

IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH 'I-2', NEW DELHI

Before Sh. C.M.Garg, JM AND Sh. O.P.Kant, AM

ITA No.4680/Del./2010 : Asstt. Year : 2006-07

Haier Appliances India Ltd., B-1/A-14, Mohan Co-op Indl Estate, New Delhi PAN:AABCH3162L	Vs	DCIT, OSD, CIT-IV, New Delhi
(APPELLANT)		(RESPONDENT)

ITA No.5235/Del./2011 : Asstt. Year : 2007-08

Haier Appliances India Ltd., B-1/A-14, Mohan Co-op Indl Estate, New Delhi PAN:AABCH3162L	Vs	ACIT, Circle-12(1) New Delhi
(APPELLANT)		(RESPONDENT)

ITA No.4404/Del./2012 : Asstt. Year : 2008-09

Haier Appliances India Ltd., B-1/A-14, Mohan Co-op Indl Estate, New Delhi PAN:AABCH3162L	Vs	DCIT, Circle-10(1) New Delhi
(APPELLANT)		(RESPONDENT)

Appellant by : Sh. Neeraj Jain, Adv.
: Sh. Abhishek Agarwal, CA
Respondent by : Ms. Y Kakkar, Sr. DR

Date of Hearing : 09.09.2015

Date of Pronouncement :28.10.2015

ORDER

PER O.P.Kant, A.M.

These appeals arise from the common judgement dated 16.03.2015 of the Hon'ble Delhi High Court in following appeals of the assessee, along with appeals of other assesses and cross appeals

of the Revenue filed u/s 260A of the Income Tax-act, 1961 (in short 'Act') led by the case of Sony Ericsson Mobile Communications India Pvt. Ltd. (now known as Sony India Limited) reported in (2015) 374 ITR 118 (Delhi):-

Assessment Year	ITA No.	Assessee	Cross appeal by Revenue
2006-07	100 of 2014	Haier Appliances Pvt. Ltd.	621 of 2014
2007-08	101 of 2014	Haier Appliances Pvt. Ltd.	622 of 2014
2008-09	99 of 2014	Haier Appliances Pvt. Ltd.	642 of 2014

2. As common issue of determination of Arms Length Price (in short 'ALP') of international transaction of advertising, marketing and promotion (in short 'AMP') expenses is involved in the appeals before us and the facts and circumstances also being similar, the appeal in ITA No.4680/Del/2010 for Assessment Years 2006-07 is decided first and other appeals are decided accordingly.

3. The facts in brief are that the assessee company is a wholly owned subsidiary company of 'Haier Electrical and Appliances Corporation Ltd.', China and is engaged in the business of distribution of consumer durable products, for example Air Conditioner, Washing machine, refrigerator, television etc., purchased from foreign associated enterprise (in short 'AE'). However, the intangible rights contained in brand name or trademark/ trade name in respect of goods so purchased and distributed were

owned by the foreign AE only. In the previous year corresponding to the relevant assessment year, the assessee reported following international transaction with the AE in the transfer pricing audit report submitted to the Assessing Officer(in short 'AO'):

(a) Purchase of finished products from the foreign AE i.e. HAH (HK) Company Ltd., Hong Kong, amounting to Rs.41.66 crores for the purpose of distribution/ resale in India.

(b) Purchase of capital items of Rs.1,95,97,166/-.

4. The AO made a reference to the transfer pricing Officer (in short 'TPO') u/s 92CA (1) of the Act. The TPO accepted the arms length price reported by the assessee in respect of international transactions, however, the TPO observed that from the profit and loss account that the assessee had incurred expenses of Rs.74,04,23,369/- on AMP, which also included selling expenses like rebate and discounts given to the dealers . According to the TPO, the substantial part of AMP expenses incurred by the assessee were towards promotion of brand/ trade name/ trade mark etc. owned by the AE, whereas the AE only reimbursed Rs.13,11,47,568/- as capital grant towards such expenses. The TPO held that incurring expenses on advertising, marketing, and promotion (AMP) on behalf of the AE was an international transaction and further, applying the 'bright line test', he proposed to segregate routine expenses incurred by the assessee on AMP and non routine expenses incurred on AMP by the

assessee, which goes to create/enhance the value of intangible in the nature on brand name, trade mark or trade name etc owned by the AE. The TPO took following two comparables and worked out arithmetic mean of their percentage of AMP expense including rebate and discounts given to the dealers to the total expenses, at 1.4095% as follows:

S. No.	Name of the comparables companies	Sale (Rs.)	AMP	Percentage of Adv. Exp of sales.
1.	Goa Electronics Ltd.	231,731,837	139,642	0.060
2.	Vivek Ltd.	2,988,076,269	82,467,269	2.759
	Arithmetic Mean			1.4095

5. The percentage of 1.4095 was held as bright line and AMP expenses in excess of the ratio of the percentage were held as non routine and abnormal. The TPO, then applying the percentage of 1.4095 over the total expenses incurred in profit and loss account, computed the adjustment of Rs.57,24,40,796 on account of arm's length price of international transaction of AMP expenses as follows:-

