TRANSFER PRICING

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Safe Harbour Rules applicability extended to AY 2022-23

CBDT releases Notification No. 66/2022 dated 17th June, 2022 to extend applicability of Safe Harbour Rules under Rule 10TD of Income-tax Rules to AY 2022-23. The CBDT has extended the validity of provisions of Rule 10TD(1) & Rule 10(2A) till Assessment Year 2022-23. Rule 10TD(1) and Rule 10TD(2A) prescribe a list of eligible international transactions where transfer price declared by the assessee shall be required to be accepted by the Income-tax Authorities.

Sub-rule (3A) to Rule 10TD sets time limit for the application of the provision of sub-rules (1) and (2A). It provides that provisions shall apply for the Assessment Year 2017-18 and two Assessment Years immediately following that. In other words, the provisions applied for Assessment Years 2017-18 to 2019-20. Later the Board has inserted a new sub-rule 3B to the Rule 10TD(3B) to extend the applicability of provisions of sub-rules (1) and (2A) till Assessment Year 2021-22.

The Board has now amended Rule 10TD(3B) to further extend the applicability of Safe Harbour Rules until Assessment Year 2022-23.

Virtusa Consulting Services Private Limited [Writ Appeal No. 1903 of 2021 Madras HC]

Virtusa Consulting Services Pvt Ltd ("the assessee") engaged in the business of software development and rendering services to its wholly owned subsidiary outside India, Group entities and also unrelated third party customers. A reference was made to the TPO beyond 21 months provided for completion of assessment u/s.153.

It was held that the reference made to the TPO beyond the period of 21 months is beyond the period of limitation and since such reference to TPO is bad, then all further proceedings, in furtherance of the same are also bad. The HC quashed the assessment order passed by the AO in the case of the assessee for AY 2006-07. Reference was made to Section 92CA, Section 144C and Section 153 (both old and new). The HC observed that "Though, the provision does not state as to when a reference is to be made, a reading of Section 153 would explicit that the reference is to be made during the course of the assessment proceedings before the expiry of the period to pass an assessment order.". Referring to the whole scheme of relevant sections, observes that when the time period of assessment is 21 months from the end of the AY, reading the proviso to mean that a reference can be made after the expiry of the period of limitation to pass assessment order, would make the same obsolete. The HC also observed that the additional period of 12 months to complete assessment would only be available in cases where reference to TPO is made during the course of assessment proceedings.

It was further noted that under the provisions it is required that a "reference" must be made to the TPO and that there is no requirement of "approval" from the Commissioner. Hence, it rejected the argument that concurrence of the Commissioner was received before the expiry of 21 months. It also held that the extended period (of additional 12 months to complete assessment) comes into operation only on a reference and not on concurrence. Separately, it was noted that in the present case, even the extended time limit of 33 months was surpassed by the Revenue.

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Remand to DRP by ITAT also governed by limitation period under Section 153 – Holds Sections 144C and 153 to be mutually-inclusive – Roca Bathroom Products Private Limited [TS-359-HC-2022(MAD)-TP]

Relevant Facts:

- The Hon'ble Tribunal had remanded the matter for fresh adjudication to the DRP / AO.
- No proceedings were initiated by the DRP or AO pursuant to the directions from Hon'ble Tribunal. Only when the Assessee wrote to the income-tax authorities for refund of taxes, notice dated Jan. 2020 were issued by the DRP.
- The Assessee challenged the notice received as barred by limitation under Section 153 of the Act via writ petition before Hon'ble High Court.
- The Revenue Department contented that Section 144C of the Act is a complete code by itself, not governed by the timelines set out in Section 153 of the Act emphasizing on the opening para of Section 144C(13) of the Act.
- Single Judge of the Hon'ble High Court allowing the writ petition held that notices issued by the DRP after a period of four years from the date of order of the Tribunal would be barred by limitation by application of the provisions of Section 153(2A) of the Act.
- Revenue Department preferred an appeal before Divisional Bench.

High Court's Ruling (Division Bench)

Confirming the order of the Single Judge, Divisional Bench of Hon'ble High Court observed as under:

- The provisions of Sections 144C and 153 of the Act are not mutually exclusive, but are rather mutually inclusive. The period of limitation prescribed under Section 153 (2A) or 153 (3) of the Act is applicable, when the matters are remanded back irrespective of whether it is to the Assessing Officer or TPO or the DRP, the duty is on the assessing officer to pass orders.
- Even in case of remand, the TPO or the DRP have to follow the time limits as provided under the Act. The entire proceedings including the hearing and directions have to be issued by the DRP within 9 months as contemplated under Section 144C (12) of the Act,
- Irrespective of whether the DRP concludes the proceedings and issues directions or not, within 9 months, the Assessing officer is to pass orders within the stipulated time,

- In matter involving transfer pricing, upon remand to DRP, the Assessing officer is to pass a denova draft order and the entire proceedings as in the original assessment, would have to be completed within 12 months, as the very purpose of extension is to ensure that orders are passed within the extended period, as otherwise the extension becomes meaningless.
- The outer time limit of 33 months in case of reference to TPO under Section 153 of the Act, would not refer to draft order, but only to final order and hence, the entire proceedings would have to be concluded within the time limits prescribed.
- The non-obstante clause would not exclude the operation of Section 153 of the Act as a whole. It only implies that irrespective of availability of larger time to conclude the proceedings, final orders are to be passed within one month in line with the scheme of the Act.
- When no period of limitation is prescribed, orders are to be passed within a reasonable time, which in any case cannot be beyond 3 years. However, when the statute prescribes a particular period within which orders are to be passed, then such period, irrespective of whether it is short or long, shall be applicable.

