

- Article 7(2) of UN TP Manual:

  "where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the profits which it might be expected to make ***if it were a distinct and separate enterprise engaged in the same or similar activities*** *under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment"*

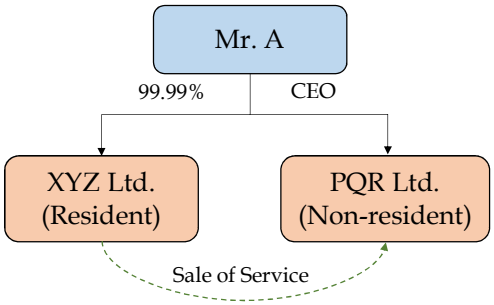
- DTAA recognises PE as a distinct entity, for the purpose of attribution of profits;

- Interplay between Indian TP Regulations and Article 7(2);

CASE STUDY 2 – INTERPLAY BETWEEN SECTION 92A(1) & 92A(2)

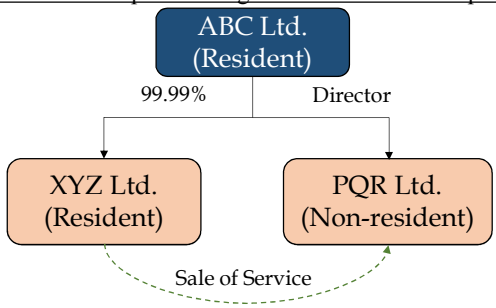
CASE STUDY

Scenario 1: Individual having control over two enterprises



- Mr. A holds 99.99% in XYZ Ltd. and acts as the CEO of the Foreign Co., PQR Ltd.;
- XYZ Ltd. received service charges from POR Ltd.;

Scenario 2: Enterprise having control over two enterprises



- ABC Ltd. holds 99.99% in XYZ Ltd.;
- Mr. M, employee of ABC Ltd. has been appointed as nominee director in PQR Ltd. on behalf of ABC Ltd.;
- XYZ Ltd. received services charges from POR Ltd.;

ANALYSIS

Section 92A(1)

"associated enterprise", in relation to another enterprise, means an enterprise –
*(a) which **participates**, directly or indirectly, or through one or more intermediaries, **in the management or control or capital** of the other enterprise; or*
(b) in respect of which one or more persons who participate, directly or indirectly, or through one or more intermediaries, in its management or control or capital, are the same persons who participate, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise.

Section 92A(2)

For the purposes of sub-section (1)*, two enterprises shall be deemed to be associated enterprises if, at any time during the previous year, –*
…….

(j) where one enterprise is controlled by an individual, the other enterprise is also controlled by such individual or his relative or jointly by such individual and relative of such individual;

**Inserted vide Finance Act, 2002*

ANALYSIS (cont'd…)

- Two plausible views:

1. Sub-section (1) & (2) of section 92A are **independent of each other**

2. Sub-section (1) & (2) of section 92A **operate jointly**

ANALYSIS (cont'd…)

1. Sub-section (1) & (2) of section 92A are <u>independent of each other</u>

- If conditions under sub-section (1) are fulfilled, two enterprises will be treated as AEs;
- Sub-sec. (2) is a **deeming fiction** – expands/enlarges the scope of AE provided under sub-section (1);
- Sub-sec. (1) **does not** begin with a **subjective clause** "subject to sub-section (2)";
- Whereas sub-sec. (1) provides basic rule - de facto control on decision making, sub-sec. (2) gives practical illustrations of such control;
- Case Laws:
  - Kaybee (P.) Ltd. vs. ITO [2015] 171 TTJ 536 (Mum.);
  - Diageo India (P.) Ltd. vs. DCIT [2011] 142 TTJ 287 (Mum.);

ANALYSIS (cont'd…)

2. Sub-section (1) & (2) operate <u>jointly</u>

- Explanatory Memorandum to Finance Act, 2002

  *"It is proposed to amend sub-sec.(2) of the said section to clarify that the mere fact of participation of one enterprise in the management or control or capital of the other enterprise or the participation of one or more persons in the management or control or capital of both the enterprises shall not make them associated enterprise **unless** the criteria specified in sub-sec. (2) are fulfilled."*

- The expression 'participation in management, capital, control' is not defined in the Act:
  - **Sub-sec. (2) gives meaning to the expression** - the practical illustrations thereunder are exhaustive and not illustrative;
  - Sub-sec. (2) governs the operation of sub-sec. (1);

ANALYSIS (cont'd…)

2. Sub-section (1) & (2) operate <u>jointly</u> (cont'd…)

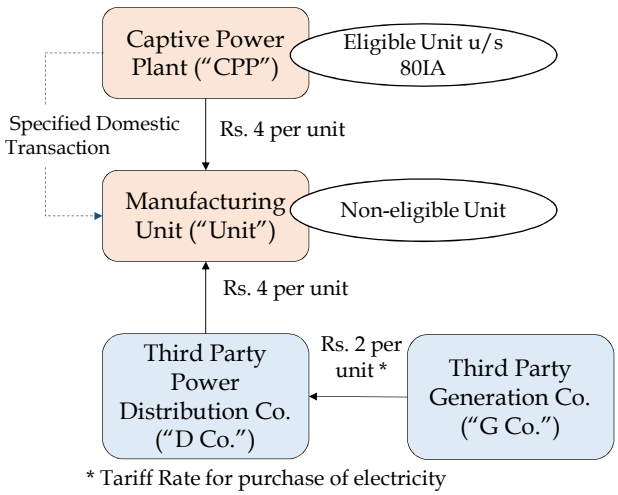
- Once the requirements of sub-sec.(2) are fulfilled, two enterprises will be treated as AEs;
  - Such interpretation would render provisions of sub-sec.(1) otiose or superfluous

- Sub-sec. (1) is fulfilled - if an enterprise has *de facto control* over the other enterprise - **BUT** if such participation is not covered under sub-sec. (2), two enterprises cannot be treated as AEs

- Case Laws:
  - Page Industries Ltd. vs. DCIT [2016] 159 ITD 680 (Bang Trib.);
  - Orchid Pharma Ltd. vs. DCIT [2017] 182 TTJ 809 (Chennai Trib.);
  - ACIT vs. Veer Gems [2017] 77 taxmann.com 127 (Ahm Trib.) upheld by Gujarat High Court in 338 of 2017

CASE STUDY 3 – INTER UNIT TRANSFER

INTER UNIT TRANSFER

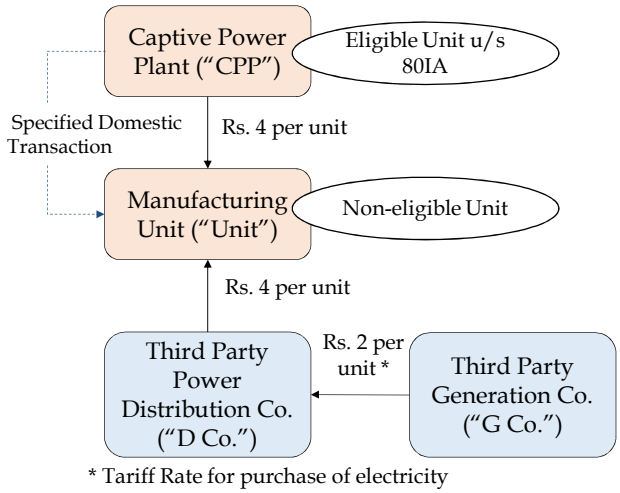


* Tariff Rate for purchase of electricity

FACTS:

- A Ltd. had set-up a CPP eligible for deduction u/s 80IA;
- Electricity generated by CPP is captively consumed in the manufacturing unit of A Ltd.;
- The Unit also purchases electricity from a Power distribution company
- Captive consumption of power is covered u/s 92BA and thus, ALP has to be determined

INTER UNIT TRANSFER (cont'd...)



