IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCHES "A", BANGALORE

Before Shri George George K, JM & Shri Laxmi Prasad Sahu, AM

IT(TP)A No.524/Bang/2017 : Asst.Year 2012-2013

M/s.HP India Sales Private Limited (Formerly known as Hewlett-Packard India Sales Private Limited), 24 Salarpuria Area, Hosur Main Road, Adugodi Bangalore – 560 030. **PAN : AAACC9862F.**	v.	The Joint Commissioner of Income-tax, LTU Bangalore.
(Appellant)		(Respondent)

Appellant by : Sri.Ajay Vohra, Senior Counsel / Sri. Neeraj Jain, Sri.Lalit Attal & Sri.Karon Dhanuka, Advoicates
Respondent by : Sri.Harishchandra Naik, CIT-DR

Date of Hearing : 27.07.2022		**Date of Pronouncement : 18.08.2022**

O R D E R

Per George George K, JM :

This appeal at the instance of the assessee is directed against final assessment order dated 03.01.2017 passed u/s 143(3) r.w.s. 144C(13) of the I.T.Act. The relevant assessment year is 2012-2013.

2. The brief facts of the case are as follows:

The assessee is a company engaged in import of computer peripherals from its Associated Enterprises (AEs) for sale in India and also rendered certain support services. The return of income for assessment year 2012-2013 was filed on 29.02.2012, admitting total income of Rs.544,61,99,276. The return was revised on 25.03.2014

admitting total income of Rs.519,65,70,114. The assessment was selected for scrutiny and notice u/s 143(2) of the I.T.Act dated 12.08.2013 was issued and served on the assessee. During the course of assessment proceedings, it was noticed that international transaction with the AEs exceeded the prescribed limit, therefore, the matter was referred to the Transfer Pricing Officer (TPO) to determine the Arm's Length Price (ALP) of the said transactions. The TPO u/s 92CA of the I.T.Act vide order dated 28.01.2016 proposed TP adjustment of Rs.29,03,35,855. Pursuant to the TPO's order, draft assessment order was passed on 28.03.2016 u/s 143(3) r.w.s. 144C(1) of the I.T.Act incorporating the above said TP adjustment proposed by the TPO. The Assessing Officer also made certain additions / disallowances on the corporate tax front. Aggrieved by the draft assessment order, the assessee preferred objections before the Dispute Resolution Penal (DRP). The DRP vide its directions dated 26.12.2016 rejected the objections of the assessee and confirmed the TP adjustment proposed by the TPO. In corporate tax front, partial relief was given to the assessee by deleting the disallowance of excess depreciation on motor vehicles. Pursuant to the directions of the DRP, the impugned final assessment order was passed. Aggrieved by the final assessment order dated 03.01.2017, the assessee has filed the present appeal raising the following grounds:-

"General Ground

A. The assessment order dated January 03,2017, passed

by the learned Assessing Officer ("learned AO") under section 143(3) read with section 144C (13) of the Income Tax Act, 1961 ("the Act") in the case of HP India Sales Private Limited (formerly known as Hewlett-Packard India Sales Private Limited) ("HPISPL" or lithe Appellant") is not in accordance with law and is contrary to the facts and circumstances of the case.

1. ***Transfer Pricing adjustment under section 92CA of the Act***

1.1. The Honorable Dispute Resolution Panel ("DRP"), learned AO and Transfer Pricing Officer ("TPO") grossly erred in law and on facts of the case in determining the transfer pricing adjustment of Rs 290,335,855 in respect of alleged international transaction pertaining to excess Advertising, Marketing and Promotion ("AMP") expenditure, alleging the same to be not at arm's length in terms of the provisions of sections 92C (1) and 92C (2) of the Act read with Rule 10D of the Income-tax Rules, 1962 (lithe Rules").

1.2. The Honorable DRP have erred in upholding the approach followed by learned TPO in suo-moto benchmarking the alleged international transaction relating to AMP expenses without there being any reference from the AO in relation thereto, in addition to its power and jurisdiction to computing Arm's Length Price ("ALP") of the international transaction actually undertaken by the Appellant and referred by the learned AO to determine arm's length nature of such international transaction(s).

1.3. The learned AO and TPO erred in law and on facts by alleging that the unilateral AMP expenditure, being payments made to third parties, is an "international transaction" as per the provisions of section 92B of the Act, without appreciating that HPISPL had not incurred any expenditure on the directions of the Associated Enterprises ("AEs") and without having regard to the rulings in the case of Maruti Suzuki India limited vs Commissioner of Income-tax - ITA 110/2014 & 710/2015 - Honorable Delhi High Court, Bausch & Lomb Eyecare (India) Private limited vs ACIT - Honorable Delhi High Court ITA Nos. 643, 675-77/2014 and 165, 166/2015 Honda Siel Power Products Limited - Honorable Delhi High Court ITA 346/2015 and other judicial precedents that the Appellant relied upon. Furthermore, the learned TPO has erred in applying bright line method which is not one of the prescribed methods under section 92C of the Act, in determining the existence of an international transaction.

1.4. The learned AO, TPO and Honourable DRP erred in law and in fact by exceeding their jurisdictions by determining the ALP of a transaction with third parties that is not an international transaction as def0ined in Section 92B and with flagrant disregard to the rulings of Maruti Suzuki India Limited vs Commissioner of Income-tax ITA 110/2014 & 710/2015 Honorable Delhi High Court, and the jurisdictional tribunal ruling in the case of Essilor India Private Limited vs Dcrr. IT(TP} A No.29/Bang/2014 and IT (TP}A. No. 227/Bang/2015.