<i>Total Revenue of the assessee</i>	<i>Rs.261,33,40,369/-</i>
<i>Arm's Length % of AMP expenditure</i>	<i>1.4095%</i>
<i>Arm's Length AMP expenditure</i>	<i>Rs. 3,68,35,032/-</i>
<i>Expenditure incurred by the assessee on AMP</i>	<i>Rs.74,04,23,369/-</i>
<i>Expenditure incurred for developing the Intangibles</i>	<i>Rs.74,04,23,396 – Rs.3,68,35,032</i>
<i>Arm's length value of the Capital Grant</i>	<i>Rs.70,35,88,364/-</i>
<i>Amount of Capital Grant received by the assessee</i>	<i>Rs. 13,11,47,568/-</i>
<i>Difference</i>	<i>Rs.57,24,40,796/-</i>

% of difference with value at which international Transaction has taken place 436.48%

6. The assessee challenged the adjustment of Rs. 57,24,40,796 made by the AO/TPO before the Dispute Resolution Panel (in short ‘DRP’), but could not succeed and therefore filed the present appeal before the Income-Tax Appellate Tribunal (in short ‘ITAT’) against the order passed by the AO in conformity with the order of DRP, challenging the action of the AO/TPO/DRP in holding the AMP expenses as international transaction as well as the adjustment made in this regard. The ITAT after having heard both the parties, following the decision of the Special Bench of the ITAT in the case of LG Electronics India P Ltd. versus Asst. CIT (2013) 22 ITR (Trib) 1 (Delhi)(SB), held that the incurring AMP expenses of non routine nature on behalf of the AE was an international transaction. The ITAT further approved the application of bright line test for working out the non routine AMP expenses and held that ALP of AMP expenses should be determined on cost plus method, but excluded the selling expenses like rebate, discount etc from the ambit of AMP expenses for determining international transaction and remitted the matter back to the file of the AO/TPO with the following directions:-

“i) Expenditure in connection with the sales as mentioned above cannot be brought within the ambit of advertisement, marketing and promotions expense for determining the cost/

value of the international transactions. However, the TPO shall examine the veracity of description and quantification of the amount of selling expenses and accordingly, allow the assessee's claim.

ii) After deducting the selling price from the AMP expenses as mentioned above, the TPO shall decide the issue of AMP expenses by applying the proper comparables after hearing the assessee and keeping in view the Special Bench directions in this behalf.”

7. Aggrieved with the order of the ITAT, both the assessee as well as the Revenue, filed appeal u/s 260A of the Act before the Hon'ble jurisdictional High Court of Delhi bearing ITA Nos.100 of 2014 and ITA No.621 of 2014 respectively. These appeals were heard by their lordship together with the appeals of the other assessee and cross appeals of the Revenue, led by the case of Sony Ericsson Mobile Communication India Pvt. Ltd., where the common substantial questions of law preferred by the assessee's and the Revenue in their appeals/ cross appeals were as under:-

Assessee's Appeals

“1. Whether the additions suggested by the Transfer Pricing Officer on account of Advertising/Marketing and Promotion Expenses (AMP Expenses' for short) was beyond jurisdiction and bad in law as no specific reference was made by the Assessing Officer, having regard to retrospective amendment to Section 92CA of the Income Tax Act, 1961 by Finance Act, 2012.

2. Whether AMP Expenses incurred by the assessee in India can be treated and categorized as an international transaction under Section 92B of the Income Tax Act, 1961.

3. *Whether under Chapter X of the Income Tax Act, 1961, a transfer pricing adjustment can be made by the Transfer Pricing Officer/ Assessing Officer in respect of expenditure treated as AMP Expenses and if so in which circumstances?*

4. *If answer to question Nos.2 and 3 is in favour of the Revenue, whether the Income Tax Appellate Tribunal was right in holding that transfer pricing adjustment in respect of AMP Expenses should be computed by applying Cost Plus Method.*

5. *Whether the Income Tax Appellate Tribunal was right in directing that fresh bench marking/comparability analysis should be undertaken by the Transfer Pricing Officer by applying the parameters specified in paragraph 17.4 of the order dated 23.01.2013 passed by the Special Bench in the case of LG Electronics India (P) Ltd. ?”*

Revenue's Appeals

“1. Whether the Income Tax Appellate Tribunal was right in distinguishing and directing that selling expenses in the nature of trade/volume discounts, rebates and commission paid to retailers/dealers etc. cannot be included in the AMP Expenses?”

8. Their lordship decided all the appeals referred above led by the case of Sony Erricsson Mobile Communication India Pvt. Ltd in a common judgement dated 16.03.2015 reported in 374 ITR 118 including the appeals of the assessee and Revenue referred in para -1 of this order. Their lordship has propounded legal findings on the relevant issues in heading ‘D’ to ‘P’ of the judgment and summed up the view taken on the substantial questions of law in their judgment as under:

“Answer to Substantial Questions of Law

Para 194. In view of the aforesaid discussion, substantial questions of law in the appeals filed by the assessee are answered as under:

"Q.1. Whether the additions suggested by the Transfer Pricing Officer on account of Advertising/Marketing and Promotion Expenses ('AMP Expenses' for short) was beyond jurisdiction and bad in law as no specific reference was made by the Assessing Officer, having regard to retrospective amendment to Section 92CA of the Income Tax Act, 1961 by Finance Act, 2012."

