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Edition: 1st May 2021 – 31st May 2021

Renfro India Private Limited – Mumbai ITAT
Outcome: In favour of the taxpayer
Category: Principle of consistency

The taxpayer was engaged in the business of manufacture and sale/export of knitted socks during the period under consideration (AY 2009-10). The taxpayer sold the above-mentioned products to its AE and applied the Resale Price Method as the most appropriate method ("MAM") by selecting the AE as the tested party.

During the course of the assessment, the TPO changed the MAM from RPM to Transactional Net Margin Method ('TNMM') and computed an adjustment by alleging that the computation mechanism adopted by the taxpayer was complex, lacking information and tedious.

The Dispute Resolution Panel ('DRP') accepted few contentions of the TPO/AO but eventually deleted the entire TP adjustment as the taxpayer could prove before the DRP that the AE sold the goods to unrelated customers at a price equal or less than the price at which those goods were purchased from the Taxpayer (thereby earning no margin)

Aggrieved, the Revenue filed an appeal before the Mumbai ITAT.

Before the tax court (ITAT), the Department Representative argued that the taxpayer did not furnish sufficient information in support of RPM and that the computation mechanism followed by the taxpayer was tedious and complex.

Whereas, the taxpayer argued that the taxpayer was entering into this transaction with its AE since AY 2004-05 and has been consistently adopting RPM as the MAM to benchmark the same. This position was always accepted by the Revenue and accordingly, the transaction was considered to be at an arm's length. In support of this argument, the AR furnished a year wise table (AY 2004-05 – AY 2013-14) and highlighted that in all these years RPM was adopted as the MAM to benchmark the said transaction and this was accepted by the Revenue in all years except AY 2009-10 i.e. the year under dispute. Therefore, the AR argued that in the absence of any change in the fact pattern, the rule of consistency should be applied and even in this year, for benchmarking the said transaction, RPM should be considered as the MAM.

The Tax Court accepted the arguments of the AR and concluded that RPM was accepted by the Revenue as the MAM in the earlier as well as later assessment years and since there was no change in the fact pattern in this year, there is no reason to reject RPM as the MAM in this year. The extract is as follows:

"In the instant case, the Revenue has not brought on record any material fact to show difference in the nature or manner of transactions with AEs. Thus, in the light of facts of the case and the decisions referred above, we find no cogent reason to reject taxpayer's RPM as the most appropriate method to benchmark ALP in the impugned assessment year, when the same was accepted in the earlier and later assessment years by the TPO. The taxpayer succeeds on rule of consistency. The ground no.1 of CO is thus, allowed."

Alcatel Lucent India Ltd – Delhi High Court
Outcome: In favour of the taxpayer
Category: Draft Assessment Order

In the case of the taxpayer, for AY 2017-18, the AO passed an order which was titled "Draft Assessment Order u/s 143(3) r.w.s. 144C of the I.T. Act, 1961". However, in the same order, the AO had levied interest u/s 234A, 234B, 234C and 234D, issued demand notice as well as initiated penalty proceedings u/s 270A of the Income-tax Act, 1961 (the Act).

Aggrieved by the said action, the Taxpayer filed a writ petition before the Delhi High Court ("Delhi HC") wherein the AR of the taxpayer argued that a perusal of the said order would show that this order was actually a Final Assessment Order passed by the AO as the said order was accompanied by an interest computation, demand notice as well as a notice pertaining to initiation of penalty proceedings. Just titling the same as a Draft Assessment Order doesn't make it a Draft Assessment Order. As per the provisions of the Act, the AO was first required to pass a draft order u/s 144C(1) of the Act thereby enabling the Taxpayer to file its objections before the DRP (if aggrieved) within the time period specified under the provisions of the Act. By not doing so, the AO has violated the principles of natural justice.

The Delhi HC accepted the arguments of the Taxpayer and acknowledged the fact that there was a violation of the provisions of the Act as the order which was passed by the AO was actually a Final Order and not a Draft Order.

Accordingly, the Court pronounced that this order shall be treated as a Draft and not a Final Order and hence the notice of demand as well as the penalty proceedings shall stand withdrawn. Further, a time limit of 30 days shall be allowed to the Taxpayer to approach the DRP as per the provisions of the Act. The extract of the pronouncement is as follows:

"Having heard counsel for the parties, the writ petition is disposed of with the following directions:

(i) The assessment order dated 26.03.2021 shall be treated as a draft assessment order.