1.5. The Honorable DRP, learned AO and TPO have erred in law and on facts in holding that the appellant promoted the brand of the AE merely on the ground that the AMP expenses incurred by the Appellant are more than the AMP expenses incurred by the comparable entities. Thereby, the Honorable DRP, learned TPO and AO have alleged that the Appellant has put in its efforts / finances for the promotion of brand name of the Associated Enterprises and thereby building marketing intangibles for its AEs without giving cognizance to the commercial expediency of the Appellant.

1.6. The Honorable DRP, learned TPO and AO have erred in law and on facts in presuming that the transaction of brand promotion has taken place without bringing on record any tangible and reliable evidences and such a finding of the Honorable DRP, learned AO and TPO is perverse as being not supported by any materials on record.

1.7. The Honorable DRP, learned AO and TPO have erred on facts and in law in ignoring the facts that the AMP expenses incurred by the Appellant were in respect of its own business requirements / considerations / purposes and that all and any benefit resulting from such expenditure are to its own account (in the form of increased sales and market share) and benefits, if any, fetched on this account by the AEs, were purely incidental.

1.8. The Honorable DRP, learned AO and TPO have failed to consider that the alleged AMP expenses were incurred exclusively in relation to the Appellant's business, which is also evident from the fact that the expenditure have been accepted by the AO under section 37 of the Act.

1.9. The Honorable DRP, learned AO and TPO have erred in law and on facts by disregarding judicial pronouncements in undertaking transfer pricing adjustments.

1.10. The Honorable DRP, learned AO and TPO have not placed correct reliance on Organization for Economic Cooperation and Development ("OECD") TP Guidelines for Multinationals Enterprises and Tax Administrators, July 2010 and other international commentaries and jurisprudence, as updated by revised guidance under Action 10 on the Base Erosion and Profit Shifting project.

1.11. The Honorable DRP, learned AO and TPO have not placed correct reliance on the India Chapter of the United Nations Transfer Pricing Manual ("UN Manual") wherein it is clarified that compensation for AMP function need not be separate if the same is performed with the intention to exploit the results in the form of sales and profitability for the Indian entity.

Notwithstanding and without prejudice to the above grounds that the AMP expenditure incurred by the Appellant does not constitute an international transaction under Chapter X of the Act, the Appellant craves to raise following grounds of appeal on merits.

1.12. The Honorable DRP, learned AO and TPO have erred in law and on facts in concluding that the distribution and AMP are two distinctive functions and requires to be remunerated separately.

1.13. The Honorable DRP have erred in upholding the approach of the learned AO and TPO of carrying out separate benchmarking analysis for AMP and making an adjustment without considering and appreciating the fact that aggregation approach followed by the Appellant using Transactional Net Margin Method ("TNMM") would have already factored in all operating expenses (which includes the AMP expenditure) and proving it at arm's length to the satisfaction of the Honorable DRP, learned AO and TPO.

1.14. The Honorable DRP, learned AO and TPO have erred in law and on facts in not appreciating that the Appellant has not provided any value added / brand building services to its AE by incurring AMP expenses, and therefore, no mark-up could have been charged / levied on such expenses, even if the same was to be characterized as an 'international transaction'.

1.15. Notwithstanding the fact that the Appellant did not add

any value to its AE by way of incurring the AMP expenses, the learned AO and Honorable DRP erred in recognizing that even if the mark-up is to be applied, the same could have been charged only on the value added expenses incurred by the Appellant for such alleged brand promotion service and not on the entire amount incurred / paid to third party vendors.

1.16. The Honorable DRP, learned AO and TPO have erred in not appreciating that in view of the Appellant being contractually assured of a margin after cost recovery, the entire AMP expenditure has in fact been recovered from the AE and hence adjustment should only be restricted to mark-up element, that too if the international transaction relating to distribution was not at ALP.

1.17. IheHonorable DRP, learned AO and TPO have erred in law and on facts in choosing comparable companies without sharing the search strategy, for benchmarking the alleged transaction of rendering AMP services.

1.18. The Honorable DRP, learned AO and TPO have erred in law and on facts in considering certain expenses which are inextricably linked to sales promotion and do not lead to brand promotion (such as sales commission, trade discounts, sales schemes etc.), as a part of the alleged AMP brand promotion expenses while benchmarking the alleged brand promotion service, thereby resulting in the unjustified demand.

1.19. The Honorable DRP, learned AO and TPO have erred in law and on facts in not considering the several judicial precedents, including the decision by the Special Bench of Income Tax Appellant Tribunal ("ITAT") in the case of LG Electronics India (P.) Ltd (ITA No. 5140/DeI/2011) wherein it was held that selling expenses cannot constitute part of AMP expenses. The said aspect has been upheld by the Honorable High Court of Delhi including in the case of Maruti Suzuki India Ltd vs CIT (ITA 110/2014 & ITA 710/2015).

1.20. The Honorable DRP, learned AO and TPO have erred in applying the Bright Line Test ("BLT") as methodology to quantify the AMP service alleged to have been rendered by the Appellant to its AE and not placed reliance on Delhi High Court ruling of Sony Ericsson Mobile Communication India Private Limited (ITA Nos. 638/2015 & 648/2015).

1.21. The Honorable DRP, learned AO and TPO have erred in law and on facts in rejecting the Appellant's contention against the companies chosen as comparable by the learned TPO as listed below, in relation to determining the mark-up on excess AMP expenditure without giving concrete reasons:

a) Asian Business Exhibition & Conference Limited;
b) I C C International Agencies Limited;
c) Cyber Media (India) Limited;
d) Killick Agencies & Marketing Limited; and
e) Marketing Consultants & Agencies Limited

1.22. The Honorable DRP, learned AO and TPO have erred in law and on facts by not granting the benefit of quantitative adjustments (such as non-payment of royalty, etc.) while computing the transfer pricing adjustment for the alleged excessive AMP expenditure incurred by the Appellant.