In terms of and subject to discussion under the heading C, paragraph Nos.41 to 50, the substantial question of law No.1 is answered in favour of the Revenue and against the assessee.

"Q.2. Whether AMP Expenses incurred by the assessee in India can be treated and categorized as an international transaction under Section 92B of the Income Tax Act, 1961."

In terms of and subject to discussion under the heading C, paragraph Nos.51 to 57, the 'substantial question of law No.2 is answered in favour of the Revenue and against the assessee.

"Q.3. Whether under Chapter X of the Income Tax Act, 1961, a transfer pricing adjustment can be made by the Transfer Pricing Officer/ Assessing Officer in respect of expenditure treated as AMP Expenses and if so in which circumstances?"

Q.4. If answer to question Nos.2 and 3 is in favour of the Revenue, whether the Income Tax Appellate

Tribunal was right in holding that transfer pricing adjustment in respect of AMP Expenses should be computed by applying Cost Plus Method.

Q.5. Whether the Income Tax Appellate Tribunal was right in directing that fresh bench marking/comparability analysis should be undertaken by the Transfer Pricing Officer by applying the parameters specified in paragraph 17.4 of the order dated 23.01.2013 passed by the Special Bench in the case of LG Electronics India (P) Ltd.?"

In terms of and subject to discussion under the headings D to P, we hold that the legal ratio accepted and applied by the Tribunal relying upon the majority decision in L.G. Electronics India Pvt. Ltd (supra) is erroneous and unacceptable. For reasons set out above, we have passed an order of remand to the Tribunal to examine and ascertain facts and apply the ratio enunciated in this decision. For the purpose of clarity, we would like to enlist our findings:-

- (i) In case of a distributor and marketing AE, the first step in transfer pricing is to ascertain and conduct detailed functional analysis, which would include AMP function/expenses.*
- (ii) The second step mandates ascertainment of comparables or comparable analysis. This would have reference to the method adopted which matches the functions and obligations performed by the tested party including AMP expenses.*
- (iii) A comparable is acceptable, if based upon comparison of conditions a controlled transaction is similar with the conditions in the transactions between independent enterprises. In other words, the economically relevant characteristics of the two transactions being compared*

must be sufficiently comparable. This entails and implies that difference, if any, between controlled and uncontrolled transaction, should not materially affect the conditions being examined given the methodology being adopted for determining the price or the margin. When this is not possible, it should be ascertained whether reasonably accurate adjustments can be made to eliminate the effect of such differences on the price or margin. Thus, identification of the potential comparables is the key to the transfer pricing analysis. As a sequitur, it follows that the choice of the most appropriate method would be dependent upon availability of potential comparable keeping in mind the comparability analysis including befitting adjustments which may be required. As the degree of the comparability increases, extent of potential differences which would render the analysis inaccurate necessarily decreases.

- (iv) The assessed, i.e. the domestic AE must be compensated for the AMP expenses by the foreign AE. Such compensation may be included or subsumed in low purchase price or by not charging or charging lower royalty. Direct compensation can also be paid. The method selected and comparability analysis should be appropriated and reliable so as to include the AMP functions and costs.*
- (v) Where the Assessing Officer TPO accepts the comparables adopted by the assessed, with or without making adjustments, as a bundled transaction, it would be illogical and improper to treat AMP expenses as a separate international transaction, for the simple reason that if the functions performed by the tested parties and the comparables match, with or without adjustments, AMP expenses are duly accounted for. It would be incongruous to accept the comparables and*

determine or accept the transfer price and still segregate AMP expenses as an international transaction.

- (vi) The Assessing Officer/TPO can reject a method selected by the assessed for several reasons including want of reliability in the factual matrix or lack/ non-availability of comparables. (see Section 92C(3) of the Act).*
- (vii) When the Assessing Officer/TPO rejects the method adopted by the assessed, he is entitled to select the most appropriate method, and undertake comparability analysis. Selection of the method and comparables should be as per the command and directive of the Act and Rules and justified by giving reasons.*
- (viii) Distribution and marketing are inter-connected and intertwined functions. Bunching of inter-connected and continuous transactions is permissible, provided the said transactions can be evaluated and adequately compared on aggregate basis. This would depend on the method adopted and comparability analysis and the most reliable means of determining arm's length price.*
- (ix) To assert and profess that brand building as equivalent or substantial attribute of advertisement and sale promotion would be largely incorrect. It represents a coordinated synergetic impact created by assortment largely representing reputation and quality. "Brand" has reference to a name, trademark or trade name and like 'goodwill' is a value of attraction to customers arising from name and a reputation for skill, integrity, efficient business management or efficient service. Brand creation and value, therefore, depends upon a great number of facts relevant for a particular business. It reflects the reputation which the proprietor of the brand has gathered over a passage or period of time in the form of widespread popularity and universal approval and acceptance in the eyes of the customer.*

Brand value depends upon the nature and quality of goods and services sold or dealt with. Quality control being the most important element, which can mar or enhance the value.

