

**IN THE INCOME TAX APPELLATE TRIBUNAL,
CHENNAI D BENCH, CHENNAI
[Coram: Pramod Kumar AM and G Pavan Kumar JM]**

I.T.A. No. 853/Chny/2014 and 563/Chny/2015
Assessment year: 2009-10 and 2010-11

Hyundai Motor India LimitedAppellant
*Plot No. H-1 SPICOT Industrial Park
Irrungattukottai, Sriperumbudur Taluk
Kancheepuram 602 117 [PAN: AAACH2364M]*

Vs

**Deputy Commissioner of Income Tax
LTU-II, Chennai**Respondent

I.T.A. No. 739/Chny/2014 and 614/Chny/2015
Assessment year: 2009-10 and 2010-11

**Deputy Commissioner of Income Tax
LTU-II, Chennai**Appellant

Vs

.....Respondent
Hyundai Motor India Limited

I.T.A. No. 842/Chny/2016
Assessment year: 2011-12

Hyundai Motor India LimitedAppellant
[PAN: AAACH2364M]

Vs

**Deputy Commissioner of Income Tax
LTU-II, Chennai**Respondent

I.T.A. No. 761/Chny/2016
Assessment year: 2011-12

**Deputy Commissioner of Income Tax
LTU-II, Chennai**Appellant

Vs

.....Respondent
Hyundai Motor India Limited
[PAN: AAACH2364M]

CO No. 73/Chny/ 2016
Arising out of I.T.A. No. 842/Chny/2016
Assessment year 2011-12

Hyundai Motor India Limited **Cross objector**
[PAN: AAACH2364M]

Vs

Deputy Commissioner of Income Tax
LTU-II, Chennai **Respondent**

Appearances by:

R Vijayraghavan, K R Sekar, and S P Chidambaram for the assessee
Sriram Sheshadhri for the assessee (appearing separately for the last year)
S Bharat and P Peeraya for the revenue

Date of concluding the hearing : February 1, 2017
Date of pronouncing the order : April 27th, 2017

O R D E R

Per Pramod Kumar AM:

1. These six appeals and one cross objection, which we will take up together, consist of three sets of cross appeal for the assessment years 2009-10, 2010-11 and 2011-12 and the solitary cross objection filed by the assessee for the assessment year 2011-12.

2. These three set of cross appeals are directed against the orders 31st January 2014, dated 30th January 2015 and 28th January 2016 passed by Deputy Commissioner of Income Tax, LTU-II, Chennai (hereinafter referred to as ~~the~~ Assessing Officer), in the matter of assessments under section 143(3) r.w.s. 144C(13) of the Income Tax Act, 1961 (hereinafter referred to as ~~the~~ Act) for the assessment years 2009-10, 2010-11 and 2011-12 respectively. There is also a cross objection filed by the assessee for the assessment year 2011-12 but that is, for the reasons we will set out now, not maintainable. The scheme of the Act, as we understand it, does not permit filing of cross objection against the order of the Assessing Officer. A cross objection, in appropriate cases, can only be filed to challenge the order passed by the Commissioner (Appeals). This aspect of the

matter is clear from the relevant statutory provision, that is section 253(4), which provides as follows:

The Assessing Officer or the assessee, as the case may be, on receipt of notice that an appeal against the order of the Commissioner (Appeals), has been preferred under sub-section (1) or sub-section (2) by the other party, may, notwithstanding that he may not have appealed against such order or any part thereof, within thirty days of the receipt of the notice, file a memorandum of cross-objections, verified in the prescribed manner, against any part of the order of the Commissioner (Appeals), and such memorandum shall be disposed of by the Appellate Tribunal as if it were an appeal presented within the time specified in sub-section (3).

3. The cross objection is thus dismissed as not maintainable.
4. We will first take up the appeal of the assessee for the assessment year 2009-10.
5. Ground no. 1 is general and it does not call for any specific adjudication by us.