Contact us: 720, 7th Floor, Ecstasy Business Park, City of Joy, JSD Road, Mulund (W), Mumbai – 400 080.
Tel: 022-25935424; email: info@transprice.in

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(ii) The petitioner will have 30 days' time to file its objections with the DRP. The aforementioned timeframe will commence from the date of the receipt of a copy of this order.

(iii) The notice of demand and the notice for initiation of penalty proceedings shall stand withdrawn.

(iv). In case the order passed by the DRP is adverse to the interest of the petitioner, it will have liberty to assail the same as per law. "

Value Labs LLP – Hyderabad ITAT
Outcome: In favour of the taxpayer
Category: Applicability of TP provisions

The taxpayer, M/s Value Labs LLP transferred its investments in the form of equity shares in Value Labs India, Value Labs, Sweden, VLIT Services BV, Netherlands and Value Labs UK Ltd, to Value Labs Global Solutions Pte. Ltd., Singapore. These shares were transferred by the taxpayer at their face value of 1 Euro/ 1 Sweden Croner/ 1 Pound.

The AO treated the said transfers as international transactions u/s 92B of the Act and thereby made a reference to the TPO for the same.

Thereafter, the TPO passed an order proposing an adjustment of Rs. 1.06 crore which was incorporated by the AO in his draft order and subsequently upheld by the DRP.

Aggrieved, the taxpayer filed an appeal before the Hyderabad Tax Court contending that the said transactions are capital account transactions and are hence not covered under section 92(1) of the Act. Therefore, on the said transactions, TP provisions are not applicable.

The arguments of the taxpayer were accepted by the Tax Court in line with the Bombay High Court decision in the case of PCIT Vs. PMP Auto Components Pvt. Ltd. (2009) 416 ITR 435 (Bom) and Vodafone India Services Limited 368 ITR 001 (Bom) and the Tax Court held that such a capital account transaction does not give rise to any income and hence the provisions of TP shall not apply. The extract is as follows:

"Various judicial precedents and more particularly Bombay high court decision in the case of PCIT Vs. PMP auto Components Pvt. Ltd. (2009) 416 ITR 435 (Bom) and

Vodafone India Services Limited 368 ITR 001 (Bom) hold in view of the CBDT Circular No.2/2015 dt.29.01.2015 that such a capital account transaction does not give rise to income in the revenue count so as to be treated as an international transaction u/s. 92B of the Act. Their Lordships hold that there is no further distinction regarding insourced and outsourced transactions in the instant segment so far as provisions of the Act to this effect are concerned. We adopt the very reasoning mutatis mutandis and delete the impugned ALP adjustment of Rs.1,06,35,050."

TransPrice Comments: Issue of shares and transfer of shares are different international transactions, which seems to have been confused by the Tax Court. On transfer of shares, income in the form of Capital Gains might arise, which makes the applicability of Bombay High Court judgement in Vodafone inapplicable in the case of transfer.

NTT Data Global Delivery Services Private Limited (Formerly known as Keane India Limited) – Bangalore ITAT
Outcome: In favour of the taxpayer
Category: Treatment of forex, risk adjustment

The taxpayer computed its operating margin as well as the operating margins of its comparable companies by treating foreign exchange loss/gain as operating in nature.

The TPO disregarded this treatment of the taxpayer and computed the margin of the taxpayer as well the comparables by treating foreign exchange loss/gain as non-operating and accordingly computed an adjustment.

Aggrieved, the taxpayer filed its objections before the DRP. Further, during the course of the DRP proceedings, the taxpayer also claimed a risk adjustment to the average margin of the comparable companies to adjust the difference in the risk profile of the taxpayer vis-à-vis its comparable companies.

The DRP upheld the contentions of the taxpayer and directed the AO/TPO to treat foreign exchange fluctuation as operating in nature and further directed the TPO to grant a 1% risk adjustment to the average margin of the comparable companies to adjust the risk differential by relying on Intellinet Technologies India Pvt. Ltd. v. ITO (ITA No.1237/Bang/2007) and DCIT v. Hello Soft Pvt. Ltd. (2913) 32 taxmann.com 101 (ITAT, Hyd).

Aggrieved, the Revenue filed an appeal before the Tax Court contending that the DRP was incorrect in treating foreign exchange fluctuation as operating in nature and further, the 1% risk adjustment granted by the DRP was ad-hoc and baseless.