Rejects disallowance u/s 10B(7) r.w.s. 80IA(10) wherein the AO alleged excess deduction under Section 10A of the Act based on the profit margin of comparable companies vis-à-vis the assessee's actual profit margin from such services - Halliburton Technology Industries Pvt Ltd [TS-357-ITAT-2022(PUN)-TP]

Facts:

- The Assessee provided IT enabled services to its AEs and registered as a hundred percent export oriented undertaking with the SEEPZ special economic zone. Operating profit from the rendition of the services was claimed as deductible under Section 10B of the Act by the Assessee.
- The AO observed that for the year under the consideration, the Assessee has earned more than ordinary profits as the operating margin of the Assessee was 22.38 percent and the operating margins of the comparable is 13.08 percent.
- The AO then held that where taxpayer has such close connection 'with any other person' and where it earns abnormal profits from the transactions with such other person, the existence of 'arrangement' between the parties to the transactions can be safely inferred.
- The AO accordingly made an addition by disallowing excess deduction under Section 10B(7) of the Act i.e. profit declared by the Assessee minus profit considering margin of comparable companies.
- CIT(A) deleted such addition. Aggrieved, Revenue filed an appeal before Hon'ble Tribunal.

Tribunal's Ruling

Upholding order of CIT(A) and relying on various judicial precedence, Hon'ble Tribunal upheld as under:

- The AO has not brought out why the profits of the Assessee will not be considered as ordinary profits in the course of business.
- The AO has specifically not demonstrated any proof of arrangement for disallowance under the provisions of Section 10B(7) r.w.s. 80-IA(10) of the Act.

  Hon'ble Tribunal inter-alia relies on Hon'ble High Court decision in case of Schmetz India Pvt. Ltd. Income- Tax Appeal No. 1382 of 2013 (affirmed by Hon'ble Supreme Court), wherein it was held that extra ordinary profits earned by the taxpayer could not lead to the conclusion that there was an arrangement between taxpayer and its associated enterprises.

  Hon'ble Tribunal further relies on co-ordinate bench ruling in Honeywell Automation India Limited and Another Vs. DCIT and Another (2021) 62 CCH 0177 (Pune-Trib), wherein case of excessive deduction made by the AO under Section10A(7) read with section 80IA(10) of the Act, similar to the one under consideration, was disapproved. In case of Honeywell Automation India Limited (supra), Hon'ble Tribunal had held that the expression "arranged" referred to in Section 10A(7) r.w.s. 80-IA(10) of the Act should not be understood in its plain language but the same should be understood in the context in which it is placed in the Section. Existence of a mere agreement to do business was not enough to fulfill the requirement of Section 10A(7) r.w.s. 80-IA(10) of the Act in the context of the words "the course of business between them is so arranged". The arrangement had to be one which was prefaced by an intention to abuse the tax concessions, as per the intendment of the legislature.

Directs to treat amortization of goodwill as non-operating for TP purpose - TE Connectivity Services India Pvt Ltd [TS-330-ITAT-2022(Bang)-TP]

Relevant Facts:

- The Assessee recorded a Goodwill pursuant to the acquisition of the 'Shared Services Business' on a slump sale basis.
- The TPO recomputed the margin of the Assessee considering Goodwill as operating in nature.

Tribunal's Ruling

- Relying coordinate bench decision in *Continental Automotive Components (India) Pvt. Ltd. [[IT(TP)A No.713/Bang/2017] and ST-Ericsson India Pvt. Ltd. v. DCIT [IT(TP)A No.609 & 168/Del/2015)]*, upheld that amortization of goodwill is an extra-ordinary item and is not pertaining to the regular operation of the Assessee, and hence non-operating in nature.
- Appreciates Assessee's argument that goodwill was a cost associated with the purchase of the business and it is not a tool deployed in business. The same can be distinguished from assets such as plant and machinery, office equipment, computers, which are purchased and used for undertaking normal day-to-day operations.

Allows custom-duty adjustment plea, remits calculation - India Kawasaki Motors Private Limited [TS-302-ITAT-2022(PUN)-TP]

Tribunal's Ruling

- Hon'ble Tribunal noted that the Assessee had 100 percent imported the traded goods, which resulted in higher incidence of customs duty on traded goods. This increased the cost of the traded goods directly affected the gross profit margin, when compared to the comparables. Accordingly, there is merit in the contention of the Assessee that the suitable adjustments should be made to iron out the differences of profit between the profit of tested company and the comparables.
- However, relies on *ACIT vs. Nord Drive Systems Pvt. Ltd. [ITA No.825/PUN/2016]* (being the latest decision) wherein it was held that the adjustments is required to be made only in the profit margin of the comparables. Accordingly, directs the AO / TPO to make adjustments to the margins earned by comparables instead of the margins of the Assessee.