1.23. The Honorable DRP, learned AO and TPO have erred in not granting appropriate favourable economic adjustments (including the working capital adjustment) when assessing the arm's length nature of alleged international transaction of provision of AMP services.

1.24. The Honorable DRP have erred in law and on facts in not giving specific direction for the following grounds of objection raised before the Honorable DRP. In this regard the Appellant relies on the Honorable Delhi High Court in Vodafone Essar Limited vs Dispute Resolution Pane - II in writ petition (civil) No. 7028/2010 and M/s Itron Metering Solutions India Pvt Ltd vs DCIT Circle-Bt l), New Delhi which states that speaking order has to be passed by the Honorable DRP

2.3. The learned TPO have erred in stating that the Assessee has used Resale Price Method ("RMP") to benchmark its international transactions. Based on this, the learned TPO has stated that gross margins do not reflect the expenditure relating to the additional function carried out by the Assessee in the form of AMP function. In doing so, the learned TPO has erroneously disregarded the fact that the Assessee has used Transactional Net Margin Method ("TNMM") to benchmark its transactions which factors in the benchmarking of the AMP expenses. Further the Honorable DRP has upheld the learned TPO's erroneous remarks stating that the ground is academic in nature and does not require specific directions.

2.4. Without prejudice to the fact that the Assessee is not in agreement with the learned TPO's / Honorable DRP contention that AMP expenses should be benchmarked separately, the revised Net profit Margin ("NPM") of the Assessee, after adding an alleged mark up of 15.69 percent to the allegedly excessive AMP expenses, as proposed by the learned TPO is 7.25 percent which is still higher than the ALP determined thereby establishing the alleged transaction of AMP expenses to be at arm's length.

No specific findings by the Honorable DRP on certain grounds of objections filed before the Honorable DRP at the time of DRP proceedings

1.25. The Honorable DRP have erred in law and on facts by not providing its own findings for certain grounds of objection on AMP raised by the Appellant at the time of DRP proceedings by merely stating that the Honorable DRP places reliance on High Court ruling of Sony Ericsson Mobile Communication India Private Limited (ITA Nos. 638/2015 & 648/2015) which is pending adjudication before the Supreme Court.

2. ***Disallowance of provision for leave encashment - Rs. 106,847,430***

2.1 The Honourable DRP and the learned AO have erred, in law and on facts, in disallowing an amount of Rs. 106,847,430 on account of leave encashment provision created by HPISPL for the subject AY;

2.2 The Honorable DRP and the learned AO have erred, in law and on facts, in disregarding the decision of the Honorable Calcutta High court in case of Exide Industries Limited and Anr vs UOI and Ors (292 ITR 470), wherein it was held that even a provision made for leave encashment is a liability and the same must be allowed as a deduction in computing the taxable income since the same is not in the nature of a contingent liability;

2.3 The Honorable DRP and the learned AO have erred in law and on facts, in making the subject disallowance after having noted that the Honorable Supreme Court (SLP Civil Appeal - 12060/2008) had allowed for claim of deduction towards provision for leave encashment in the return of income, after discharging applicable taxes.

3. ***Disallowance of depreciation on intangibles - Rs.2,873,837***

3.1 The Honorable DRP and the learned AO have erred in law and on facts in disallowing the depreciation claim of Rs.2,873,837 on intangible assets claimed by the Appellant.

3.2 The Honorable DRP and the learned AO have further, erred in law and on facts in not following the jurisdictional Bangalore Tribunal and the Commissioner of Income-tax (Appeals) ["CIT(A)"] decision in Appellant's own case for AY 2000-01, AY 2004-05, AY 2005-06, AY 2006-07, AY 2007-08 and AY 2008-09, on identical issues, which has been held in favor of the Appellant.

3.3 Without prejudice to the above, the Honorable DRP and the learned AO have erred in law and on facts in not allowing the said expenditure as a deduction under section 37 of the Act.

4. Disallowance of interest on Customs duty - Rs.346,884,164

4.1 The Honorable DRP and the learned AO have erred in law and on facts, in disallowing an amount of Rs.346,884,164, which represents interest on custom duty, stating that the same is covered within the provisions of section 43B of the Act;

4.2 The Honorable DRP and the learned AO have erred in disregarding the detailed submission made by Appellant, wherein it was stated that the interest on custom duty is not covered with the scope of the provisions of section 43B of the Act and reliance placed on the decision of Honorable Calcutta High Court in the case of Hindustan Motors Limited Vs CIT (218 ITR 450) and other decisions relied on by the Appellant;

4.3 The Honorable DRP and the learned AO has further erred in law and on facts, in stating that decisions of the Courts are conflicting on the subject issue, without appreciating that the decision of the Calcutta High Court (supra) was on interest on custom duty.

4.4 Without prejudice to the above, the Honorable DRP and the learned AO, have erred in law in not directing / providing relief in respect of the aforementioned disallowance in AY 2013-14, having noted that the same has been remitted during previous year 2012-13.

5. Consequential relief - Deferred revenue

5.1 Without prejudice and notwithstanding the Appellant's grounds on taxability of Deferred Revenue raised for earlier AYs, the Honorable DRP and the learned AO have erred in law and on facts, in not granting any relief to the Appellant with respect to the negative movement of Deferred Revenue account representing the income recognized during the year, which has been bought to tax by the AO in the earlier years (ie in AY 2008-09, AY 2009-10).

5.2 The Honorable DRP and the learned AO have erred in law and on facts in upholding the principles of taxation of amount of deferred revenue pronounced by the erstwhile AO in the assessment order of earlier AYs.

5.3 The Honorable DRP and Learned AO have erred in law and on facts on one hand upholding the principles of taxation of amount of deferred revenue pronounced by the erstwhile AO in the assessment order of earlier AY's and on the other hand not granting the credit in respect of income recognized by the Appellant in AY 2012-13

5.4 The learned AO and the Honorable DRP has erred in law and facts in not appreciating the fact that non-grant of relief in respect of negative movement of Deferred Revenue results in double taxation of same income in different years which is not permissible under the taxation laws.