- (x) *Parameters specified in paragraph 17.4 of the order dated 23rd January, 2013 in the case of L.G. Electronics India Pvt. Ltd (supra) are not binding on the assessed or the Revenue. The 'bright line test' has no statutory mandate and a broad-brush approach is not mandated or prescribed. We disagree with the Revenue and do not accept the overbearing and orotund submission that the exercise to separate 'routine' and 'non-routine' AMP or brand building exercise by applying 'bright line test' of non-comparables should be sanctioned and in all cases, costs or compensation paid for AMP expenses would be 'NIL', or at best would mean the amount or compensation expressly paid for AMP expenses. It would be conspicuously wrong and incorrect to treat the segregated transactional value as 'NIL' when in fact the two AEs had treated the international transactions as a package or a single one and contribution is attributed to the aggregate package. Unhesitatingly, we add that in a specific case this criteria and even zero attribution could be possible, but facts should so reveal and require. To this extent, we would disagree with the majority decision in L.G. Electronics India Pvt. Ltd. (supra). This would be necessary when the arm's length price of the controlled transaction cannot be adequately or reliably determined without segmentation of AMP expenses.*
- (xi) *The Assessing Officer/TPO for good and sufficient reasons can de-bundle interconnected transactions, I.e. segregate distribution, marketing or AMP transactions. This may be necessary when bundled transactions cannot be adequately compared on aggregate basis.*

- (xii) *When segmentation or segregation of a bundled transaction is required, the question of set off and apportionment must be examined realistically and with a pragmatic approach. Transfer pricing is an income allocating exercise to prevent artificial shifting of net incomes of controlled taxpayers and to place them on parity with uncontrolled, unrelated taxpayers. The exercise undertaken should not result in over or double taxation. Thus, the Assessing Officer/TPO can segregate AMP expenses as an independent international transaction, but only after elucidating grounds and reasons for not accepting the bunching adopted by the assessed, and examining and giving benefit of set off. Section 92(3) does not bar or prohibit set off.*
- (xiii) *CP Method is a recognized and accepted method under Indian transfer pricing regulation. It can be applied by the Assessing Officer/TPO in case AMP expenses are treated as a separate international transaction, provided CP Method is the most appropriate and reliable method. Adoption of CP Method and computation of cost and gross profit margin comparable must be justified.*
- (xiv) *The object and purpose of Transfer Pricing adjustment is to ensure that the controlled taxpayers are given tax parity with uncontrolled taxpayers by determining their true taxable income. Costs or expenses incurred for services provided or in respect of property transferred, when made subject matter of arm's length price by applying CP Method, cannot be again factored or included as a part of inter-connected international transaction and subjected to arm's length pricing.*

Para 195. The above noted pointers have to be read along with our discussion under the headings D to P. In case of

any doubt, debate or purported conflict, it would be preferable to rely upon detailed elucidation made under the headings, D to P.

Para 196. Common questions raised by the Revenue in their appeals:-

“1. Whether the Income Tax Appellate Tribunal was right in distinguishing and directing that selling expenses in the nature of trade/volume discounts, rebates and commission paid to retailers/dealers etc. cannot be included in the AMP Expenses?”

In terms of and subject to our discussion under the headings O and P, the substantial question of law has to be answered against the Revenue and in favour of the assessee.

9. Further, in para 193 of the consolidated judgment, their lordship has led as under:-

“Para 193. We would not like to go into several factual aspects for the first time, for the factual matrix has not been examined and ascertained by the Tribunal. Moreover, in terms with our legal finding, factual findings will have to be examined. An order of remand for de novo consideration to the Tribunal would be appropriate because the legal standards or ratio accepted and applied by the Tribunal was erroneous. On the basis of the legal ratio expounded in this decision, facts have to be ascertained and applied. If required and necessary, the assessed and the Revenue should be asked to furnish details or tables. The Tribunal, at the first instance, would try and dispose of the appeals, rather than passing an order of remand to the Assessing Officer/TPO. The

endeavor should be to ascertain and satisfy whether the gross/net profit margin would duly account for AMP expenses. When figures and calculations as per the TNMM or RP Method adopted and applied show that the net/gross margins are adequate and acceptable, the appeal of the assessed should be accepted. Where there is a doubt or the other view is plausible, an order of remand for re-examination by the Assessing Officer/TPO would be justified. A practical approach is required and the tribunal has sufficient discretion and flexibility to reach a fair and just conclusion on the arm 's length price."

10. In above background, the appeal of the assessee and cross appeal of the Revenue have been re-fixed by the registry and heard by us.

11. At the time of hearing, the learned Authorised Representative of the assessee made a written submission, the relevant paras of which are reproduced as under:-

"In the transfer pricing document, on the basis of the functional analysis, the appellant was characterized as a reseller or distributor of white goods, performing routine selling & distribution and other management functions, and assuming normal risk associated with carrying on of its business. The appellant performs similar functions, assumes similar risks and employs similar assets, while distributing finished products imported from the associated enterprise and also with respect to the finished goods purchased from the third parties. Further, the transaction of purchase of finished goods from the third parties (for resale in the domestic market) satisfy the comparability criteria as laid down in Sub-rule (2) of Rule 10B of the Rules, in as much as apart from the product comparability they satisfy

functional comparability and the two transactions are undertaken under similar market and economic conditions.

