

## TRANSFER PRICING

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### **Organon (India) Pvt Ltd [TS-342-HC-2023(CAL)-TP]**

Calcutta HC dismisses Revenue's appeal against ITAT's order deleting AMP adjustment for AYs 2012-13 and 2013-14; HC notes that ITAT dismissed Revenue's plea that assessee was only a distributor and not a manufacturer; ITAT had found that the assessee outsourced its entire production requirements to toll manufacturers/ contract manufacturers on a license basis; ITAT had also found, on examining assessee's financials, that the products manufactured are either of its own or through contract manufacturers and they are subjected to levy of Central Excise Duty which has been collected from the assessee; HC holds, "in the absence of any material produced before this Court or before the Tribunal to dislodge this factual finding, the order of the Tribunal cannot be interfered nor can it be termed as perverse"; HC also holds that ITAT rightly held that the usage of the word "Organon" as the name of the assessee in India is immaterial and what would be material is the products manufactured by the assessee and not the company which manufactures; HC upholds ITAT's finding that mere usage of foreign word does not automatically make it fall within the ambit of an international transaction; ITAT had also noted that Revenue ignored the bifurcation of total expenditure towards AMP and selling expenditure (made by identifying at the time of incurrence itself, whether the said expenditure constitutes AMP expenditure or selling expenditure); Accordingly, opining that ITAT was convinced with assessee's case and granted relief, HC holds that "in the absence of any perversity in the order..., we find no grounds to interfere with the same" and thereby dismisses Revenue's appeal.:HC CAL

### **ADM Agro Industries Kota & Akola P. Ltd [TS-355-ITAT-2023(DEL)-TP]**

Delhi ITAT applies PLI of operating profit to value added cost, excludes cost of goods for determining ALP qua international transactions relating to merchanting trades segment; For AY 2018-19, TPO accepted purchases made by assessee in the trading segment to be at ALP whereas for merchanting trades segment, TPO accepted assessee's adoption of TNMM as well as comparables from business auxiliary services; However, TPO/DRP rejected assessee's PLI of OP/VAC (Berry Ratio) by stating that since PLI of comparables is OP/OC, assessee cannot have a different PLI and that it has to be OP/OC; States that "where operating expense is considered as a relevant base, there would be no difficulty in using berry ratio as PLI in terms of Rule 10(B)(1)(e)"; Refers to jurisdictional HC ruling in Sumitomo Corporation India Pvt. Ltd wherein it was held that Berry Ratio is effectively applied only in case of stripped down distributors who have no financial exposure and risk in respect of the goods distributed by them; In context of given case, ITAT observes that the only variation made by TPO to assessee's PLI is to add the cost of goods to the denominator; However, notes the fact that "operating cost of the comparables are not inclusive of cost of goods, as they are business auxiliary service providers, hence, they do not have any cost of goods"; Explains that since assessee is found to be functionally comparable to the business auxiliary service providers, it establishes that assessee has undertaken limited functions and risk in the concerned segment and earns a fixed profit margin; Thus, ITAT holds that the cost of goods cannot be included in the denominator of PLI; Accordingly, ITAT directs AO to compute ALP by applying PLI of operating profit to value added cost, excluding the cost of goods; Additionally, ITAT rejects Revenue's plea that assessee is involved only in one segment, i.e., trading segment and not merchanting trades segment by inter alia noting that in the TP study report, assessee had furnished segmental information regarding both the segments which has been accepted by TPO; Notes that neither TPO nor DRP have made any adverse comment regarding the merchanting trades segment; Lastly, absent any allegation either by RBI or any other regulatory authority regarding merchanting trades segment of the assessee, ITAT opines that Revenue "cannot give a new dimension to the entire issue by making allegations which are not borne out on record"; Thus, directs the AO to compute ALP by applying PLI of operating profit to value added cost by excluding the cost of goods.:ITAT DEL

- **The TPO could not have substituted the actual figures for projected figures in DCF valuation for the purpose of determining the value of shares– TPG Growth II Markets Pte Ltd [TS-346-ITAT-2023(Mum)-TP]**

**Facts:**

- The Assessee, a foreign company had undertaken transactions in respect of purchase and Sale of Indian entities shares from / to the AE.
- The TPO proposed an adjustment on these international transactions by alleging over payment and under receipt of consideration.
- In doing so, the TPO rejected the valuation report from independent valuer furnished by the Assessee. Instead of the projected figured, the TPO used the actual financial results for determining the value of shares using Discounted Cash Flow Method (DCF Method).

#### **Hon'ble Tribunal**

Rejecting the approach of the TPO, Hon'ble Tribunal observed as under:

- The TPO could not have substituted the actual figures for projected figures in DCF valuation for the purpose of determining the value of shares.
  - BEPS: Action 8 dealing with OECD Guidance for Tax Administrations on the Application of the Approach to HTVI clearly provides that where the actual cash flows are significantly higher than the projected cash flows, there is a presumption that projected cash flows should have been higher requiring scrutiny for the probability weighing of such outcome. However, the Guidance goes on to provide that it would be incorrect to base revised valuation on actual cash flows without taking into account the said probability. We note that no such scrutiny or probability-weighting was done by the TPO.
  - Rule 10B(5) also does not support the case of the Revenue. The proviso to Rule 10B(5) deals with the availability of data of current year subsequent to the determination of arm's length price and permits use of the same for determination of ALP during assessment proceedings even though the data was not available at the time of furnishing of the return of income. Thus, Rule 10(5) does not provide for or deal with the data pertaining to future/subsequent years. The data used by the TPO pertains to years subsequent to the current year.
- **Invalid Transfer Pricing Order cannot be a basis for reopening of the Assessment us 147 / 148 - Kimberly Clark Lever Private Limited [TS-364-HC-2023(BOM)-TP]**