Transfer Pricing Issue:

6. In ground no. 2, the assessee has raised a grievance against attributing a notional income of Rs 54,15,28,903 to the assessee on account of compensation for deemed brand development and as compensation for assessee depriving himself of the use of his own logo and brand name in the motor vehicles manufactured by the assessee.

7. However, in the three sets of cross appeals, there is this common transfer pricing issue, with respect to the arm's length price adjustment in respect of brand promotion by the assessee for its foreign parent company, in all the three assessment years. The facts of these three assessment years are also interconnected. We will, therefore, take up this transfer pricing issue first and we will take up all the three assessment years together on this issue. As learned representatives fairly agree, the short issue that we are required to adjudicate in this respect is whether, on the facts and in the circumstances of this case, the Assessing Officer was justified in making the arm's length price adjustment of Rs 54,15,28,903, Rs 62,20,34,587 and Rs 253,44,00,000 for the assessment years 2009-10, 2010-11 and 2011-12 respectively, in respect of brand promotion by the assessee for its non-resident parent company. So far as this issue in appeal is concerned, the relevant material facts, to the extent necessary for adjudication on these appeals, are like this. The assessee before us is a fully owned subsidiary of South Korean automobile giant Hyundai Motor Company (HMC, in short)- fourth largest automobile manufacturer in the world, and is engaged in the business of manufacturing cars in India. The assessee entered into a number of international transactions with its associated enterprises abroad. During the course of scrutiny of arm's length determination of these transactions, the Transfer Pricing Officer observed, so far as

the assessment year 2009-10 is concerned, that the assessee is manufacturing cars under the brand name Hyundai a brand which is legally owned by the HMC Korea, and that the assessee is to mandatorily, under the agreement with HMC Korea, use the badge with trademark Hyundai in every vehicle manufactured by it. The TPO was of the view that by doing so the assessee has significantly contributed to the development of Hyundai brand in Indian market and the HMC Korea is thus benefited due to brand promotion activity carried out by the assessee company. However, as noted by the TPO, the assessee company has not shown any compensation received from the holding company (i.e. legal owner of the Hyundai brand) for developing the brand. The TPO then referred to the decision a special bench of this Tribunal, in the case of **LG Electronics Pvt Ltd Vs ACIT [(2013) 22 ITR (Trib) 1 (Del)]** which, according to the TPO, has treated brand building in the local market as an international transaction. It was in this background that the TPO faulted the assessee for not having benchmarked the international transactions relating to brand development and proceeded to add, based on his analysis of certain observations in paragraph 1.42 of the OECD's Transfer Pricing Guidelines, that instead of benchmarking the aggregating all the transactions and then benchmarking the same on the basis of TNMM (transactional net margin method), it is desirable that transaction relating to brand building is benchmarked separately and on the basis of the CUP (Comparable Uncontrolled Price) Method. The TPO, thereafter, discussed in detail as to how the use of Hyundai badge on the vehicles manufactured by the assessee was mandatory and that the assessee was under an obligation to use the name Hyundai in the name of all the cars manufactured by the assessee. He was of the view that this mandatory requirement of using the name Hyundai in name of the cars has not given any benefit to the assessee company but has deprived the assessee of developing its own brand name and logo, thus being double jeopardized. The TPO then observed that no unrelated entity would enter into such an arrangement which would benefit one party and make the other party vulnerable and that any unrelated entity would indulge in creating and promoting its own brand so that the brand owned by it gets developed over a period of time and helps in capturing domestic market as well as global market. It was then noted that the brand name Hyundai is getting popularized which has led the holding company to have bigger share in the automobile market globally but the assessee company has no identity and has to wear the mask of holding company even though the cost spent and efforts taken in promoting the brand name are attributed to the assessee company. The TPO then set out his analysis about the virtues of emerging Indian automobile market presence in which ensures that even in case of downfall in global market, Hyundai Korea will not suffer. He was of the view that Hyundai is a very important player in Indian car market and this is to a very large extent due to the efforts by the assessee company that the brand name Hyundai has become an intangible asset in India. The TPO was of the view that HMC Korea, has to, therefore, compensate the assessee company with arm's length amount for the benefit acquired at the cost of the assessee company which has been deprived of developing its own brand name and logo. The TPO was of the view that Indian market is not a fluctuating market, that it is a decisive market which stands by quality and comfort and that brand building is a difficult task in India as the brand cannot be popularized just because of its global reputation. He went on to add that