6. Other grounds

6.1 The Honorable DRP and the learned AO have erred in law and on facts in making adjustments of Rs. 746,941,286 to the returned income of the Appellant.

6.2 The learned AO has erred in law and on facts in proposing to initiate penalty proceedings under section 271(1) (c) of the Act.

Each of the above ground is independent and without prejudice to the other grounds of appeal preferred by the Appellant.

The Appellant craves leave to add, alter, vary omit, substitute or amend the above grounds of appeal, at any time before or at the time of hearing of the appeal, so as to enable the learned members of the Honorable Tribunal to issue orders."

Ground A is a general ground and no specific adjudication is called for, hence, we dismiss the said ground. The other grounds, we shall adjudicate as under:-

Transfer Pricing Adjustment of Rs.29,03,35,855 on account of AMP Expenses (Ground 1 and sub grounds)

3. During the relevant previous year, the assessee had entered into following international transactions with its AEs:-

Transaction	Most Appropriate Method
Import of computer and computer peripherals	Transactional Net Margin Method
Purchase of software licenses	Aggregated with transaction of import of computer and computer peripherals.
Prior period income and expenses	TNMM (Aggregated with transaction of import or import of computer and computer peripherals)
Reimbursement of expenses	Aggregated with transaction of import of computer and computer peripherals
Recovery of expenses	Aggregated with transaction of import of computer and computer peripherals.

4. Since the operating margin of the assessee was at 2.5% and the margin of comparable companies was at 2.26%, the international transaction of import of resale of computer and computer peripherals was considered to be at arm's length. During the course of transfer pricing proceedings, the TPO did not dispute the benchmarking analysis of the international transaction undertaken by the assessee and accepted the same to be at arm's length. The TPO, however,

proceeded to make an adjustment of Rs.29,03,35,855 pertaining to Advertisement, Marketing and Promotion (AMP) expenses. Applying the Bright Line Test (BLT), the TPO computed AMP / sales ratio of the assessee at 1.17%. This was compared with similar ratio of comparables computed at 0.88%. The difference between the two ratios computed at 0.29% (1.17% - 0.88%) was applied on assessee's sale of Rs.8653,80,00,000 and a sum of Rs.25,09,60,200 was held to be the TP adjustment on excess expenditure incurred by the assessee on account of AMP for developing of intangible onwed by the AE. The TPO also added a mark up of Rs.3,93,75,655 calculated at 15.69% on the TP addition of Rs.25,09,60,200 for the services of brand promotion rendered by the assessee to its AE. The mark up percentage was calculated as an average margin earned by uncontrolled comparables selected by the TPO. The total TP addition was thus computed at Rs.29,03,35,855.

5. Aggrieved, the assessee filed objections before the DRP. The DRP vide its directions dated 26.12.2016, rejected the assessee's objections and confirmed the TP addition of Rs.29,03,35,855. The relevant finding of the DRP reads as follows:-

> *"Having considered the submission, on perusal of paragraph 4 of the order of the TPO, it is noticed by us that under TNMM the assess selected 9 comparable out of which 6 not found suitable by TPO, by application of trading sales less than 75%, by application of different financial filter, and 4 due to non-availability of data for the financial year relevant to assessment year. The TPO subsequently carried out an independent search and selected 8 companies which include*

3 companies selected by the taxpayer. The OP/OC means margin with respect to these comparable arrived at 3.89% as against the margin in respect of the assessee company computed by TPO at 1O.14%.However it is noticed by us that there is a contradiction in the finding of TPO in paragraph 4 and 14.6 of the order of the TPO. However the final outcome remain the same that, margin of assessee company, at the entity level under TNMM, is at arm's length. However the same does not help the assessee considering the fact that the decision of Delhi High court in the case of Sony Erricson Mobile Communication India Private Limited and others Vs CIT (ITA 16 of 2014 with CA 155 of 2014) in which it was held that once the margin at entity level under TNMM, are at arm's length no separate adjustment for AMP expense can be made, has not been accepted by the Department and has been SLP has been filed Hon'ble Supreme Court of India on the questions of law mentioned by TPO in paragraph 12 of his order. In such circumstances, we do not find any infirmity in independently evaluating the transaction of AMP by the TPO. The above objections are accordingly rejected"

6. Aggrieved by the directions of the DRP, the assessee has raised this issue before the Tribunal. The learned AR submitted that Bright Line Test is not one of the prescribed methods under the transfer pricing provisions. In this context, the learned AR relied on the judgment of the Hon'ble Delhi High Court in the case of Sony Ericsson Mobile Communication India Pvt. Ltd. reported in 374 ITR 118 (Delhi). Further, it was submitted by placing reliance on the judgment of the Hon'ble Delhi High Court in the case of Maruti Suzuki India Limited reported in 381 ITR 117 (Delhi) that Revenue needs to be established the existence of international transaction before undertaking benchmarking of AMP expenses and such transaction cannot be inferred merely on the basis of Bright Line Test. The learned AR by referring to sections 92B(1) and 92F of the I.T.Act, contended

that the AMP expenditure is not an international transaction. It was also contended that even assuming for the sake of argument that though the AMP expenditure incurred by the assessee, results in an indirect benefit to the AE, no part of such expenditure can be disallowed in the hands of the assessee. In support of the above submission, the learned AR relied on the judgment of the Hon'ble Delhi High Court in the case of Maruti Suzuki India Limited (supra). Lastly, it was contended that the AMP expenditure being closely linked with the business of the assessee, has to be benchmarked on aggregate basis by applying entity level TNMM and if the margins at the entity level are at arm's length, no separate adjustment on account of AMP expenditure is warranted. In this context, reliance was placed on the judgment of the Hon'ble Delhi High Court in the case of Magneti Marelli Powertrain India Pvt. Ltd. reported in 389 ITR 469 (Delhi).