#### **Facts:**

- The AO made a reference to the TPO on 26 October 2009. The TPO passed an order under Section 92CA(3) on 29 October 2010.
- The AO thereafter initiated reassessment proceedings under Section 147/ 148 of the Act. The AO's the reasons to believe that the income had escaped assessment was the transfer pricing order.
- The reassessment proceedings were quashed by the Hon'ble Tribunal. Department preferred an appeal to High Court

#### **Hon'ble High Court:**

Upholding Tribunal's Order and dismissing Revenue's appeal, Hon'ble High Court noted as under:

- It is judicially well settled that the belief of the Assessing Officer that there has been escapement of income must be based on some material on record. There must be some material on record to enable the Assessing Officer to entertain a belief that certain income chargeable to tax has escaped assessment for the relevant Assessment Year. In this case, the only material relied upon is the order of the TPO.
- An Assessing Officer can make reference to the TPO under Section 92CA of the Act only after selecting the case for scrutiny assessment. The instructions of CBDT is also a pointer to the legislative import that the reference to the TPO for determining the arm's length price in relation to an international transaction is envisaged only in the course of the assessment proceedings, which is the only process known to the Act, whereby the assessment of total income is done
- Admittedly in this case, no notice under Section 143(2) of the Act was issued before making the said reference to the TPO. Accordingly, the subsequent order passed by the TPO determining the assessment to the international transaction was a nullity in law and void ab initio.
- The Assessing Officer could not have relied upon an order of the TPO which is a nullity to form a belief that certain income chargeable to tax has escaped the assessment for the relevant Assessment Year.

- **Accepts corporate guarantee benchmarking based on yield approach @ 0.35% - Macrotech Developers Limited [TS-237-ITAT-2023(Mum)-TP]**

Dealing with the issue of corporate guarantee, Hon'ble Tribunal observed as under:

- The argument of Corporate Guarantee being not an international Transaction is no more valid in view of the decision of Honorable Madras High court in case of PCIT V Redington [India] Limited [2021] 430 ITR 298 (Mad).
- Further, the same is not a shareholder activity as (a) The relationship between the Assessee and the company in whose favor of the guarantee is given is of fellow subsidiary and (b) It is not shown that Guarantee is given for supporting continuous cash flow of subsidiary. It is also not for control of capital structure and not solely for ownership purposes.
- When Guarantee is covered in clause 92B (2)(1)© specifically and it is a capital financing transaction specifically included there in, it is unnecessary to stretch it to bring in to clause (d) of ' Provision of services'.
- Regarding DRP's determination of 0.5% as the arm's length rate based on Bombay High Court decision in CIT vs. Everest Kanto Cylinders Ltd. (2015) 378 ITR 57 (Bom.), observes that DRP neither cared to look at the methodology adopted nor consider the economic aspect of the transaction; States that judicial decisions should be applied if they pertain to similar AY, showing similar economic conditions, adopting proper benchmarking methodology.
- ITAT upholds alternative benchmarking of Assessee, imputing commission @ 0.35%, based on yield approach, observing that the same "is derived after the proper credit rating of associated enterprises, on DealsScan database, determining the appropriate interest saving and thereafter attributing it between the two parties. It is also to be noted that the arm's-length price of the guarantee commission by yield method would be the maximum rate"

- **Special Bench on determination of arm's length price for 'bundle of sports rights– Star India Private Limited [TS-329-ITAT-2023(Mum)-TP]**

Hon'ble Tribunal while dealing with the issue of TP adjustment of acquiring Bundle of Sport Broadcasting Rights in case of Star India Private Limited, answered the following questions in its Special Bench Order:

**1. Can Assessee resile from the most appropriate method adopted in its Transfer pricing study report?**

Special Bench held that since the ultimate aim of the transfer pricing exercise is to determine an accurate value of the arms' length price for the purpose of taxation/and therefore the Assessee would not be barred from adopting a different method, from that adopted by the Assessee in the transfer pricing report, if the latter is not found to be the Most Appropriate

**2. Which is the most appropriate method in the transaction under consideration?**

The Vice President in minority ruling holds CUP as MAM over 'Other method' by opining that *"if the CUP method is pitted against the 'other method', then there is no prize for guessing that it is the former which will prevail over the latter provided the comparable uncontrolled data required for it is available. The ensuing discussion will demonstrate that the data required for the application of the CUP exists and is on record"*

The Accountant Member rejects CUP opining absent comparable uncontrolled transaction prices and 'other method' being more appropriate to the impugned 'unique intangible asset'. The Judicial Member agrees with the Accountant Member and finds 'Other Method' appropriate over CUP.

**3. Whether the ALP determined by the Assessee is correct?**

The Vice President upholds international transaction of purchase of broadcasting rights to be at ALP under CUP as held by Assessee, notes that Assessee purchased several broadcasting rights in a bundled manner and had no choice of refusing a particular right from the bundle offered. Accordingly, deletes said TP adjustment made by AO on the basis of deficiencies found by it in the valuation report submitted by the Assessee.

The members in majority direct for placing the matter before the Division Bench for disposal having regard to the decision of the Special Bench on adopting 'Other Method' as most appropriate method noting that the same was not at all argued before it.