Had it been a reality that any foreign company can enter into the Indian market just by brand popularity, the Indian market should have been stacked with millions of foreign companies but there are many hints in history to illustrate the failure of prominent foreign companies in establishing their share in Indian market. As for the nature of brand promotion, the TPO, *inter alia*, stated as follows:

Brand Value is the amount that a brand is worth in terms of income, potential income, reputation, prestige, and market value. Brands with a high value are regarded as considerable assets to a company, so that when a company is sold a brand with a high value may be worth more than any other consideration.

It is a collection of perceptions in the mind of the consumer. A brand serves to differentiate competing products or services by highlighting what is unique about each. Both physical and emotional factors are triggered that create a relationship between consumers and the product/service.

It is true that a customer is ready to pay a premium for the brand when he pays for the product, This payment is not a compensation for the advertisement but a compensation for the loyalty he/she develops on his/her mind on the brand. The emergence of various brands of same specifications has resulted in less distinction of variation between the products of various brands. But the customers are moving towards a brand though they understand from the advertisements that the specifications and facilities are same in all the brands. It is the value the brand gains from the customer. The customer pays certain part of the total payment for the product as a premium for the brand. This premium paid by the buyer is not in monetary terms but through the support given and loyalty shown on the brand. This support and loyalty result in huge gain in increasing the value of the company. Thus, this support and loyalty becomes an intangible asset for the company which gets accumulated every year

8. The TPO then noted that the assessee had the brand value of Hyundai, as evident from the Interbrand valuation- which is one of the most respected brand valuation worldwide, the Hyundai was one of the top 100 brands worldwide for the fourth year in a row but the valuation of Hyundai brand has gone up from US \$ 4.5 billion in 2007 to US \$ 4.8 billion in 2008. He was of the view that the increase in brand value each year can be attributed to every vehicle manufactured by the group companies, and as sales of the assessee company was 18.07% of the global sales worldwide, 18.07% of the global appreciation in the brand value can be attributed to the assessee company. This amount was quantified at Rs 198,66,80,250.

9. The plea of the assessee that he has not rendered any brand building service and there was no brand promotion activity carried out by the assessee company+ in the absence of which there was no requirement to compensate the assessee company, was brushed aside with the observation that the use of brand name Hyundai along with the model name and the use of logo in the front of all the