7. The learned Departmental Representative supported the orders of the TPO and the DRP.

8. We have heard rival submissions and perused the material on record. The issue as to whether AMP expenditure is an international transaction or not was considered by the Delhi High Court in Maruti Suzuki India Ltd. 381 ITR 117 and it was held as under:-

> *"Step wise analysis of statutory provisions*
>
> *62. If a step by step analysis is undertaken of Sections 92B to 92F, the sine qua non for commencing the transfer pricing exercise is to show the existence of an international transaction. The next step is to determine the price of such*

transaction. The third step would be to determine the ALP by applying one of the five price discovery methods specified in Section 92C. The fourth step would be to compare the price of the transaction that is shown to exist with the ALP and make the transfer pricing adjustment by substituting the ALP for the contract price.

63. A reading of the heading of Chapter X ["Computation of income from international transactions having regard to arm's length price"] and Section 92 (1) which states that any income arising from an international transaction shall be computed having regard to the ALP, Section 92C (1) which sets out the different methods of determining the ALP, makes it clear that the transfer pricing adjustment is made by substituting the ALP for the price of the transaction. To begin with there has to be an international transaction with a certain disclosed price. The transfer pricing adjustment envisages the substitution of the price of such international transaction with the ALP.

64. The transfer pricing adjustment is not expected to be made by deducing from the difference between the 'excessive' AMP expenditure incurred by the Assessee and the AMP expenditure of a comparable entity that an international transaction exists and then proceed to make the adjustment of the difference in order to determine the value of such AMP expenditure incurred for the AE. And, yet, that is what appears to have been done by the Revenue in the present case. It first arrived at the 'bright line' by comparing the AMP expenses incurred by MSIL with the average percentage of the AMP expenses incurred by the comparable entities. Since on applying the BLT, the AMP spend of MSIL was found 'excessive' the Revenue deduced the existence of an international transaction. It then added back the excess expenditure as the transfer pricing 'adjustment'. This runs counter to legal position explained in CIT v. EKL Appliances Ltd. (2012) 345 ITR 241 (Del), which required a TPO "to examine the 'international transaction' as he actually finds the same." In other words the very existence of an international transaction cannot be a matter for inference or surmise.

65. As already noticed, the decision in Sony Ericsson has done away with the BLT as means for determining the ALP of an international transaction involving AMP expenses.

Revenue's contentions

66. It is contended by the Revenue that the mere fact that the Indian entity is engaged in the activity of creation, promotion or maintenance of certain brands of its foreign AE or for the creation/promotion of new/existing markets for the AE, is by itself enough to demonstrate that there is an arrangement with the parent company for this activity. It is urged that merely because MSIL and SMC do not have an explicit arrangement/agreement on this aspect cannot lead to the inference that there is no such arrangement or the entire AMP activity of the Indian entity is unilateral and only for its own benefit. According to the Revenue, "the only credible test in the context of TP provisions to determine whether the Indian subsidiary is incurring AMP expenses unilaterally on its own or at the instance of the AE is to find out whether an independent party would have also done the same." It is asserted: "An independent party with a short term agreement with the MNC will not incur costs which give long term benefits of brand & market development to the other entity. An independent party will, in

such circumstances, carry out the function of development of markets only when it is adequately remunerated for the same."

67. Reference is made by Mr. Srivastava to some sample agreements between Reebok (UK) and Reebok (South Africa) and IC Issacs & Co and BHPC Marketing to urge that the level of AMP spend is a matter of negotiation between the parties together with the rate of royalty. It is further suggested that it might be necessary to examine whether in other jurisdictions the foreign AE i.e., SMC is engaged in AMP/brand promotion through independent entities or their subsidiaries without any compensation to them either directly or through an adjustment of royalty payments.

Absence of a machinery provision

68. The above submissions proceed purely on surmises and conjectures and if accepted as such will lead to sending the tax authorities themselves on a wild-goose chase of what can at best be described as a 'mirage'. First of all, there has to be a clear statutory mandate for such an exercise. The Court is unable to find one. To the question whether there is any 'machinery' provision for determining the existence of an international transaction involving AMP expenses, Mr. Srivastava only referred to Section 92F (ii) which defines ALP to mean a price "which is applied or proposed to be applied in a transaction between persons other than AEs in uncontrolled conditions". Since the reference is to 'price' and to 'uncontrolled conditions' it implicitly brings into play the BLT. In other words, it emphasises that where the price is something other than what would be paid or charged by one entity from another in uncontrolled situations then that would be the ALP. The Court does not see this as a machinery provision particularly in light of the fact that the BLT has been expressly negatived by the Court in Sony Ericsson. Therefore, the existence of an international transaction will have to be established de hors the BLT.

69. There is nothing in the Act which indicates how, in the absence of the BLT, one can discern the existence of an international transaction as far as AMP expenditure is concerned. The Court finds considerable merit in the contention of the Assessee that the only TP adjustment authorised and permitted by Chapter X is the substitution of the ALP for the transaction price or the contract price. It bears repetition that each of the methods specified in S.92C (1) is a price discovery method. S.92C (1) thus is explicit that the only manner of effecting a TP adjustment is to substitute the transaction price with the ALP so determined. The second proviso to Section 92C (2) provides a 'gateway' by stipulating that if the variation between the ALP and the transaction price does not exceed the specified percentage, no TP adjustment can at all be made. Both Section 92CA, which provides for making a reference to the TPO for computation of the ALP and the manner of the determination of the ALP by the TPO, and Section 92CB which provides for the "safe harbour" rules for determination of the ALP, can be applied only if the TP adjustment involves substitution of the transaction price with the ALP. Rules 10B, 10C and the new Rule 10AB only deal with the determination of the ALP. Thus for the purposes of Chapter X of the Act, what is envisaged is not a quantitative adjustment but only a substitution of the transaction price with the ALP.