FACTS:

- A Ltd. records the sale of power by CPP to its Unit at the rate at which Unit buys power from D Co.
  - Applying Internal CUP Method, the transaction is reported to be as ALP
- TPO alleges that the tariff rate at which D Co. purchases electricity from G Co. would be the ALP
  - FAR of CPP and D Co. are not comparable;
  - D Co. should be the tested party and not the manufacturing unit;
  - CPP is not engaged in distribution to earn distribution margin embedded in the rate at which D Co. sells power;

Is allegation of TPO valid?

ANALYSIS

- Comparison of Economic circumstances:
  - The nature and extent of government regulation of the market
    - Tariff is determined by Appropriate commission – Sec. 62 of the Electricity Act, 2003;
    - G Co. cannot sell power at a rate higher than tariff;
    - Captive generation company is ordinarily not governed by tariff commission;
  - Level of the market (e.g. wholesale or retail)
    - The trade levels when electricity is sold to consumer and to a distribution company are different
- Internal comparable preferred over external comparable;
- CPP is performing the twin function of **generation** and **distribution**;

ANALYSIS (cont'd…)

- 'Market Value' defined u/s 80IA(8):

  "Explanation. – For the purposes of this subsection, "market value", in relation to any goods or services, means –
  (i) the price that such goods or services would ordinarily fetch in the open market; or
  (ii) the arm's length price as defined in clause (ii) of section 92F, where the transfer of such goods or services is a specified domestic transaction referred to in section 92BA."

- 'open market price' and 'ALP' are arrived on the presumption that neither of the parties to the transaction have any control over the transaction
  - Captive consumption recorded at open market price = ALP;
  - View otherwise would lead to absurdity;

ANALYSIS (cont'd…)

- Case Laws on '*market value of inter-unit transfer is the value charged by state electricity board to the end-customers and* ***not*** *the price at which it purchases electricity from the generation company*'
  - CIT vs. Godawari Power & Ispat Ltd. (223 Taxman 234)(Chhattisgarh HC);
  - CIT vs. Kanoria Chemicals & Industries Ltd. (219 Taxman 35)(Calcutta HC);
  - West Coast Paper Mills Ltd. vs. ACIT (52 taxmann.com 268)(Mum Trib.);
  - ACIT vs. Jindal Steel & Power Ltd. (16 SOT 509)(Delhi Trib.);

- Under CUP method, 'price' is compared **not** the 'transaction'
  - Functional comparability cannot be given that high a weightage;
  - Identification of tested party and FAR would accede a higher weightage in case of margin based methods *viz.* cost plus method, transactional net marginal method, etc.

ANALYSIS (cont'd…)

- Whether the views differ if occasionally CPP has sold electricity to D Co. as well at Rs. 1.5 per unit?
- Such sale to D Co. would be **'in-firm power'** –
  - CPP would sell only excess power, which is not capitvely consumed to D Co.;
  - There would be no commitment to sell power on a regular basis;
- Terms of supply of firm commitment and in-firm commitment are obviously different – Thus, not comparable;

MARKETING INTANGIBLES

CONCEPT

ADVERTISEMENT | **MARKETING** | SALES **PROMOTION**

- In case of MNCs, brand is owned by one entity but is exploited across the group;
- Group entities incur **AMP expenses** in their jurisdiction which results into two-fold benefit:
  - Direct Benefit - Increase in sales such entities;
  - Indirect Benefit – Enhances value of the brand;

Whether AMP activities by Group entities would fall under the radar of Indian TP Regulations

CONCEPT (cont'd…)

- OECD TP Guidelines:
  - Recognizes such indirect brand building;
  - Entities performing functions of 'Development, Enhancement, Maintenance, Protection & Exploitation' of intangible ("**DEMPE**") should be **compensated**;
  - Provides framework for identifying DEMPE (Para 6.34);
- UN TP Manual:
  - Recognises marketing intangibles;
  - Such local marketing activities may result into 'unique and valuable intangible' distinct from foreign owned brand;
  - Provides for significance of D**A**EMPE and its FAR analysis
    - '**A**' stands for acquisition of intangible

OVERVIEW OF LANDMARK CASE LAWS (1/3)

L.G. Electronics India (P.) Ltd. vs. ACIT [2013] 140 ITD 41 (Delhi Trib.) (SB) – *Manufacturer*

- There exists an **implied agreement** between A and its AE for enhancing value of foreign brand;
- A **has entered into an international transaction** in relation to such brand building;
- **Bright Line Test** ("BLT") appropriate for ascertaining value of such international transaction
  - Bright line is line drawn within overall amount of AMP expenses
  - On one side of the bright line are AMP expenses incurred in normal course of business
  - Remaining amount on the other side represents expenses incurred on behalf of AE

OVERVIEW OF LANDMARK CASE LAWS (2/3)

Sony Ericsson Mobile Communications India (P.) Ltd. vs. CIT [2015] 374 ITR 118 (Delhi) - *Distributor*

- Existence of international transaction was not disputed by the A;
- In the absence of statutory provision, **BLT is not permissible**;
- It would be erroneous and fallacious to treat brand building as counterpart of advertisement expenses;
- Department has filed SLP against the Court's order which has been granted;

OVERVIEW OF LANDMARK CASE LAWS (3/3)

Maruti Suzuki India Ltd. vs. CIT [2016] 381 ITR 117 (Delhi) – *Manufacturer*

- Distinguished between 'Brand Promotion' and 'Product Promotion';
- **Existence of international transaction has to be established *de hors* BLT**;
- 'Price' of international transaction has to be adjusted
  - The very existence of an international transaction cannot be presumed by assigning some price to it and then deducing that since it is not an ALP, an 'adjustment' has to be made
- Substantive and machinery provisions fail – TP Regulations not applicable;

Hyundai Motor India Ltd. vs. DCIT [2017] 187 TTJ 97 (Chennai Trib.)