Accordingly, the appellant, in its transfer pricing document, compared the gross profit margin and operating profit margin from resale of goods purchased from associated enterprises and unrelated third parties, as under:

	AE's Transactions	Non AE's Transactions	Total
Income	INR		INR
Sales			
Gross Sales	632,003,433	1,837,767,613	2,469,771,046
Sales Tax	65,302,343	189,889,051	255,191,394
Net Sales	566,701,089	1,647,878,563	2,214,579,652
Add:			
Closing Stock	88,318,799	175,248,536	263,567,335
Goods-in-transit	138,272,964	22,234,962	160,507,926
Less:			
Expenses			
Purchases & Direct Expenses	419,932,495	1,218,273,010	1,638,205,505
Other Clearing Expenses	14,631,339	26,934,517	41,565,856
Opening Stock	74,927,420	74,247,258	149,174,678
Goods in Transit	76,316,874	20,918,535	97,235,409
Gross Profit	207,484,725	504,988,741	712,473,465
Add:			
Other Income	1,242,068	3,611,740	4,853,808
Less:			
Indirect expenses			
Rebate & Discount	122,482,449	356,159,898	478,642,347
Personnel Cost	20,664,078	60,087,921	80,751,999
Selling & Distribution Cost	23,954,441	69,655,786	93,610,227
Advertisement & Publicity	66,988,607	194,792,442	261,781,049
Less: Grant From Promoters	33,560,080	97,587,488	131,147,568
Administrative & Other Heads	31,755,906	92,341,232	124,097,138
Depreciation	1,408,505	4,095,713	5,504,218

Net Profit/ (Loss) for the year	(24,967,113)	(170,945,024)	(195,912,137)
Gross Profit ratio	36.61%,	30.64%	32.17%
Net Profit Ratio	-4.41%	-10.379T	-8.85%

It was submitted that the gross profit margin (Gross Profit/ Sales) earned by the appellant on transactions undertaken with the associated enterprise at 36.61% is higher than the gross profit margin earned on similar transactions undertaken with unrelated third parties at 30.64%. Further, the operating profit margin (OP/ Sales) earned by the appellant on transactions with the associated enterprise is at {-}4.41% was also found to be higher than the average operating profit margin earned on similar transactions undertaken with unrelated third parties at (-)10.37%.

It is further submitted that Hon'ble High Court, while dealing with the applicability of most appropriate method prescribed under transfer pricing provision of the Act, with respect to business of trading, held as under:

"159. RP Method, i.e. the Resale Price Method computes the arm's length price by ascertaining or identifying the price at which the product is resold by the AE to an independent enterprise. From this price, the amount of gross profit margin accruing to the AE or to an unrelated enterprise, i.e. comparable, is subtracted. The comparable should be engaged in purchase and re-sale of same or similar property and/or obtaining or providing similar services. From this amount, the expenses incurred by the AE in connection with the purchase of property or obtaining of services are further subtracted. At the fourth stage, adjustments are made taking into account the functional and other differences, including the accountancy practices, if any, between the tested international transaction and the comparable uncontrolled transactions to the extent they would

materially affect the gross profit margins in the open market. The price computed after the two reductions and after the adjustment on account of the functional and other differences, determines the arm's length price of the purchased property or services obtained by the assessed from the AE."

Further, Hon'ble High Court, also dealt with the methodology of application of RPM while benchmarking the alleged transaction of AMP expenses. Hon'ble High Court at Para 165 states that while applying RPM for benchmarking the transaction of AMP, the gross profit earned by the assessee shall be adjusted with the AMP expense and such adjusted gross profit margin shall be compared with the adjusted gross profit margin earned in undertaking uncontrolled transactions or earned by unrelated entities, as under:

165. An external comparable should perform similar AMP functions. Similarly the comparable should not be the legal owner of the brand name, trade mark etc. In case a comparable does not perform AMP functions in the marketing operations, a function which is performed by the tested party, the comparable may have to be discarded. Comparable analysis of the tested party and the comparable would include reference to AMP expenses. In case of a mismatch, adjustment could be made when the result would be reliable and accurate. Otherwise, RP Method should not be adopted. If on comparable analysis, including AMP expenses, gross profit margins match or are within the specified range, no transfer pricing adjustment is required. In such cases, the gross profit margin would include the margin or compensation for the AMP expenses incurred. Routine or non-routine AMP expenses would not materially and substantially affect the gross profit margins when the

tested party and the comparable undertake similar AMP functions.

Applying the Principles laid down by the Hon'ble Delhi High Court, the results of the benchmarking analysis is as under;

(i) Comparison of adjusted gross profit margin - internal comparable:

Particulars	Item No.	AE's Transactions	Non AE's Transactions	Total
Opening Stock				
Opening Stock	1	749,27,420	742,47,258	1491,74,678
Goods in Transit	2	763,16,874	209,18,535	972,35,409
Purchases & Direct Expenses				
Purchases & Direct Expenses	3	4199,32,495	12182,73,010	16382,05,505
Other Clearing Expenses	4	146,31,339	269,34,517	415,65,856
Sales				
Sales	5	6320,03,433	18377,67,613	24697,71,046
Sales Tax	6	653,02,343	1898,89,051	2551,91,394
Net Sales (5-6)	7	5667,01,089	16478,78,563	22145,79,652
Closing Stock				
Closing Stock	8	883,18,799	1752,48,536	2635,67,335
GIT	9	1382,72,964	222,34,962	1605,07,926
Gross Profit (8+9+7-1-2-3-4)	10	2074,84,725	5049,88,741	7124,73,465
Gross Profit Ratio(10/7 %)	20	36.61%	30.64%	32.17%
AMP Expenses				
Advertisement, Publicity and Sales Promotion	15	669,88,607	1947,92,442	2617,81,049
Less: Grant From Promoters	16	335,60,080	975,87,488	1311,47,568
Net AMP Expenses	15-16	334,28,527	972,04,954	1306,33,481
Adjusted Gross profit	17	1740,56,197	4077,83,787	5818,39,984
Adjusted Gross Profit Ratio	2.43	30.71%	24.75%	26.27%