70. What is clear is that it is the 'price' of an international transaction which is required 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. The burden is on the Revenue to first show the existence of an international transaction. Next, to ascertain the disclosed 'price' of such transaction and thereafter ask whether it is an ALP. If the answer to that is in the negative the TP adjustment should follow. The objective of Chapter X is to make adjustments to the price of an international transaction which the AEs involved may seek to shift from one jurisdiction to another. An 'assumed' price cannot form the reason for making an ALP adjustment.

71. Since a quantitative adjustment is not permissible for the purposes of a TP adjustment under Chapter X, equally it cannot be permitted in respect of AMP expenses either. As already noticed hereinbefore, what the Revenue has sought to do in the present case is to resort to a quantitative adjustment by first determining whether the AMP spend of the Assessee on application of the BLT, is excessive, thereby evidencing the existence of an international transaction involving the AE. The quantitative determination forms the very basis for the entire TP exercise in the present case.

72. As rightly pointed out by the Assessee, while such quantitative adjustment involved in respect of AMP expenses may be contemplated in the taxing statutes of certain foreign countries like U.S.A., Australia and New Zealand, no provision in Chapter X of the Act contemplates such an adjustment. An AMP TP adjustment to which none of the substantive or procedural provisions of Chapter X of the Act apply, cannot be held to be permitted by Chapter X. In other words, with neither the substantive nor the machinery provisions of Chapter X of the Act being applicable to an AMP TP adjustment, the inevitable conclusion is that Chapter X as a whole, does not permit such an adjustment.

73. It bears repetition that the subject matter of the attempted price adjustment is not the transaction involving the Indian entity and the agencies to whom it is making payments for the AMP expenses. The Revenue is not joining issue, the Court was told, that the Indian entity would be entitled to claim such expenses as revenue expense in terms of Section 37 of the Act. It is not for the Revenue to dictate to an entity how much it should spend on AMP. That would be a business decision of such entity keeping in view its exigencies and its perception of what is best needed to promote its products. The argument of the Revenue, however, is that while such AMP expense may be wholly and exclusively for the benefit of the Indian entity, it also enures to building the brand of the foreign AE for which the foreign AE is obliged to compensate the Indian entity. The burden of the Revenue's song is this: an Indian entity, whose AMP expense is extraordinary (or 'non-routine') ought to be compensated by the foreign AE to whose benefit also such expense enures. The 'non- routine' AMP spend is taken to have 'subsumed' the portion constituting the 'compensation' owed to the Indian entity by the foreign AE. In such a scenario what will be required to be benchmarked is not the AMP expense itself but to what extent the Indian entity must be compensated. That is not within the realm of the provisions of Chapter X.

74. The problem with the Revenue's approach is that it wants every instance of an AMP spend by an Indian entity which happens to use the brand of a foreign AE to be presumed to involve an international transaction. And this, notwithstanding that this is not one of the deemed international transactions listed under the Explanation to Section 92B of the Act. The problem does not stop

here. Even if a transaction involving an AMP spend for a foreign AE is able to be located in some agreement, written (for e.g., the sample agreements produced before the Court by the Revenue) or otherwise, how should a TPO proceed to benchmark the portion of such AMP spend that the Indian entity should be compensated for?

75. As an analogy, and for no other purpose, in the context of a domestic transaction involving two or more related parties, reference may be made to Section 40 A (2) (a) under which certain types of expenditure incurred by way of payment to related parties is not deductible where the AO "is of the opinion that such expenditure is excessive or unreasonable having regard to the fair market value of the goods." In such event, "so much of the expenditure as is so considered by him to be excessive or unreasonable shall not be allowed as a deduction." The AO in such an instance deploys the 'best judgment' assessment as a device to disallow what he considers to be an excessive expenditure. There is no corresponding 'machinery' provision in Chapter X which enables an AO to determine what should be the fair 'compensation' an Indian entity would be entitled to if it is found that there is an international transaction in that regard. In practical terms, absent a clear statutory guidance, this may encounter further difficulties. The strength of a brand, which could be product specific, may be impacted by numerous other imponderables not limited to the nature of the industry, the geographical peculiarities, economic trends both international and domestic, the consumption patterns, market behaviour and so on. A simplistic approach using one of the modes similar to the ones contemplated by Section 92C may not only be legally impermissible but will lend itself to arbitrariness. What is then needed is a clear statutory scheme encapsulating the legislative policy and mandate which provides the necessary checks against arbitrariness while at the same time addressing the apprehension of tax avoidance.

76. As explained by the Supreme Court in CIT v. B.C. Srinivasa Setty (1979) 128 ITR 294 (SC) and PNB Finance Ltd. vs. CIT (2008) 307 ITR 75 (SC) in the absence of any machinery provision, bringing an imagined international transaction to tax is fraught with the danger of invalidation. In the present case, in the absence of there being an international transaction involving AMP spend with an ascertainable price, neither the substantive nor the machinery provision of Chapter X are applicable to the transfer pricing adjustment exercise."