- FACTS:
  - Ā **manufactured** cars in India under the brand name 'Hyundai' legally owned by HMC Korea, its parent company;
- ACTION OF TPO:
  - Using the badge 'Hyundai' on the cars manufactured by Ā leads to accretion in value of foreign brand;
  - Ā should be compensated for such brand building, proportionate to sale of cars by the assessee company (in volume) vis-à-vis the global sale worldwide;
  - Though AMP expenses as % of Net Sales by Ā is less than its comparables, it does not mean that brand value it not created;
- DRP confirmed said addition but, directed to use 'value' of cars sold, instead of 'volume' of sale;

Hyundai Motor India Ltd. vs. DCIT [2017] 187 TTJ 97 (Chennai Trib.) (cont'd…)

- FINDINGS OF ITAT:
  - TPO's emphasis is on 'benefit' accruing to HMC Korea on account of increased brand valuation as a result of 'cars sold in India, and **not** as a result of 'conscious brand promotion' by Ā;
  - If instead of 'Hyundai', Ā used brand owned by itself, advantage of increase in brand vale as a result of sale of cars would have gone to Ā rather than AE
    - It is this arrangement, for benefit of AE, which is stated to be 'international transaction'
  - **Two aspects of his arrangement being 'International transaction'**
    1) **What is the true nature, and proximate cause of the use of foreign brand name?**
    2) **Scope of 'international transaction' u/s 92B**

Hyundai Motor India Ltd. vs. DCIT [2017] 187 TTJ 97 (Chennai Trib.) (cont'd…)

- FINDINGS OF ITAT: (cont'd...)

1) **What is the true nature and proximate cause of the use of foreign brand name?**
   - The brand 'Hyundai' has a certain degree of credibility across the globe including India;
   - Its use indeed amounts to a benefit to Ā;
   - The use of brand name owned by the foreign AE is a privilege, a marketing compulsion and of direct and substantial benefits to the Ā;
   - However, increased visibility of trade name in Indian market does contribute to increase value of brand
     - **Whether such 'incidental benefit' can be treated as international transaction**

Hyundai Motor India Ltd. vs. DCIT [2017] 187 TTJ 97 (Chennai Trib.) (cont'd…)

- FINDINGS OF ITAT: (cont'd...)

2) Scope of 'international transaction' u/s 92B

Sr. No.	Text of section 92B(1)	Analysis by ITAT
"international transaction" means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of		
(i)	purchase, sale or lease of tangible or intangible property,	▪ Brand name is an intangible ▪ Transaction under consideration is 'increase in value of intangible' as a by-product of business model employed by A ▪ Increase in value is not on account of sale, purchase, lease of intangible ▪ Not covered under clause (ii) of Explanation to Sec. 92B providing clarity on 'intangible property'

Hyundai Motor India Ltd. vs. DCIT [2017] 187 TTJ 97 (Chennai Trib.) (cont'd…)

2) Scope of 'international transaction' u/s 92B (cont'd...)

Sr. No.	Text of section 92B(1)	Analysis by ITAT
(ii)	Provision of service	▪ Accretion in value of brand due to use in A's product cannot be treated as 'service' ▪ ''Privilege' to A cannot be a service by A ▪ Service has to be conscious activity and not a subliminal exercise ▪ For determining ALP, rendition of service should result into benefit, an independent enterprise would pay for • Since no service is performed, discussion on benefit academic
(iii)	lending or borrowing money,	▪ There is no dealing in money and thus, this limb of definition is irrelevant

Hyundai Motor India Ltd. vs. DCIT [2017] 187 TTJ 97 (Chennai Trib.) (cont'd…)

2) Scope of 'international transaction' u/s 92B (cont'd...)

Sr. No.	Text of section 92B(1)	Analysis by ITAT
(iv)	any other transaction having a bearing on the profits, income, losses or assets of such enterprises	▪ Accretion value of AE's brand name is not on account of costs incurred by the A, or even by its conscious efforts ▪ It does not result in profits, income, expenditure, losses or assets of the A ▪ It cannot, thus, result in an international transaction qua the taxpayer ▪ Unless the transaction is such that it affects profits, losses, income or assets of both the enterprises, it cannot be an international transaction between these two enterprises.

Hyundai Motor India Ltd. vs. DCIT [2017] 187 TTJ 97 (Chennai Trib.) (cont'd…)

2) Scope of 'international transaction' u/s 92B (cont'd...)

Sr. No.	Text of section 92B(1)	Analysis by ITAT
(v)	and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises.	▪ Alleged brand building is not a case of allocation of, apportionment of, or contribution to, any costs or expenses in connection with a benefit, service or facility

- Accretion of brand value, as a result of use of the brand name of foreign AE under the technology use agreement-which has been accepted to be an arrangement at ALP, does not result in a separate international transaction to be benchmarked

HARD TO VALUE INTANGIBLES ("HTVI") & INTELLECTUAL PROPERTY RIGHTS

CONCEPT

- HTVI covers intangibles or rights in intangibles for which, at the time of transfer:
  - No reliable comparables exist;
  - Difficult to predict the level of ultimate success of the intangible;
- Features of HTVI
  - Partially developed at the time of transfer;
  - Not expected to be exploited commercially for several years;
  - Intangible itself is not HTVI, but integral to the development or enhancement on another HTVI;
  - The intangible is either used in connection with or developed under a Cost Contribution Arrangements or similar arrangements, etc.

DQ (International) Ltd. vs. ACIT [2016] 72 taxmann.com 142 (Hyd Trib.)

- FACTS:
  - Ā was a producer of animation visual effects, game art and entertainment content for the global media and entertainment industry;
  - Ā sold the IP Rights of one of its animation series to DQ Ireland **at the development stage**
  - Consideration as determined by taking average of the valuation determined by two independent valuers;
  - Valuation under DCF method and any other method was based on projections of revenue considering detailed market expectation on the date of sale;

DQ (International) Ltd. vs. ACIT [2016] 72 taxmann.com 142 (Hyd Trib.)(cont'd…)

- ACTION OF TPO:
  - TPO stated that projected cash flows are not credible as they were provided by Ā only;
  - There may be substantial differences between the forecasted figures and the actuals;
  - TPO replaced the projected figures with the actual revenue figures of DQ Ireland and determined the ALP;
  - Even though legal ownership of IPR was transferred to DQ Ireland, the economic ownership lay with Ā;
  - TPO applied PSM in ratio of 80:20 between Ā and DQ Ireland;

DQ (International) Ltd. vs. ACIT [2016] 72 taxmann.com 142 (Hyd Trib.) (cont'd…)

- FINDINGS OF ITAT:
  - The valuation method based on projections **cannot** be **replaced with actuals** down the line;
  - Actual figure vary from projections, but what is important is value available at the time of making business decision;
  - For valuation of intangibles, only future projections alone can be adopted;
  - Valuation cannot be reviewed with actuals after 3/4 years;
  - Revision of value of intangibles subsequently amounts to ***evaluation*** and ***not valuation;***

DQ (International) Ltd. vs. ACIT [2016] 72 taxmann.com 142 (Hyd Trib.) (cont'd…)

- FINDINGS OF ITAT:(cont'd…)
  - When the TPO agreed that there was an outright sale - the international transaction ended there itself;
  - Now, TPO was trying to go beyond sales and making TP adjustments;
  - Once, the IP is sold and ALP is determined, the 'IPR' becomes the property of 'AE';
  - Ā has no *locus standi* to claim any benefit neither the revenue;

OECD TP GUIDELINES

- Para 6.813:

> *"……..For a **transfer of intangibles** or rights in intangibles at a stage when they are **not ready** to be commercialized but **require further development**, **payment terms** adopted by independent parties on initial transfer might include the determination of **additional contingent amount**s that would become payable only on the achievement of specified milestone stages in their further development."*

OECD TP GUIDELINES (cont'd…)

- Para 6.912:
  - The tax administration can consider ***ex post* outcomes** as **presumptive evidence** about the appropriateness of the ***ex ante* pricing arrangements**;
  - Where the tax administration is able to **confirm** the **reliability** of the information on which *ex ante* pricing has been based, notwithstanding the approach described in this section, then **adjustments based on *ex post* profit levels should not be made**;
  - In **evaluating** the *ex ante* pricing arrangements, the tax administration is entitled to use the *ex post* evidence about financial outcomes to inform the determination of the arm's length pricing arrangements, including any contingent pricing arrangements, that would have been made between independent enterprises at the time of the transaction;

Sun Pharmaceutical Industries Limited vs. ACIT [2017] 84 taxmann.com 217 (Ahmd Trib.)