vehicles manufactured by the assessee company was a definite developmental activity undertaken by the assessee+ and that %here was no need for the assessee company to include brand name and logo alongwith the model name of the vehicleõ the vehicle can be easily marketed only with the model name as the customer values the vehicle based on the model+. Similar was the fate of the assesseeç plea that the assessee and the Hyundai Korea have %not entered into any contract for brand building services+ and that %there is no such arrangement, the holding company cannot be said to have benefited at the expense of the assessee company and, as such, the assessee is not entitled to any compensation+. The TPO rejected this argument by observing that the agreement of the assessee with Hyundai Korea %requires the assessee company to use the badge with the trademark of Hyundai in every vehicle manufactured by the assessee company using the technology supplied by the holding company+. It was held that there was thus a contract between the assessee company and the Hyundai Korea for use of brand name and logo without any consideration+ and I is on the basis of this agreement that it can be easily inferred that there is an international transaction, without any consideration, between the assessee and Hyundai Korea- an associated enterprise. As for the next plea of the assessee, i.e. assesseeç economic ownership of Hyundai brand name in India, even if assessee is economic owner of the brand Hyundai in India, it is beyond dispute that benefits of brand promotion accrue both to the legal owner as also the economic owner and while the position of legal owner is legally protected, the economic owner does not have such an advantage. The TPO was, therefore, of the view that the benefit of brand promotion accrues to legal owner which must be compensated. Once again, he leaned on the special bench decision in the case of LG Electronics (*supra*) wherein it is said to have been held that %is not denied that there can be no economic ownership of a brand but that exists only in a commercial senseõ .when it comes in the context of the Act, it is only the legal ownership of the brand that is recognized+. As for the assesseeç pointing out that there is no brand promotion expense incurred by the assessee, the TPO observed that %a the absence of separate item for expense on brand development in the profit and loss account of the company, it has become task of the TPO to derive the quantum by other means+ and that %has been a well established fact that in a difficult scenario where the expenses cannot be segregated exclusively, the expenses can be calculated from the quantum of income derived due to those expenses+. He then concluded that %has been through a scientific analysis that the increase in brand value has been derived and the part of the assessee company in the increase in brand value has been computed+ and that %his contribution can be treated as income from the activity undertaken by the assessee company to promote its brand+. As for the plea that the assessee company has infact benefited by the use of brand name ±Hyundaiq the TPO, inter alia, stated as follows:

If the contention of the assessee company has been taken for consideration, then the following questions arise for discussion-

- i) *If the holding company is not getting benefitted by the brand development, why it has been made a mandatory requirement in the agreement?*

ii) *If the use of brand in all the vehicles benefits only the assessee company, what is the reason behind the charitable purpose of the holding company in allowing the assessee company to use the existing popular brand?*

No business entity will enter into an agreement for charity with another entity. It is for certain hidden benefits, the holding company has made the assessee company use the brand name and logo in all the vehicles manufactured. Had it been for charity, the holding company would have not insisted the assessee company to pay a fee as royalty fee and to pay fees for technical knowhow and for technical services. The assessee company has compensated the holding company for the use of technology, knowhow and for the technical services rendered by the holding company. The compensation given is no way less than the compensation that has been paid by an entity to another independent entity for the same cause.

It is true that the technology has been developed and licensed by the holding company. But it has been materialized by the efforts taken by the assessee company. The industriousness in understanding the customer requirements, the perfection in manufacture, the sincerity in production, the genuineness in marketing, the intensity in sales all are undertaken by the assessee company which play a major role in brand creation. As pointed out earlier, the perfection and sincerity can be exhibited only in the practical implications. The above statement undoubtedly substantiates that the assessee company has the competence to build its own brand name. But it has been deprived of such activity because of the mandatory requirement to exhibit the brand name and logo of the holding company.

It may be true that the brand "Hyundai" is globally visible but the assessee company has put its efforts to promote that brand in Indian market which is 175th of the global market. The assessee has claimed that the technology and quality has primarily led the increase in brand value. The technology cannot increase the brand value on its own. The success of technology lies in its perfect execution and that has been done by the assessee company. Further, the credits of maintaining the quality goes to the assessee company only as the quality assurance has been given not for the concept but for the manufacture.

Hence from all angles, it has been evidently seen that the holding company, not the assessee company, is getting benefitted of the brand development activity. The assessee company has to be compensated for that activity as it has been deprived of developing its own brand for which it is fully competent and entitled.

..... It is further clarified that the emergence of global brands into Indian market was only after the globalization era. In India, the year 1991 was

said to be the entry gate for the concept "Liberalisation, Privatisation and Globalisation". The last decade of the 20th Century saw huge chunks of global bees sprang into India with a cautious note. Every company entered into the market with checks and balances and had trial and error method to capture the market. The emergence of global companies and their sustenance had become a significant one. It was not all the companies with reputed brand name entered India and established their market. It was only a very few companies which were able to find a permanent place in Indian market. Had it been the fact that only brand value captured the market, all the companies with reputed brand value should have sustained in Indian market. But the Indian market was unique of its quality and expectation. The Indian market practiced to have loyalty on quality and cost efficient. The Indian market has a major portion which values cost much than anything else. The Indian market was ready to compromise luxury for the benefit of cost. Its immediate need was comfort and not luxury. So, the Indian market tried to see each and every brand not by its name but by the comfort and cost effective nature. Thus the global companies, which would have understood the temperament of the Indian market, tried to bring out their product with maximizing the comfort and minimizing the cost. Those companies survived in Indian market and the others vanished from the market.