(ii) Comparison of adjusted gross profit margin – external comparable:

It is submitted that the TPO in his order has considered two companies, namely (i) Vivek Limited and (ii) Goa

electronics Limited as comparable to the appellant for the purpose of benchmarking AMP expense of the appellant. The computation of adjusted gross margin of the aforesaid companies are as follows:

Particulars	Vivek Limited	Goa Electronics Ltd.
Sales of Goods	29,880.77	2,292.14
Cost of Sales		
Stores Consumed	52.07	
Opening Stock	2,646.88	15.96
Closing Stock	2,953.03	7.55
Trade Purchases	27,009.54	2,182.16
Total cost of sales	26,703.39	2,190.57
Gross Profit	3,177.38	101.57
GP Margin to sales	10.63%	4.43%
AMP Expenditure	824.67	1.39
Adjusted GP margin	2352.71	100.18
Adjusted GP Margin to sales	7.87%	4.37%
Average adjusted GP margin to sales		6.12%
Appellant adjusted gross margin in AE segment		30.71%
Appellant adjusted gross margin on entity level		26.27%

In view of the aforesaid, it would be seen that the adjusted gross profit margin earned by the appellant is higher than (i) gross profit margin earned from transaction undertaken with unrelated third parties and (ii) gross profit margin earned by comparable companies considered by the TPO, to compensate the alleged non routine AMP expenditure incurred by the appellant.

Even otherwise, applying the ratio of decision of Special Bench in the case of LG Electronics, no adjustment on account of AMP expense will be sustained in the present case, for the reason submitted as under:

Head	Total	Advertisement / Brand Promotion expenses	Sales Promotion	Remarks
0% Finance Scheme	1,18,42,863		1,18,42,863	Cost of 0% Finance Scheme Offered to customers
Local Branch Activities	33,13,897		33,13,897	Dealer expenses etc
Electronics Print Media	13,63,39,688	13,63,39,688		
Free Gift	18,48,403		18,48,403	Free Gifts on products sales
Hoarding /Glow Sign	74,84,263	74,84,263		
ISD Salary	1,55,62,353		1,55,62,353	Salary of the sales staff o' dealers place.
Others	18,95,898		18,95,898	Miscellaneous Sales Promotions Activities
Point of purchase materials	1,03,22,444		1,03,22,444	Printed Demonstration Material / Stickers and catalogues of the products sold.
Sales counter expenses	3,27,74,491		3,27,74,491	Expenses incurred for sales counters in shops etc.
Sponsorship fees	4,75,000	4,75,000		-
Sun shades	25,02,600	25,02,600		-
Travelling expenses	1,44,784		1,44,784	Misc. traveling expenses
Expenses payable	3,72,74,365	-	-	
Total	26,17,81,049	14,68,01,551	7,77,05,133	
Trade discount and volume rebate	47,86,42,347		47,86,42,347	
Total considered by TPO	74,04,23,369			

Computation of adjustment:

Particulars	Adjustment made by the TPO ('Rs.)	Adjustment considering SB order ('Rs.)
Total Revenue of the assessee	2,61,33,40,369	2,61,33,40,369
Arm's length % of AMP expenditure	1.4095%	1.4095%
Arm's length AMP expenditure	3,68,35,032	3,68,35,032
Expenditure incurred by the assessee on AMP	74,04,23,369	14,68,01,551
Expenditure incurred for developing the intangibles	70,35,88,364	10,99,66,519
Arm's length value of the Capital Grant	70,35,88,364	10,99,66,519

<i>Amount of Capital Grant received by the assessee</i>	<i>13,11,47,568</i>	<i>13,11,47,568</i>
<i>Difference</i>	<i>54,24,40,796</i>	<i>Nil</i>

In view thereof, no adjustment will survive in the present case on account of alleged difference in arm's length price of AMP expenditure incurred by the appellant.”

12. On the other hand, the learned Senior Departmental Representative vehemently argued that the matter needs to be remitted back to the file of the AO/TPO. She submitted that figures given in tables by the learned Authorised Representative were not emanating either from the order of the TPO or the DRP and therefore, gross profit and net profit ratio computed were not verifiable. Further, she submitted that AMP functions performed either by the third parties or the Associated Enterprises or other comparables were not available on record, in absence of which to compute the arms length price of international transaction of AMP following the ratio laid down by the Hon'ble Jurisdiction High Court in case supra, was not feasible at the level of the ITAT.

13. We have heard the rival submissions and perused the relevant material placed on record including the impugned judgment of the Hon'ble High Court. The learned Authorised Representative has submitted that the assessee company has followed Resale Price Method for benchmarking its international transaction of distribution. Further, the learned AR has submitted that gross profit margin earned

by the assessee being higher than gross profit margin by internal as well as external comparables, no adjustment for AMP expenses was required in the case of the assessee.