- FACTS:
  - Ā, parent company of the Sun Pharma Group, was a pharmaceutical company engaged in manufacturing and sale of generic drugs;
  - The manufacturing activities were carried out at its factories located in India;
  - SPARC was the demerged R&D unit of SPIL;
  - All the IPRs held by SPARC were transferred to SPG, a foreign entity which was WOS of the Ā;
  - Consequent to the above transaction, SPG entered into an agreement with the Ā for contract manufacturing of generic drugs as per the technology of SPG;
  - The margin from contract manufacturing services provided by Ā to its AE were benchmarked under TNMM;
  - Further, SPG was the owner of all IPRs and also liable to pay infringement penalty for the two legal suits filed against it for violation of US patent rights;

Sun Pharmaceutical Industries Limited vs. ACIT [2017] 84 taxmann.com 217 (Ahmd Trib.)(cont'd…)

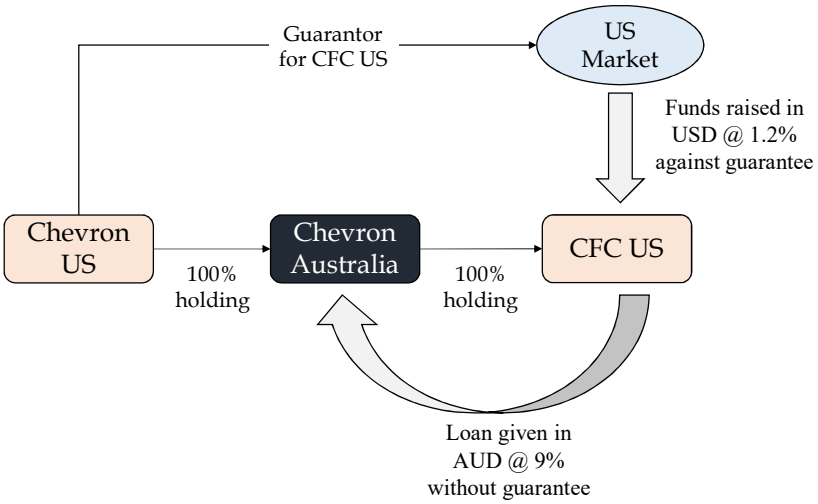
- ACTION OF TPO:
  - TPO stated that Ā
    - performed substantial manufacturing functions;
    - assumed the associated risks; and
    - owned the IPRs;
  - TPO applied the PSM as MAM and made a TP adjustment taking the split up ratio as 50:50 between Ā and SPG (without taking into consideration the infringement loss borne by SPG);
- CIT(A) upheld the application of PSM **but** enhanced the split up ratio to 80:20
  - Ā was not a contract manufacturer but an entrepreneurial manufacturer

Sun Pharmaceutical Industries Limited vs. ACIT [2017] 84 taxmann.com 217 (Ahmd Trib.)(cont'd…)

- FINDINGS OF ITAT –
  - **Key Value Drivers** for determining whether Ā is a contract manufacturer or not include -
    - Entity performs substantial functions;
    - Entity owns significant assets (IPRs, R&D facility, etc.);
    - Entity assumed key risks and had the capacity to assume such risks (Risk of loss, litigation, infringement risks);
  - ITAT noted that Ā performs just one function – manufacturing;
  - Ā does not own the IPRs/R&D technology and does not assume the risk attached to such assets – since, the infringement loss was borne by SPG;
  - Considering the business arrangement Ā was held to be contract manufacturer
    - ITAT held that TNMM as MAM instead of PSM

CREDIT FACILITY ARRANGEMENT - AUSTRALIAN DECISION

Chevron Australia Holdings Pty Ltd. v. Commissioner of Taxation [2017] FCAFC 62



Taxation of transaction flows for CFC

Difference between interest received @ 9% and interest paid @ 1.2%

Not taxable in US as CFC is 'check the box entity'

Taxation of transaction flows for Chevron Australia

Withholding tax provisions not applicable on interest paid to CFC and interest claimed as deduction

Dividend from CFC exempt from tax

ANALYSIS (cont'd…)

- Revenue's Arguments:
  - The terms and contract of credit facility arrangement between CFC and Chevron Australia was such that no independent entity would have entered into the same type of loan agreement;
  - There is lack of operation/financial covenants;
  - There is lack of parental guarantee in the entire agreement;
  - Interest paid to CFC is not at ALP as on an independent analysis, the interest paid would have substantially lower otherwise;
- Decision of Full Federal Court of Australia (FCA):
  - The FCA addressed three key aspects –

1. Property | 2. Consideration | 3. Arms Length Consideration

ANALYSIS (cont'd…)

❑ Decision of Full Federal Court of Australia (FCA): (cont'd…)

1. Property

- Includes '**services**'
- services includes any **rights, benefits, privileges** or facilities under and agreement

- Funds advanced by way of loan is the 'property'
- the **absence of security, guarantee** or other charge is **factored in the consideration**

2. Consideration

Relevant with respect to
- **Consideration actually given**/agreed by Chevron Australia in respect of loan
- **Identifying arm's length consideration**

- FCA clearly **distinguishes** 'consideration' and 'arm's length consideration'
- Former is used to inform conclusions regarding latter
- The term is broad enough to encompass consideration given by borrower
  - to lender, or
  - to third party – to the parent company upon the hypothesis of the payment of a fee

ANALYSIS (cont'd…)

❑ Decision of Full Federal Court of Australia (FCA): (cont'd…)

3. Arm's Length Consideration (ALC)

Two critical criteria for determining ALC:
1. **Standard of reasonable expectation**
2. **Hypothetical independent party construct**

- Involves evaluative prediction of events and transactions that did not take place;
- Such evaluation must be based upon evidence including admissible, probative and reliable expert opinion;
- **The hypothetical (arm's length) agreement should remain close to the actual agreement**

- **Comparability factors** to be considered:
  - **Operational and financial covenants** - an independent borrower like Chevron Australia dealing at arm's length would have given security and such covenants to acquire the loan;
  - **Parental affiliation;**