The foremost step taken by the global companies to meet the expectations of the Indian market was either to have a manufacturing unit in India itself or to have joint venture with any Indian company. This step is to cut down the production cost and marketing cost. The parent company of the assessee company has taken the step of establishing a manufacturing unit in India by creating a wholly owned subsidiary.

The assessee company on its creation as a wholly owned subsidiary started to function from the scratch and penetrated into Indian market by introducing its vehicles which would suit the Indian market with minimum price and maximum comfort. The comfort level has been getting modified further by various versions of the same model and it shows how the assessee company competes to hold the market.

After establishing a competitive share in the market, the assessee company started to export the same cars to other developing countries, where the expectations are same. Thus, the assessee company already started from scratch and has come to this level, but it has lost its identity as it wears the mask of the holding company. The whole effort taken to capture the market has been attributed to the holding company so far. Hence it is true from the facts that the assessee company has indulged in creating and developing the marketing intangible for the holding company.

10. It was in this backdrop that the Assessing Officer proposed an arm's length price adjustment of 198,66,80,250 in respect of compensation that the assessee should have received, from Hyundai Korea, for brand development. Aggrieved by

this draft proposal, assessee carried the matter in appeal before the Dispute Resolution Panel. The arguments placed by the assessee, which were broadly similar to the arguments advanced before the TPO, did not find favour with the DRP either. The DRP rejected the submissions of the assessee and confirmed, in principle, the stand of the Assessing Officer. The only new plea of the assessee that its selling advertisement expenses at Rs 312.05 crores constituted 2.01% of sales, whereas similar expenses incurred by Hindustan Motors (5.93%), Tata Motors (1.26%) and Mahindra & Mahindra (2.41%) averaged 3.20%, and, for that reason, ALP adjustment cannot be made in connection with the same, was also rejected on the ground that the data given by the assessee is inclusive of selling expenses in cases of comparables whereas comparison should only be at the level of AMP (*advertisement, marketing and promotion*) expenses. While the DRP thus upheld the ALP adjustment in principle, the quantum of adjustment was scaled down in the sense that as against the share in global sales, in terms of quantity of cars sold, the DRP adopted the share in global sales, in terms of value of cars sold. This variation in the mechanism of allocating contribution to global brand value resulted in the reduction of ALP adjustment to Rs 54,15,28,903. The assessee is aggrieved and is in appeal before us.

11. The situation in the two subsequent assessment years was a slightly different. As regards the plea that the assessee did not incur excessive expenditure on advertising, promotion and marketing being less than 1.63% of sales as against similar expenses by comparables, i.e. Hindustan Motors (4.25%), Tata Motors (1.09%) and Mahindra and Mahindra (2.53%), averaging to 2.62%, the TPO did accept that the percentage of AMP expenses as a proportion of net sales is not an unreasonable high figure and that the arguments of the assessee that there is no excess over and above a market benchmark average in this financial year is accepted. Yet, the TPO proceeded with this stand as taken in the preceding year and observed that however, this does not mean that there are no taxable marketing intangibles being brand value being created since as discussed earlier, brand building is a continuous activity carried out by HMIL through the instrument of sales. It was once again stated that a significant portion of this benefit accrues to the parent company and the parent company has not compensated for this benefit accruing to them through the efforts of the assessee company. The TPO then further observed as follows:

The issue of the advertising expenses not being in excess of comparables has already been discussed above. However, it is considered position of this office that brand building activity is a conscious part of 'sales sub conscious', in that as and when selling and allied activities take place, brand building activities are implicit yet conscious drivers of the same. From being a conscious objective, selling becomes part of the psyche of the organization and in carrying this out, brand building activities are fellow participants. Plus any brand value that is built accrues to the credit of HMC. Therefore, the assessee's statement that "there is no brand promotion activity carried out by the HMIL for HMC" is rejected on account of not being supported by facts, logic and science (established academic literature).....