9. The decision of the Delhi High Court in Sony Ericsson Mobile Communications India (P.) Ltd. v. CIT [2015] 374 ITR 118 was followed and it was held that the bright line test followed by the Revenue in making the AMP TP adjustment cannot be accepted. In the present case also, no material is brought on record by the TPO to establish the existence of an arrangement, understanding or action in concert with the AE for incurring the AMP expenses for the benefit of the AE. Merely because the AE has a financial interest, it cannot be

presumed that AMP expenses incurred by the assessee are at the instance or on behalf of the associated enterprise. In the absence of any international transaction relating to AMP expenses, the impugned TP adjustment cannot be sustained. Moreover, the TPO having accepted the ALP of other international transactions at the entity level, proceeded to make a separate TP adjustment for the AMP expenses. At para 4.2 of the TPOs order, the TPO has given a finding that the net margins earned by the taxpayer from the product segment is 3.82% and that at the entity level is 7.29%. The margin earned by the taxpayer at the entity level as calculated by the TPO is 2.50%. Hence, no adverse inference drawn by the TPO in respect of the distribution segment results. Thus, the TPO has accepted the entity level margins earned by the assessee but proceeded to make TP adjustment on AMP expenses. The Hon'ble Delhi High Court in Sony Ericsson Mobile Communications India (P.) Ltd. v. CIT [2015] 374 ITR 118 held that once the revenue accepts the entity level margins as per the most appropriate method, it would be inappropriate to treat a particular expenditure as a separate international transaction. It was held that such an exercise would lead to unusual and absurd results. Relevant observations from the above decision in this context are as under:-

> *"101. However, once the Assessing Officer/TPO accepts and adopts TNM Method, but then chooses to treat a particular expenditure like AMP as a separate international transaction without bifurcation/segregation, it would as noticed above. lead to unusual and incongruous results as AMP expenses is*

> *the cost or expense and is not diverse. It is factored in the net profit of the inter-linked transaction. This would be also in consonance with Rule 10B(J)(e), which mandates only arriving at the net profit margin by comparing {he profits and loss account of the tested party with the comparable. The TN/v! Method proceeds on the assumption that functions, assets and risk being broadly similar and once suitable adjustments have been made, all things get taken into account and stand reconciled when computing the net profit margin. Once the comparables pass the functional analysis test and adjustments have been made, then the profit margin as declared when matches with the com parables would result in affirmation of the transfer price as the arm's length price. Then to make a comparison of a horizontal item without segregation would be impermissible.*

10. Similarly, in the case of Maruti Suzuki India Ltd v CIT [2016] 381 ITR 117 at para 86 of the judgment, the Hon'ble Delhi High Court held as under:-

> *"MSIL's higher operating margins*
>
> *86. In Sony Ericsson Mobile Communications India (P.) Ltd. (supra) it .was held that if an Indian entity has satisfied the TNMM i.e. the operating margins of the Indian enterprise are much higher than the operating margins of the comparable companies, no further separate adjustment for AMP expenditure was warranted. This is also in consonance with Rule 10B which mandates only arriving at the net profit by comparing the profit and loss account of the tested party with the comparable. As far as MSIL is concerned. its operating profit margin is 11.19% which is higher than that of the comparable companies whose profit margin is 4.04%. Therefore, applying the TNMM method it must be stated that there is no question of TP adjustment on account of AMP expenditure."*

11. Respectfully following the above judgment of the Hon'ble Delhi High Court, we delete the AMP TP adjustment of Rs. 25,09,60,200 and the mark up thereon amounting to Rs. 3,93,75,655.

Ground Nos 2.1 to 2.3 (Corporate Tax)

12. The above grounds deals with the disallowance of provision for leave encashment of Rs.10,68,47,430. The AO disallowed the said provision under section 43B(f) for the reason that leave encashment can be claimed as deduction only on actual payment basis. The disallowance made by the A.O. was confirmed by the DRP.

13. We have heard rival submissions and perused the material on record. The Calcutta High Court in Exide Industries Ltd v UOI 292 ITR 470 struck down the provisions of section 43B(f). However, the Supreme Court in UOI v Exide Industries Ltd [2020] 425 ITR 1 held that clause (f) of section 43B is constitutionally valid and operative for all purposes. Thus, the provision for leave encashment of Rs.10,68,47,430 was righty disallowed by the AO and we confirm the same. The assessee has taken an alternate plea that AO be directed to grant relief in respect of payment made towards provision for leave encashment in subsequent years. The direction to allow deduction for subsequent years is not pertaining to the year under consideration and hence we refrain from giving such directions. However, we direct the AO to verify the actual payments made during the previous year relevant to the assessment year under consideration towards leave encashment and allow the same as deduction under section 43B(f). The AO shall also ensure that the assessee does not get double deduction on provision basis and payment basis.

Ground 3 (Corporate Tax)

14. The above ground deals with the disallowance of depreciation on intangibles amounting to Rs.28,73,837. The AO has disallowed the same following the earlier years assessment orders, even though the said issue was decided in favour of the assessee by the CIT(A) and ITAT for the earlier years. The AO concluded that the issue is pending before the High Court of Kamataka and hence the disallowance was made. The DRP confirmed the disallowance to keep the issue alive. However, the AO was directed to make a protective disallowance till the final outcome on the IT AT decision in respect of the above issue.

15. We have heard rival submissions and perused the material on record. The Kamataka High Court in assessee's own case for AY 2000-01 in ITA No 250 of 2011 dated 30.11.2020 has decided this issue in favour of the assessee and held as follows:-

> *"Thus, from perusal of the order passed by the Assessing Officer itself it is axiomatic that he has found that the goodwill has been calculated and has been allotted to intangibles. For yet another reason, the order passed by the tribunal has to be upheld. It is pertinent to note that the order passed by the tribunal is based on the decision of the Delhi Bench of Tribunal which has been upheld by High Court of Delhi in Hindustan Coca Cola Beverages (p) Ltd.*
>
> *In view of preceding analysis, the substantial question of law framed by a bench of this court is answered against the revenue and infavour of the assessee. In this result, we do not find any merit in this appeal. The same fails and is hereby dismissed."*

16. Following the above, we allow depreciation on intangibles amounting to Rs. 28,73,837 for the year under consideration.