14. After considering rival submissions, issue which arises before us is that whether we can compute the arms length price of the international transaction of AMP expenses in the given circumstances or we need to remit the matter back to the AO as submitted by the learned SR DR. The Hon'ble High court in Sony Ericsson (supra) has held that the foreign AE may choose different option of compensating the local AE for AMP expenses like low purchase price, no or low charges of royalty or direct compensation. Accordingly, the Hon'ble High Court directed that the arms length price of the transaction of AMP expenses should be computed preferably along with the arms length price of international transaction of distribution in a bundled manner and for this purpose AMP function of the assessee should be first compared with the AMP functions of the comparables. The Hon'ble High Court in their judgment (supra) has analyzed various methods of computation of international transaction of AMP expenses. While discussing Resale Price Method, in para 162 of the impugned judgment, the Hon'ble High Court in respect of choosing internal comparable has held as under:-

“162 In the case of Reebok India Co. Ltd., the assessee has applied RS Method using internal comparable. Contrary to the

general rule, the internal comparable possibly may not be appropriate when the assessed has incurred considerable (not necessarily extra-ordinary or non-routine) AMP expenses. The reason is obvious; there is no comparability analysis possible. In such cases, it is not possible to examine and compare the functional comparability between the controlled tested transaction and uncontrolled internal party transaction on account of AMP expenses. Internal comparable would not account for the credible gross profit rate, which an AE should be ensured when it incurs AMP expenses. Functionally the comparable is merely a manufacturer and thus, the said function is compared. AMP expenses do not get factored and compared. As an abundant caution, we would still add that where adjustments clause (iv) can give reliable and accurate results, internal comparables could still be applied. This would likely happen, when AMP expenses are insignificant in quantum.”

15. Once we advert back to the facts of the case in hand, we find that the assessee has incurred considerable AMP expenses and the advertising, marketing and promotion functions performed either by the third parties or the associated enterprise are not emanating either from the order of the AO/TPO or DRP or from the transfer pricing studies submitted by the assessee, therefore it is not possible for us to examine and compare functional comparability between the assessee company and its associated enterprises or third parties.

16. Further, in para 163 to 168 the Hon'ble Court, while discussing Resale Price Method, has given direction as when to use external comparables. The relevant para of the judgement are reproduced as under:-

“163. Thus, in such cases, external comparables where said parties are performing similar functions including AMP expenses would give more accurate and precise results.

164. However, it would be wrong to assert and accept that gross profit margins would not inevitably include cost of AMP expenses. The gross profit margins could remunerate an AE performing marketing and selling function. This has to be tested and examined without any assumption against the assessed. A finding on the said aspect would require detailed verification and ascertainment.

165. An external comparable should perform similar AMP functions. Similarly the comparable should not be the legal owner of the brand name, trade mark etc. In case a comparable does not perform AMP functions in the marketing operations, a function which is performed by the tested party, the comparable may have to be discarded. Comparable analysis of the tested party and the comparable would include reference to AMP expenses. In case of a mismatch, adjustment could be made when the result would be reliable and accurate. Otherwise, RP Method should not be adopted. If on comparable analysis, including AMP expenses, gross profit margins match or are within the specified range, no transfer pricing adjustment is required. In such cases, the gross profit margin would include the margin or compensation for the AMP expenses incurred. Routine or non-routine AMP expenses would not materially and substantially affect the gross profit margins when the tested party and the comparable undertake similar AMP functions.

166. On behalf of the assessee, it was initially argued that the TPO cannot account for or treat AMP as a function. This argument on behalf of the assessee is flawed and fallacious for several reasons. There are inherent flaws in the said argument. Moreover, the contention of the assessed in these appeals would mandate rejection of the RP Method, as an appropriate or most appropriate method. Comparison or comparative analysis is undertaken at stage (ii). Adjustments are permissible and

undertaken at stage (iv). Under clause (iii), i.e. at stage (iii), from the price ascertained at stage (ii), expenses incurred by the enterprise in connection with the purchase of property or obtaining of services is reduced. Under clause (iv), adjustments have to be made on account of functional difference which would include assets used and risk assumed. It is at stage (iv) of the RP Method that the Assessing Officer/TPO can make adjustments if he finds that an assessee has incurred substantial AMP expenses in comparison to the comparables. Once adjustments are made, then the appropriate arm's length price can be determined. In case, it is not possible to make adjustments, then RP Method may not be the most appropriate and best method to be adopted.

167. Before us, the Revenue has not pleaded or submitted that the RP Method should not have been adopted. The TPO and the Assessing Officer did not reject the RP Method adopted by the assessee. The assessee submit that the Revenue accepts functional parity and in fact, without adjustment. Contra, Revenue would argue that the Assessing Officer/TPO and the Tribunal have adopted and applied the CUP Method for determining arm's length price of AMP expenses. We do not pronounce a firm and final opinion on the said this as it should be at first examined by the Tribunal.