The Tax Court dismissed the appeal of the Revenue on both the issues and upheld the directions of the DRP.

With respect to the issue on forex, the Tax Court relied on the decision of the Bangalore Tribunal in the case of SAP Lab

India Pvt. Ltd. (2010-TII-44-ITAT-BANG-TP) also on taxpayer's own case for assessment year 2007-2008.

With respect to the issue of risk adjustment, the Tax Court relied upon the case laws cited by the DRP.

The relevant extracts are as follows:

Forex

"We have heard rival submissions and perused the material on record. The Bangalore Bench of the Tribunal in the case of SAP Lab India Pvt. Ltd. (2010-TII-44-ITAT-BANG-TP) and also in taxpayer's own case for assessment year 2007-2008 have held that foreign exchange gains / losses are to be considered as operating in nature for determining the margins. In view of Co-ordinate Bench orders of the Tribunal, we uphold the directions of the DRP."

Risk adjustment

"The DRP had restored the issue to TPO and directed him to give 1% adjustment to the average margin for the risk differentials. The DRP in the above said directions, had relied on various orders of the Tribunal. In view of the above orders of the Tribunal (cited by the DRP), we hold that the DRP is justified in the aforesaid directions. It is ordered accordingly."

A.T. Kearney Limited – Delhi ITAT
Outcome: In favour of the taxpayer
Category: Applicability of section 144C of the Act.

This issue pertains to assessment year 2003-04. The original assessment was completed by the AO by passing an order dated 28.03.2006 u/s 143(3).

This order was challenged by the taxpayer before the CIT(A) without any success.

The taxpayer filed an appeal before the Tax Court and the matter was set aside by the Tax Court for denovo consideration by the AO.

Subsequently, giving effect to the Tax Court's order, the AO passed a draft assessment order on 31.12.2010 under section 144C of the Act and later a final assessment assessment order on 19.08.2011 after receiving directions from the DRP on 10.08.2011. This order was challenged by the taxpayer before the Tax Court by filing an additional ground.

The taxpayer vide this ground contended that this order should be treated as null and void as section 144C was introduced in the Income-tax Act. 1961 with effect from 1.04.2009 and was made prospectively applicable from AY 2011-12 onwards. Since, this issue pertains to AY 2003-04, the provisions of section 144C could not be applied to this AY.

In support of its arguments, the taxpayer relied upon the decision of the Madras High Court in the case of Vedanta Limited where the applicability of section 144C was challenged with respect to the assessment proceedings of AY 2007-08 and further on the decision of the Madras High court in the case of M/s Travelport L.P USA.

On the other hand, the DR in his written submissions as well as oral arguments argued for the dismissal of the additional ground filed by the taxpayer and claimed that the order passed by the Madras High Court in the case of Vedanta Limited was bad in law as that order was passed by ignoring previous decisions on this issue (multiple decisions were cited). Further, even the order passed by the Madras High Court in the case of M/s Travelport L.P USA. was bad in law as the same followed the order passed in the case of Vedanta Limited. Further, the DR relied on the decision pronounced by the Delhi High Court in the case of Headstrong Service India Private Limited to support his view.

The Delhi ITAT pronounced its decision in favour of the taxpayer dismissing the arguments raised by the DR and the case laws cited by the DR on the ground that none of the case laws cited were relevant to the issue under consideration and further those decisions were pronounced only on the basis of limited information projected before the Courts. Further, since the final order was passed after the deadline specified under section 153(2A) as applicable to the AY under consideration, the same was barred by limitation.

Further, the applicability of the decision pronounced in the case of Headstrong Service India Private Limited was dismissed on the ground that in the said case, the original assessment was completed by following the procedure u/s 144C but during the remand proceedings, this procedure was not followed and directly a final order was passed u/s 143(3). Therefore, the facts of that case were different as compared to the facts of this case.

The relevant extracts are as follows:

"In light of the above judicial backdrop, the facts of the present case are that the original assessment was framed u/s 143(3) of the Act vide order dated 28.03.2006 and when the dispute travelled up to the Tribunal the Tribunal set aside the matter back to the files of the AO to frame denovo assessment. While giving effect to this order, the AO has erroneously framed a draft assessment order following the provisions of section 144C(1) of the Act which was clearly not applicable on the facts of the case in hand. After receiving the directions of the DRP the final assessment order was framed on 19.08.2011 which is definitely barred by limitation in light of the provisions of section 153(2A) as applicable during the year under consideration and the same reads as under.