Grounds 4.1 to 4.4

17. The above grounds deals with the disallowance of interest on customs duty amounting to Rs.34,68,84,164. The AO disallowed the same for the reason that interest on customs duty is allowable on actual payment basis under section 43B. As the said sum was not paid during the previous year relevant to assessment year under consideration, he proceeded to disallow the same. The DRP confirmed the action of the AO.

18. Aggrieved, the assessee has raised this issue before the ITAT. The learned AR relies on the decisions in Hindustan Motors Ltd v CIT 218 ITR 450 (Calcutta), CIT v Padmavathi Raje Cotton Mills Ltd 239 ITR 355 (Calcutta) and CIT v India Pistons Ltd [2001] 119 Taxman 384 (Madras) and contends that interest on customs duty is not covered by section 43B, hence deduction should be allowed even if actual payment is not made.

19. On the other hand, the learned DR relies on the decisions in the case of Shri Pipes v DCIT 289 ITR 154 (Rajasthan) and CIT v Andhra Sugars Ltd [2014] 367 ITR 195 (High Court of Telangana and Andhra Pradesh) which have held that interest on customs duty is allowable only on payment basis under section 43B.

20. We have heard rival submissions and perused the material on record. We find that the Hon'ble Calcutta High Court in Hindustan Motors Ltd v CIT 218 ITR 450 in a majority decision held that interest payable under the Customs Act for keeping the imported goods in the customs warehouse beyond the statutory period cannot be treated as part and parcel of the duty payable on import of goods. It was held by the Hon'ble High Court that the levy of duty on import of goods and the levy of interest on account of warehoused goods are two distinct and separate liabilities arising in two different events. Following the above judgment of the Hon'ble Calcutta High Court in CIT v Padmavathi Raje Cotton Mills Ltd 239 ITR 355 held that interest levied under section 59 of the Haryana General Sales Tax Act, 1973 on arrears of purchase tax is not hit by section 43B. Whereas, the Madras High Court in CIT v India Pistons Ltd [2001] 119 Taxman 384 was directly concerned with allowability of interest paid for delayed remittance of customs duty under section 37(1). Applicability of section 43B in the said case was not an issue at all. In Shri Pipes v DCIT 289 ITR 154 (Rajasthan) interest accrued on delayed payment of sales tax under Rajasthan Sales tax Act 1954 was held to be part of tax within the meaning of section 43B and in CIT v Andhra Sugars Ltd [2014] 367 ITR 195 (Hon'ble High Court of Telangana and Andhra Pradesh) interest payable on arrears of purchase tax was held to be covered by section 43B of the Act.

21. What we observe from the above judgments is that the applicability of section 43B in respect of interest on customs duty depends on whether interest on customs duty is levied for keeping the imported goods in the customs warehouse beyond the statutory period or for non-payment of customs duty. In the instant case, the AO has not examined the nature of levy of interest on customs duty. If the interest on customs duty is payable for keeping the imported goods in the customs warehouse beyond the statutory period the said interest would not be covered by section 43B and would be allowable as deduction even if it is not paid. However, if the interest on customs duty is payable for the arrears of customs duty or delayed payment of customs duty then the said interest would be regarded as part and parcel of the customs duty. In such circumstances, the assessee cannot get deduction for interest payable as such interest is directly linked to non-payment or late payment of customs duty. As customs duty is allowable only on payment basis under section 43B, interest levied on arrears or late payment of customs duty is also allowable on actual payment basis under section 43B. The AO is directed to verify the nature of levy of interest on customs duty and decide the allowability of deduction as per our above direction. It is ordered accordingly.

Grounds 5.1 to 5.4 (Corporate Tax)

22. The above grounds deals with the issue of consequential relief on negative movement of deferred revenue for the year

under consideration. We note that this issue was considered the ITAT in assessee's own case for AY 2011-12 in IT(TP)A No 779/Bang/2016 and it held as under:-

> *"19. We have heard the rival submissions and perused the material on record. We notice the same issue is pending before the coordinate bench of the Tribunal for adjudication against the order of the CIT(A) for various assessment years from 2009-10 in assessee's own case. The issue can be decided for the year under consideration only based on the outcome of the other appeals pending for the earlier years as the decision will have a cascading effect on the issue for the year under consideration. At this point in time we can only issue a direction to the A.O. to follow the decision that would be adjudicated by the coordinate bench of the Tribunal for assessment year 2009-10 & 2010-11 on this issue. The AO is directed to grant consequential relief in accordance with the decision of the coordinate bench of the Tribunal in terms of adjustment of TDS credit and negative movement in the deferred revenue. The AO is directed accordingly and that a reasonable opportunity of being heard to be given to the assessee before the final decision. This ground of the assessee is allowed for statistical purposes."*

23. Following the above, for this year also, the AO is directed to grant consequential relief in accordance with the decision of the coordinate bench of the Tribunal in terms of adjustment of TDS credit and negative movement in the deferred revenue. The AO is directed accordingly and that a reasonable opportunity of being heard to be given to the assessee before the final decision.

Grounds 6, 6.1 & 6.2

24. The above grounds were not pressed by the learned AR during the course of hearing, hence, the grounds 6, 6.1 and 6.2 are dismissed.

25. In the result, the appeal filed by the assessee is partly allowed.

Order pronounced on this 18th day of August, 2022.

Sd/-	**Sd/-**
(Laxmi Prasad Sahu)	**(George George K)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Bangalore; Dated : 18th August, 2022.
Devadas G*

Copy to :
1. The Appellant.
2. The Respondent.
3. The DRP-1, Bengaluru.
4. The Pr.CIT, Bengaluru.
5. The DR, ITAT, Bengaluru.
6. Guard File.

Asst.Registrar/ITAT, Bangalore