168. The Tribunal has upheld adoption of CP Method after applying bright line test' in the case of Reebok India Co. Ltd. and Canon India Pvt. Ltd. The bright line test' adopted to demarcate the routine and non-routine AMP expenditure is predicated on selection of a domestic distributor and marketing company that does not own intangible brand rights. Contract value would be treated as NIL. In terms of our finding recorded above, the said finding would not be correct. The approach and procedure for ascertaining /determining arm's length price under the RP Method is different. For this reason, and other grounds recorded, we have passed an order of remit to the Tribunal for examination of the factual matrix.”

17. Once we examine the facts of the case in hand, we find that the learned Authorised Representative has submitted that gross profits margin earned by the assessee being higher than gross profit margins earned by comparables companies, no adjustment is required for the purpose of computing arms length price of international transaction of AMP expenses. If the argument of the learned AR is accepted, it will lead us to a result where the AMP transaction will be rendered as non international transaction, as against the findings of the Hon'ble High Court in the case of Sony Erricsson (supra). The Hon'ble High Court has directed to find out AMP functions of comparables and compare the same with the AMP functions performed by the assessee and then after making adjustments if any compute the arms length price of the international transaction in bundled manner for distribution as well as AMP expenses and if not possible to compute in bundled manner, then only in separate manner. But in the case in hand the AMP functions performed by the external comparable are neither submitted by assessee before the AO/TPO nor examined by the TPO. The learned Authorised Representative has also failed to exhibit us the AMP functions carried out by the assessee and compare those functions with the AMP functions of the comparables and without that analysis the arms length price of the AMP functions cannot be determined at our level. We are also in agreement with the submission of the learned Senior Departmental Representative that

the figures given in the tables by the learned Authorised Representative are not verifiable from the orders of the AO/TPO. In view of the above facts and circumstances, we are unable to determine the ALP of AMP expenses at our own either in the bundled or a separate approach.

18. Further, we may like to take note of the decision of the ITAT in the case of Reebok India Co. Vs. DCIT, Circle-21(1), the ITAT 'I' Bench Delhi in ITA No.1246/Del/2005 and SA No.158/Del/2014, where the matter has been remitted back to the file of the AO for determination of the ALP of AMP expenses, in view of the ratio laid down by the Hon'ble High Court in the case of Sony Ericson Mobile Communication P Ltd (supra). The assessee in that case was following resale price method for determination of international transaction of distribution. Relevant para of the order is as under:-

“17. Accordingly for the detailed reasons given herein above the issues addressed in Ground No.-2 2.27 are restored to the file of the AO/TPO to decide the same denovo in the light of the judgement of the Hon'ble High Court. Needless to say that the assessee shall be affording a reasonable opportunity of being heard.”

19. Further, the ITAT Delhi Bench in the case of Toshiba Vs. DCIT in ITA No.1101/Del/2015, wherein the assessee was following TNMM method for benchmarking its international transaction of distribution has also remitted the matter back to the AO/TPO for computing the ALP of AMP expenses , in view of the judgment of

the Hon'ble jurisdictional High Court in the case of Sony Ericson (supra) with following remarks:-

“15. Coming back to the facts of the instant case, we find that no detail of the AMP functions performed by the assessee is available on record. Similarly, there is no reference in the order of the TPO to any AMP functions performed by comparables. In fact, no such analysis or comparison has been undertaken by the TPO because of his applying the bright line test for determining the value of the international transaction of AMP expense and then applying the cost plus method for determining its ALP. The ld. AR also failed to draw our attention towards any material divulging the AMP functions performed by the assessee as well as comparables. As such, we are handicapped to determine the ALP of AMP expenses at our end, either in a combined or a separate approach. Under such circumstances, we set aside the impugned order and send the matter back to the file of the TPO/AO for determining the ALP of the international transaction of AMP spend afresh in accordance with the manner laid down by the Hon'ble High Court in Sony Ericson Mobile (supra). Ex consequenti, the ground raised about the TPO having no jurisdiction to determine the ALP of AMP expenses, is dismissed following the judgment in the case of Sony Ericsson Mobile (supra).”

20. In view the above decisions of the Tribunal and our findings in the facts and circumstances of the case, we remit the matter back to the file of AO/TPO for determination of ALP on international transaction on AMP expenses, in accordance with the direction laid down by the Hon'ble High Court in the case of the assessee led by Sony Ericson Mobile Communication P Ltd (supra). Needless to say

that the assessee shall be afforded a reasonable opportunity of being heard.

21. In the result the appeal of the assessee is allowed for statistical purposes.

22. In view of the above findings given in ITA No 4680/del/2010 for Assessment Year 2006-07, the matter in ITA 5235/Del/2010 and ITA No. 4404/Del/2010 for Assessment Year 2007-08 and 2008-09 respectively are also restored back to the file of AO/TPO for determination of ALP of international transaction of AMP expenses, as the facts and circumstances of the Assessment Years 2007-08 and 2008-09 are also similar to the facts of the Assessment Year 2006-07.

23. Accordingly, appeals are allowed for statistical purposes.

Order Pronounced in the Court on 28/10/2015).

-Sd/-

(C.M. Garg)

JUDICIAL MEMBER

Dated:28/10/2015

Ajay

Copy forwarded to:

1. Appellant

2. Respondent

3. CIT

4. CIT(Appeals)

5. DR: ITAT

-Sd/-

(O.P. Kant)

ACCOUNTANT MEMBER

ASSISTANT REGISTRAR