ANALYSIS (cont'd…)

- Decision of Full Federal Court of Australia (FCA): (cont'd…)
  - **Guarantee Fee:**
    - FCA stated that in determining ALC, amounts which could be shown on the evidence as **reasonably likely** to have been given by independent parties in comparable dealings could be taken into account, **irrespective** of whether such consideration was actually given by the taxpayer;
    - Example given in the decision - **A guarantee would have been given by Chevron US to enable Chevron Australia to borrow at a cheaper rate;**
    - However, no evidence was found to determine ALC for the hypothetical loan;

The decision does not provide guidance as to how the monetary value of the guarantee fee might be determined

RELEVANCE - INDIAN CONTEXT

- **Arm's Length Price** under Indian TP Regulations vis-à-vis **Arm's Length Consideration** under the Australian TP Regulations
  - ALP emphasises on FAR, terms and condition, product and service characteristic, market condition etc.;
  - ALC provides liberty to consider hypothetical transactions;
- **ALP** is a **narrower concept** as compared to **ALC;**
- It would be difficult to search comparables for similar credit facility arrangement in the Indian TP Regulation;

RELEVANCE - INDIAN CONTEXT (cont'd…)

- India's comments in the UN TP Manual –

"D.3.12.3. A further issue in financial transactions is credit guarantee fees……In most cases, interest rate quotes and guarantee rate quotes available from banking companies are taken as the benchmark rate to arrive at the ALP….

D.3.12.4. ***However, the Indian transfer pricing administration is facing a challenge due to the non-availability of specialized databases*** *and of comparable transfer prices for cases of complex inter-company loans and mergers and acquisitions that involve complex inter-company loan instruments as well as* ***an implicit element of guarantee*** *from the parent company in securing debt."*

CASE LAWS – SHARE APPLICATION MONEY

Bharti Airtel Ltd. vs. ACIT [2014] 63 SOT 113 (Delhi Trib.)

- FACTS:
  - A made payment towards share application money in its foreign subsidiary;
  - Time taken for actual allotment of shares was about 13 to 16 months;
- ACTION OF TPO:
  - TPO did not question the character of the payment – but contended that an independent entity would not leave the amount in the hands of another entity without the same being converted into equity within a reasonable period or receiving interest on the same;
  - Thus, TPO treated this as interest free loan to the subsidiary and determined addition towards notional interest
- DRP upheld the addition

Bharti Airtel Ltd. vs. ACIT [2014] 63 SOT 113 (Delhi Trib.) (cont'd...)

- FINDINGS OF ITAT:
  - The **core issue** is whether 're-characterisation of share application money into loan/advance' (i.e. **a deeming fiction**) **is envisaged under the scheme of TP Regulations** - The answer is **NO;**
  - There was no finding on record about **what should be a reasonable period for allotment of shares**;
  - Assuming that there was inordinate delay, capital contribution could have, at best, be treated as interest free loan for such period of inordinate delay not the entire period till actual allotment of shares;

Bharti Airtel Ltd. vs. ACIT [2014] 63 SOT 113 (Delhi Trib.) (cont'd...)

- FINDINGS OF ITAT: (cont'd...)
  - Even if ALP has to be determined for such interest-free loan using CUP Method –
    - **It was to be done on the basis as to what would have been interest payable to an unrelated share applicant if, despite having made the payment of share application money, the applicant is not allotted the shares;**
    - This situation is not in *pari materia* with an interest free loan on commercial basis between the share applicant and the company to which capital contribution is being made;
  - Since, the TPO had not brought on record any comparable instance in case of unrelated share applicant, the TP adjustment was not sustainable;

Bharti Airtel Ltd. vs. ACIT [2014] 63 SOT 113 (Delhi Trib.) (cont'd...)

- FINDINGS OF ITAT: (cont'd...)
  - In any event, **it is not open to the revenue authorities to re-characterize the transaction unless it is found to be a sham or bogus transaction**;
  - Even under the **judge made law**, such re-characterization is possible only when the transactions are found to be substantially at variance with the stated form;
  - In the absence of any such finding, ITAT deleted TP addition for notional interest;

Sun Pharmaceutical Industries Ltd. vs. ACIT [2017] 84 taxmann.com 217 (Ahm Trib.)

- FACTS:
  - Ā made additional subscription to equity shares of WOS which were pending allotment;
  - Share appplication money was shown unde the head 'Advances' in the Balance Sheet;
  - Ā contended that shares were not alloted as the in order to meet procedural requirements;
  - TPO/CIT(A) re-characterised the transaction as loan/advance to AE;
  - DR contended that the Indian Companies Act provides for charging of interest if the company is unable to allot shares within a period of 60 days from the receipt of application money if such amount is not to repaid within 15 days from the end of the period of 60 days;

Sun Pharmaceutical Industries Ltd. vs. ACIT [2017] 84 taxmann.com 217 (Ahm Trib.) (cont'd...)

- FINDINGS OF ITAT:
  - Re-characterisation as loan/advance not warranted on account of delay in allotment of shares and classification of share application money under the head Advance;
  - **Percentage of ownership is the only material factor which remains 100% prior and post allotment;**
  - Allotment of shares in academic, as Ā is a single shareholder in its WOS – Face value of shares does not affect actual benefit to the Ā;
  - **Provisions of Indian Companies Act not to be considered as different countries have separate laws/regulation on such issue;**
  - Case Referred - *ITO v. Sterling Oil Resources (P.) Ltd. [2016] 67 taxmann.com 2 (Mum Trib);*

Logix Microsystems Ltd. vs. DCIT [2017] 80 taxmann.com 39 (Bangalore Trib.)

- FACTS:
  - Ā made additional subscription to equity shares of US Subsidiary;
  - As on 31.3.2009 shares were pending allotment;
  - TPO held that such funds were in the nature of 'debt' and thus, covered under 'International Transaction' u/s 92B;
  - DRP upheld TPO's contention;
- FINDINGS OF ITAT:
  - It is undisputed that if shares are alloted within reasonable time – Share application money cannot be considered as loan or advance;
  - Alloting company cannot have a right to use the share application money until allotment of share;

Logix Microsystems Ltd. vs. DCIT [2017] 80 taxmann.com 39 (Bangalore Trib.) (cont'd...)

- FINDINGS OF ITAT: (cont'd...)
  - If this money was available with the AE for utilization and there was an extraordinary delay in allotment of shares – it loses the character of share application money;
  - Case Laws relied upon by Ā would not be applicable in such scenario
    - Vijai Electricals Ltd. v. Addl. CIT [2013] 36 taxmann.com 386/60 SOT 77 (URO) (Hyd Trib.)
    - Pan India Network Infravest (P.) Ltd. [ITA Nos. 7025 & 7026/Mum/2013]
    - Bharti Airtel Ltd. v. Addl. CIT *(supra)*

Logix Microsystems Ltd. vs. DCIT [2017] 80 taxmann.com 39 (Bangalore Trib.) (cont'd...)

