

## ESPN Software India Limited – ITAT – Delhi

**Outcome:** In **favour** of taxpayer

**Category:** Basket Approach

Tax Court rules in favour of taxpayer with respect to co-relation of distribution and advertisement sale activities of the taxpayer for determining the arm's length price.

In the year under assessment, taxpayer becomes a full-risk distributor as part of its business strategy, and to comply with foreign exchange regulations of RBI (Circular No. 76). Before such events had transpired, taxpayer advertised in the Indian market and earned a suitable commission on billables from its overseas AE. Tax authorities argued that the merger of the above segments was a deliberate measure to cover losses in advertisement sales.

Placing reliance on Guideline 13/2/2002-BP&L/BC-IV issued by Government of India – Ministry of I&B, Tax Court observes that a taxpayer would be required to aggregate channel subscription and air time sale segment activities. Further, it is derived that higher the subscriber base of a channel, higher is the advertisement reach. Hence, Tax Court accepts aggregated benchmarking of distribution of channel and aired advertisements.

## Indian Additives Limited – ITAT – Chennai

**Outcome:** In **favour** of taxpayer

**Category:** Profit level indicator

Tax Court ruled in respect of claim for adjustments by taxpayer to show a fair picture of profit level indicator for use in the performance of an arm's length analysis.

During taxpayer's litigation, tax officer compared an extra comparable company's (third party) margins to taxpayer, in turn creating a transfer pricing adjustment. Taxpayer argued that the comparable company enjoyed economies of scale, being significantly larger in terms of size and net worth, and sought an adjustment.

Tax Court articulates that adjustment can be made only if cost of comparable company can be made available and if it is found to be lower than that of the taxpayer. As per the facts, taxpayer claimed an adjustment on -

- **Raw material cost** – Taxpayer argues that the comparable company incurs lower raw material costs of Lube Oil, as it enjoyed better discounts from IOCL.
- **Zinc tolling fees** – Taxpayer claims an adjustment on Zinc tolling fees because the comparable company had an in-house facility to manufacture Zinc, while taxpayer did not.
- **Transport cost** – Taxpayer contends that comparable company incurs lesser transportation costs as it provides for local customers, while taxpayer provides to customers within India.

Tax Court rules to allow adjustment for raw material cost and directs matter of Zinc tolling fee, back to tax officer for allowing adjustment. However, Tax Court rejects transport cost adjustment as it could not be reliably determined that costs of comparable company are lesser than the transport cost of the taxpayer.

## SIS Live – ITAT – Delhi

**Outcome:** **Against** taxpayer

**Category:** Cash basis accounting

Tax Court rules in respect of applicability of transfer pricing provisions where cash basis of accounting is followed by taxpayer.

Accordingly, taxpayer claimed that it kept books on a cash basis, and hence expenses from international transactions could not be accounted or deducted for. Tax Court found that the transactions in the nature of availing technical services and equipment on hire from AE would be treated as an international transaction, as it fell within the meaning of international transaction under Section 92B(1) of the Income-tax Act 1961.

Further, the Tax Court rejects taxpayer's contention that determination of arm's length benchmarking should be done only in year where the expenses incurred were claimed as deduction, under the cash system.

## Commscope Networks India Private Limited – ITAT – Bangalore

**Outcome:** In favour of taxpayer  
**Category:** Foreign exchange gain

Tax Court rules in respect of treatment of foreign exchange gain arisen on account of taxpayer's turnover.

Accordingly, the question arises whether the foreign exchange gain arises on account of current year's turnover or earlier year's turnover. Tax Court opines that the foreign exchange fluctuation gain considered on an earlier year's turnover would give a distorted result. Because while working out taxpayer's profit margins, the related turnover would not be included in the denominator, but the forex gain would be considered in the numerator.

Therefore, Tax Court directs the issue back to tax officer for re-consideration, establishing that forex gain arises out of current year turnover, to be considered as operating profit while calculating taxpayer's profit margins, and if the turnover pertains to an earlier year, it should be excluded.

### Recent News:

#### RBI notifies scheme for FDI in LLPs

The Reserve Bank of India has amended the Foreign Exchange Management (Transfer or issue of Security by a Person Resident outside India) Regulations, 2000 by notifying the FDI-LLP scheme in Limited Liability Partnerships (in accordance with LLP Act, 2008).

As per new regulations, an eligible investor shall be a person resident outside India or an entity incorporated outside India that contributes foreign capital through capital contribution or acquisition/transfer of profit shares in an LLP.

It is clarified in the scheme that, investment by 'profit share' will fall under the category of 'reinvestment of earnings'.

However, the scheme shall not be applicable to the following:

- If the investor is a citizen or entity from Pakistan or Bangladesh.
- A SEBI registered Foreign Portfolio Investor, Foreign Institutional Investor, or Foreign Venture Capitalist Investor.

Permissibility of FDI in LLPs, through automatic route with no FDI linked performance conditions (for instance, condition of minimum capitalization):

- LLPs can take FDI benefit in sectors where 100% FDI is allowed.
- Indian company/ LLP having foreign investment can make downstream investment in another company or LLP where there is 100% FDI. Therefore, the Indian company/ LLP cannot make downstream investment to any entity in India, except mentioned as per the scheme. Here, the onus shall be on the Indian company/ LLP to comply.
- Conversion of company (with foreign investment) to LLP if company is engaged in sector where foreign investment up to 100% is permitted.

Regarding pricing, FDI in LLP would have to be more than or equal to the fair price of capital contribution / profit share of an LLP and a valuation certificate to that effect shall be issued by a CA / Cost Accountant / approved valuer from Govt.'s panel.

For transfer of capital contribution/ profit shares, from a non-resident to a resident, the transfer shall be less than or equal to the fair price of the capital contribution/ profit share of an LLP.

LLPs receiving FDI in previous year(s) and current year would be required to furnish 'Annual Return on Foreign Liabilities and Assets' on or before July 15 to the RBI.