- FINDINGS OF ITAT: (cont'd...)
  - In the present case, such money was available with AE for utilization and no shares were allotted till the end of the financial year –
    - the transaction would constitute an international transaction u/s 92B;
    - have a direct bearing on the profit and loss and assets of the enterprise;
  - As per the Explanation to Sec. 92B, till the date of allotment it will constitute as capital financing /advance to AE;
  - Apply LIBOR rate for determining ALP of interest as the remittance was made in foreign currency;

POINTS TO PONDER

- What would be 'reasonable' time limit for allotment of shares?
- Whether re-characterisation of equity into debt is permissible only under Chapter X-A of the Act on GAAR
- If the transaction is not treated as Impermissible Avoidance Arrangement under GAAR:
  - Does Chapter X permit re-characterisation share application money into interest-free loan in case of genuine transactions?
- Can interest charged on commercial loans be considered as ALP for such transactions?

LOCATION SAVINGS

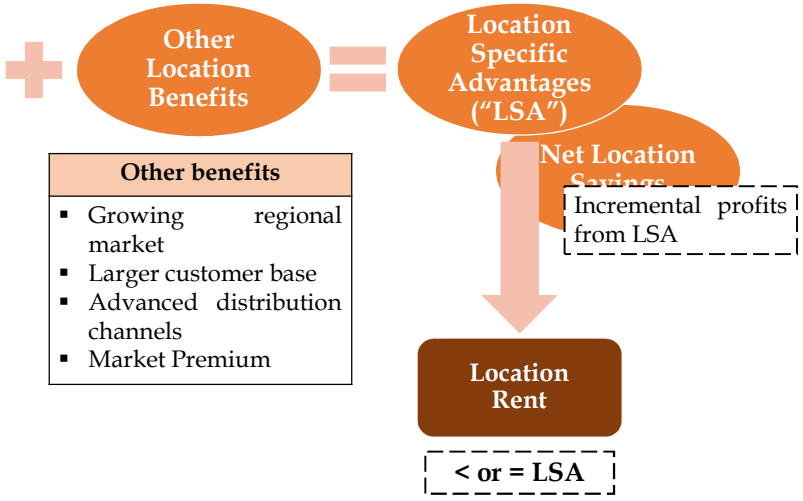
CONCEPT

- Location Saving are the **net cost savings** than an MNE realises as a result of **relocation of operations** from a **high cost jurisdiction** to a **low cost jurisdiction**

Cost Savings
▪ Labour Cost ▪ Raw material Cost ▪ Infrastructure Costs ▪ Training Costs ▪ Rental Expenditure ▪ Tax Exemptions

Dis - savings
▪ Relocation expenses ▪ Compensation to employees on discontinuance of facility ▪ High transportation cost

CONCEPT (cont'd…)



STEP APPRAOCH

Step 1	Identification of LSAs
Step 2	Whether the LSAs convert into Location rent (enable the enterprise to generate super profits)
Step 3	Quantifying the Location Rent
Step 4	Determine the treatment of Location Rent – Whether benefit passed to customer or retained within the Group
Step 5	If Location Rent is retained within the Group – Attribution as per TP Regulations

ALLOCATION OF LOCATION SAVINGS

- OECD TP Guidelines – Article 9.149

  "Where significant location savings are derived further to a business restructuring, the question arises of whether, and if so how, the location savings should be shared among the parties. The response should obviously depend on what independent parties would have agreed in similar circumstances. The conditions that would be agreed between independent parties would normally depend on the functions, assets and risks of each party and on their respective bargaining powers."

- Factors for determination of bargaining power –
  - Market Competition;
  - Ownership of intellectual property;
  - Cost switching techniques;
  - Commercial experience;

Syngenta India Ltd. vs. DCIT [2017] 187 TTJ 271 (Mumbai Trib.)

- FACTS:
  - One unit of Ā is captive manufactures of chemicals for sale in world local market by its AE in Singapore;
  - Due to unique location Ā is able to generate cost saving;
  - TPO contends that Ā ought to be compensated for such cost saving and made an adjustment thereto;
  - DRP confirmed said adjustment;

Syngenta India Ltd. vs. DCIT [2017] 187 TTJ 271 (Mumbai Trib.) (cont'd…)

- FINDINGS OF ITAT:
  - 'Location saving' **not recognised** as a separate international transaction under the Indian TP provisions which warrants separate benchmarking
    - Especially when overall profit margin for transaction with AE has been benchmarked using TNMM
  - **Key factor** is finding **suitable and reliable local market comparables**
    - If reliable data is available – no adjustment required as LSA is embedded/captured in the profits of the comparables and the ALP so determined;
    - BEPS – Action Plan 8 also provides for no adjustment;

Syngenta India Ltd. vs. DCIT [2017] 187 TTJ 271 (Mumbai Trib.) (cont'd…)

- FINDINGS OF ITAT: (cont'd…)
  - Location saving elaborately explained based on OECD TP Guidelines and OECD/G20 BEPS Action Plan – 8;
  - In a perfectly competitive market, a manufacturer will have to pass on any LSA to the customers to remain competitive in the market;
  - TPO could not make adjustment to Ā's ALP on account of 'location saving' without carrying out comparability analysis with uncontrolled transaction to show that location factor materially affected price/profit margin of transaction in question;

PASS THROUGH COST ("PTC")

CONCEPT

- PTC are **non-value adding cost** which are incidental or ancillary to the primary business activity of a taxpayer for which –
  - It **does not** perform any significant functions; and
  - It **does not** assume any risks;
- PTC are reimbursed without charging any mark-up
- Profit Level Indicator – $\frac{\text{Operating Cost}}{\textbf{VAE}}$
- Value Added Expenses ("VAE") = Total Costs – PTC
- The expression " any other relevant base" mentioned in Rule 10B(1)(e)(i), allows a denominator that excludes pass through costs;

OCED GUIDELINES

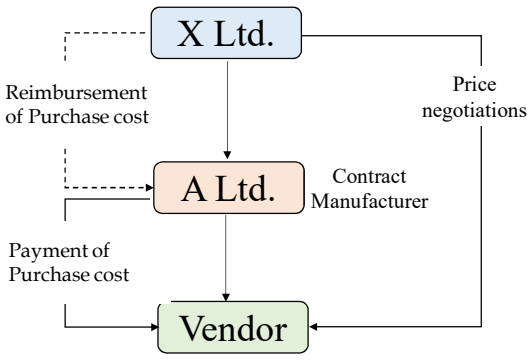
- Para 2.99 –

  "In applying a cost-based transactional net margin method, fully loaded costs are often used, including all the direct and indirect costs attributable …... The question can arise whether and to what extent it is acceptable at arm's length to treat a significant portion of the taxpayer's costs as ***pass-through costs to which no profit element is attributed (i.e. as costs which are potentially excludable from the denominator of the net profit indicator).*** *This depends on the extent to which an independent party in comparable circumstances would agree not to earn a mark-up on part of the costs it incurs."*

- Para 2.100 –

  "…a second question arises as to the consequences on comparability and on the determination of the arm's length range. Because it is necessary to ***compare like with like****, if pass-through costs are excluded from the denominator of the taxpayer's net profit indicator, comparable costs should also be excluded from the denominator of the comparable net profit indicator."*

ILLUSTRATION



Facts:

- X Ltd. has entered into a contract with A Ltd. for job work processing;
- A Ltd. is AE of X Ltd.;
- For procurement of raw materials, X Ltd. identifies the vendors and negotiates prices;
- A Ltd. is required to purchase the materials from such vendors at the negotiated price, which is later reimbursed by X Ltd. (without mark-up);
- A Ltd. charges a mark-up of 10% on other VAE to X Ltd.;

Analysis:

- No profit relating to raw materials is charged by A Ltd.;
- Procurement related functions/risk are performed/borne by X Ltd.;

Raw material cost = Pass through cost

CASE LAWS

- Adjustment of pass through cost **allowed**

Case Laws	Findings
Johnson Matthey India (P.) Ltd. v. DCIT [2015] (380 ITR 43) (Delhi HC)	Raw material is procured by the taxpayer **under the instructions** and **at the price decided by the customer**. The cost of raw material was reimbursed separately, over and above a fixed manufacturing charge
Akon Electronics India (P.) Ltd. v. DCIT [2017] (79 taxmann.com 232) (Delhi Trib.)	The A purchased kits as raw material from its AE and sold it back to AE after assembling and partial testing

CASE LAWS (cont'd…)

- Adjustment of pass through cost **not allowed**

Case Laws	Findings
DCIT vs. Tours & Travels India (P.) Ltd. [2016] 180 TTJ 65 (Delhi - Trib.) upheld in (ITA No. 380 of 2016) (Delhi HC)	Where **expenditure** was **incurred** by Ā – tour operator **in its role of a principal** and **not as an agent of its foreign AE**, for arranging tours, inasmuch as said amount was not recoverable per se from its AE, said sum could not at all be construed as 'PTC'
Fujitsu India Ltd. vs. DCIT [2017] 78 taxmann.com 279 (Delhi - Trib.)	PTC **pre-supposes** its **specific and identifiable recovery** as such from its AE **without any profit element**; if there is no separate reimbursement of such a cost and it is part of overall contracted value, then presumption will be that overall profit element is entrenched in all costs incurred by Ā, thereby taking it outside ambit of PTC

FOREIGN AE AS A TESTED PARTY

CONCEPT

OECD Guidelines

Para 3.18 -
"the one to which a transfer pricing method can be applied in the most reliable manner and for which the most reliable comparable can be found, i.e. it will most often be the one that has the ***less complex functional analysis****."*

UN Model

Para B.2.3.3 -
"The tested party normally should be the ***less complex*** *party to the controlled transaction and should be the party in respect of which the* ***most reliable data for comparability is available****.* ***It may be the local or the foreign party****…"*

Importance of 'Tested Party'

- On of the basic step of robust transfer pricing analysis
- Selection of Tested Party is important for transactional profit methods *viz.* PSM, TNMM
- The term 'Tested party' has not been defined in the Act;

DIVERGENT VIEWS - *FAVOURABLE*

- Case Laws:
  - General Motors India Pvt. Ltd [2013] (37 taxmann.com 403) (Ahm Trib)
  - Ranbaxy Laboratories Ltd. v. ACIT [2016] (68 taxmann.com 322) (Delhi Trib.)
  - GE Money Financial Services (P.) Ltd. v. ACIT [2016] (69 taxmann.com 420) (Delhi Trib.)
  - IDS Infotech Ltd v. DCIT [2017] (80 taxmann.com 88) (Chd Trib.)
- Basis for favourable judgement:
  - If the foreign AE meets the following criteria, it can be selected as a tested party –
    - Least complex (amongst the parties to the transaction);
    - Availability of reliable and accurate data for comparison;
    - Data available can be used with minimal adjustments;
  - Views are in concurrence with OECD TP Guidelines and UN TP Manual

DIVERGENT VIEWS - *AGAINST*

- Case Laws:
  - M/s. Onward Technologies Limited [2013] 155 TTJ 439 (Mum.)
  - AT & S India (P.) Ltd. v. DCIT [2016] 72 taxmann.com 324 (Kol Trib.)
  - GE Money Financial Services (P.) Ltd. v. DCIT (ITA 440 of 2014) (Delhi Trib.)
- Basis for against judgement:
  - The term "enterprise" as interpreted in transactional profit methods under Rule 10B of the IT Rules is restricted only to Indian entities;
  - The treatment of a Foreign AE as a tested party lacks legal sanction under Indian Tax Laws– it is *sans merit*

CONCLUDING THOUGHTS

- Section 92F(iii) – Definition of "enterprise"

  *"…... A **person** (including a permanent establishment of such person) who is, or has been, or is proposed to be, engaged in any activity, …"*

- Section 2(31) – Definition of "person" includes a **company**

- Section 2(17) – Definition of "company"

  "(i) any Indian company, or

  *(ii) Any **body corporate incorporated by or under the laws of a country outside India**; or…"*

Enterprise includes a foreign company

WORKING CAPITAL ADJUSTMENT ("WCA")

CONCEPT

- WCA is an attempt to adjust for difference in **time value of money** between tested party and potential comparables with an assumption that the difference should be reflected in profits;

- Example on **Outstanding Receivables**:

  A Co. provides 60 days trade terms for payment of accounts

  - Sale Price = Actual Price (on immediate payment) + 60 days interest thereon;
  - By carrying high accounts receivable a company is allowing its customers a relatively long period to pay their accounts;
  - Borrow money to fund the credit terms and/or suffer a reduction cash surplus which could have been invested;
  - In a competitive environment, the price should therefore include an element to reflect these payment terms and compensate for the timing effect;

PRACTICAL ILLUSTRATION - OECD TP GUIDELINES

WCA	Year 1	Year 2	Year 3	Year 4	Year 5
Tested Co. (WC/Sales)	25.6%	25.8%	24.1%	26.7%	29.3%
Comparable Co. (WC/Sales)	19.9%	20.6%	28.7%	24.5%	24.6%
Difference (D)	5.7%	5.1%	-4.7%	2.1%	4.7%
Interest Rate (i)	4.8%	5.4%	5.0%	5.5%	4.5%
Adjustment (D*i)	0.27%	0.28%	-0.23%	0.12%	0.21%
Comparable Co. (EBIT/Sales) (%)	1.32%	2.96%	2.59%	3.31%	4.95%
Margin (Post WCA)	**1.59%**	**3.24%**	**2.35%**	**3.43%**	**5.16%**

PRACTICAL ILLUSTRATION - OECD TP GUIDELINES (cont'd…)

- Issues involved:
  - What point in time are the Receivables, Inventory and Payables compared between the tested party and the comparables?
    - WC as on the last day may not reflect the level of WC over the year
    - Average of opening and closing WC - better option
  - Selection of appropriate rate for WCA:
    - In most cases a commercial loan rate will be appropriate.
    - Negative WC – a different rate may be appropriate
  - Whether WCA should be made when the results of some comparables can be reliably adjusted while the results of some others cannot;

PCIT vs. Kusum Health Care Pvt. Ltd. (ITA 765/2016) (Delhi High Court)

- FACTS:
  - Ā is engaged in business of exporting pharmaceuticals to AE and third parties;
  - Ā benchmarked the international transaction of export to AE using TNMM;
- ACTION OF TPO:
  - Credit period for unrelated debtors was 180 days whereas AEs were allowed a longer period;
  - Receivable qua the AE was treated as a separate international transaction;

PCIT vs. Kusum Health Care Pvt. Ltd. (ITA 765/2016) (Delhi High Court) (cont'd…)

- FINDINGS OF ITAT:
  - Ā had undertaken WCA for the comparable companies;
  - Differential impact of WCA of the Ā vis-à-vis its comparables had already been factored in the pricing/profitability;
  - Any further adjustment on the pretext of outstanding receivables not warranted;

- FINDINGS OF HC:
  - Since, WCA was already factored in the Ā's price vis-à-vis comparables, further adjustment would have distorted the picture a re-characterised the transaction;
  - This was clearly impermissible in law;
  - Upheld ITAT's view;

INTRA – GROUP SERVICES

CONCEPT

- MNEs arrange for wide scope of services (technical, financial and commercial) to be made available to its group companies;
- Such services are pooled under a 'group service centre';
- A member in need of service may approach the service centre (intra-group);
- Cost of such services is initially borne by the group centre and thereafter allocated to the group companies with or without mark-up;
- **Two main issue** from TP perspective:
  - Whether intra-group services have in fact been provided
  - Whether the intra-group cost is at ALP

M/s. Akzo Nobel India Limited vs. DCIT (ITA No. 335/Kol/2014)(Kol Trib.)

- FACTS:
  - Ā is engaged in the business of manufacturing and marketing of paints, speciality chemicals and starch;
  - Ā had entered into a Service agreement with AE wherein AE agreed to various advisory and ancilliary support services to Ā;
  - The consideration payable for such service was determined based on cost plus a margin of 5%;
  - Ā claimed that these services were rendered by ANPAP to several Akzo Group companies;
  - TPO proceed on the basis that the service rendered by AE were in the nature of stewardship activity and thus, no charges ought to be paid
    - ALP or such service was determined at NIL

M/s. Akzo Nobel India Limited vs. DCIT (ITA No. 335/Kol/2014)(Kol Trib.) (cont'd…)

- FINDINDS OF ITAT:
  - Since **services rendered** are generally **intangible**, it is **difficult to identify** services **actually received** / rendered, and then to **prove the benefits** received by the entity paying
  - **Commercial expediency** is **not be questioned** by the tax authorities
    - EKL Appliances Limited [TS-206-HC-2012(DEL)-TP]
  - ITAT identified **6 aspects** that would require consideration in order to **identify intragroup services** requiring arm's length remuneration:
    - Whether services were received from related party
    - Nature of services including quantum of services received by the related party.
    - Services were provided in order to meet specific need of recipient of the services.
    - The economic and commercial benefits derived by the recipient of intragroup services.
    - In comparable circumstances an independent enterprise would be willing to pay the price for such services?
    - An independent third party would be willing and able to provide such services?

M/s. Akzo Nobel India Limited vs. DCIT (ITA No. 335/Kol/2014)(Kol Trib.) (cont'd…)

- FINDINDS OF ITAT: (cont'd…)
  - ITAT referred to the definition of intra-group service in the OECD TP Guidelines and US Regulations
    - First, there should be an activity performed by one of the Group members which lies within the ambit of definition of activity (the 'activity test');
    - Second, that activity should result in a benefit (the 'benefit test') to one or more members of that group of related entities;
    - ITAT concluded at service rendered by AE met both the test and rejected classification under stewardship services;
  - ITAT held that Ā has established the nature of services including quantum of services received from AE as well as the economic and commercial benefits derived by it from intra group services
    - TP addition was deleted

MISCELLANEOUS

CORPORATE GUARANTEE – RECENT UPDATES

- Not an 'international transaction' (pre-2012 amendment):
  - Suzlon Energy Ltd. vs. ACIT [2017] 81 taxmann.com 190 (Ahm Trib.);
  - Cadila Healthcare Ltd. ACIT [2017] 186 TTJ 421 (Ahm Trib.);
  - Dr. Reddy's Laboratories Ltd. vs. ACIT [2017] 81 taxmann.com 398 (Hyd Trib.);
  - EIH Ltd vs. CIT [TS-609-ITAT-2017(Kol)-TP]

CORPORATE GUARANTEE – RECENT UPDATES (cont'd…)

- Corporate Guarantee commission acceptable as ALP:

Percentage	Case Laws
1%	▪ Aegis Ltd. vs. DCIT [2017] 78 taxmann.com 275 (Mum.)
0.5%	▪ Videocon Industries Ltd. vs. DCIT [2017] 186 TTJ 353 (Mum.) ▪ Xchanging Solutions Ltd. vs. DCIT [2017] 185 TTJ 385 (Bang Trib.) ▪ Laqshya Media (P.) Ltd. vs. DCIT [2017] 80 taxmann.com 309 (Mum.) ▪ Zee Entertainment Enterprises Ltd. vs. ACIT [2017] 81 taxmann.com 379 (Mum.) ▪ Endurance (India) (P.) Ltd. vs. ACIT [2017] 79 taxmann.com 181 (Pune Trib.) ▪ Piramal Glass Ltd. vs. DCIT [2017] 80 taxmann.com 68 (Mum.) ▪ Mahindra Intertrade Ltd vs. DCIT [TS-607-ITAT-2017(Mum)-TP]
0.25% – 0.27%	▪ CIT vs. Glenmark Pharmaceuticals Ltd [TS-61-HC-2017(BOM)-TP] ▪ Aster (P.) Ltd. vs. DCIT [2017] 81 taxmann.com 297 (Hyd Trib.) ▪ DCIT vs. Lanco Infratech Ltd [2017] 81 taxmann.com 381 (Hyd Trib.)

QUOTATION

Gulf Energy Maritime Services (P.) Ltd. vs. ITO [2016] 178 TTJ 683 (Mumbai Trib.)

- FACTS:
  - A rendered ship management service to its AE;
  - Transaction was benchmarked using CUP Method using quotations from third party;
  - TPO doubted the credibility of the quotations and made additions;
  - CIT(A) confirmed the said order;
- FINDINDS OF ITAT:
  - CUP Method emphasis on actual transaction - 'price charged'
    - Quotation cannot be considered
  - Rule 10AB allows hypothetical price – 'price which would have been charged'
    - ***Bonafide* quotations** - valid input for ascertaining ALP

QUASI CAPITAL TRANSACTION

Cadila Healthcare Ltd. vs. ACIT [2017] 186 TTJ 421 (Ahm Trib.)

- FACTS:
  - Ā had advanced an optionally convertible loan to its AE;
  - TPO contended that mere fact that the loan was convertible into equity did not alter its character as loan and computed notional interest;

- FINDINGS OF ITAT:
  - Real consideration for granting loan was not interest simplicitor but an opportunity to own capital on favourable terms;
  - It was to be regarded as quasi capital transaction;
  - Such advance not be compared with simple loan transaction for purpose of determining ALP;

THANK YOU!!!