.....
What remains unreported as international transaction as well as in the statement of accounts is the additional brand (marketing intangible) value created by the sale activity. This has not been captured or allocated. As the value accrues to the benefit of HMC, the beneficiary has received the same without commensurate compensation. The benefit received by HMC has transmuted into part of the enhancement of its market capitalization, an enhancement in value that has come free after accruing to HMC's credit in India and has escaped tax incidence in India

12. The assessee's plea that brand building service, even if that be so, is at best a notional income which cannot be brought to tax, the TPO observed that section 2(24), being a generic section, is not applicable in the context of transfer pricing and that income from an international transaction, as is the mandate of section 92, is to be computed having regard to arm's length price. As regards the contention of the assessee that brand building even if that be so, is not an international transaction, the TPO, *inter alia*, observed as follows:

Section 92B of the Income-tax Act reads as follows:

"92B (1) For the purposes of this section and sections 92 92C. 92D and 92E, international transaction means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises.

(2) A transaction entered into by an enterprise with a person other than an associated enterprise shall, for the purposes of sub-section (1), be deemed to be a transaction entered into between two associated enterprises, if there exists a prior agreement in relation to the relevant transaction between such other person and the associated enterprise, or the terms of the relevant transaction are determined in substance between such other person and the associated enterprise."

The emphasis (bold italics) in the above has been supplied by this office. From a literal reading of the language of this part of the section, it is amply clear that the transaction in this instance involving Brand value is:

a) *A mutual agreement/arrangement between the assessee and its AE for a cost or expense incurred or to be incurred in connection with a*

benefit, service or facility provided or to be provided to the AE (being the economic value of brand enhancement). It is because that the provider of IP, knowhow and technology is an AE being its owner and parent that the assessee has come into being and commenced business. The genesis of and continuance in business by HMIL was the creation of HMC. HMC wished to generate value through its AE (HMIL) and hence invested in it; it is obviously interested in not only monitoring, but also driving, husbanding, and even directing the factors (read: the offering of loans) and courses of events that influence the AEs fortunes.

b) a prior agreement in relation to the business operations of HMIL, in the full know that manufacturing and selling activities that aim to exploit a brand by using it will enhance the value of such brand to the benefit of the legal owner of such brand. Both HMC and HMIL are not novices in the world of business, law, regulations, economics and finance to not understand or appreciate the implications of value generation, accrual, assignment and taxability.

Moreover, the Explanation that follows the section reads "For the removal of doubts, it is hereby clarified that the expression "international transaction" shall include....." An inclusive definition is clearly indicated here. The Explanation to Section 92B has been amended by the Budget 2012 as follows:

"In section 92B of the Income-tax Act, after sub-section (2), the following Explanation shall be inserted and shall be deemed to have been inserted with effect from the 1st day of April, 2002, namely:

'Explanation— For the removal of doubts, it is hereby clarified that—

(i) the expression "international transaction " shall include—

C. The purchase, sale, transfer, lease or use of tangible property including building, transportation vehicle, machinery, equipment, tools, plant, furniture, commodity or any other article, product or thing;

D. The purchase, sale, transfer, lease or use of intangible property, including the transfer of ownership or the provision of use of rights regarding land use, copyrights, patents, trademarks, licences, franchises, customer list, marketing channel, brand, commercial secret, know-how, industrial property right, exterior design or practical and new design or any other business or commercial rights of similar nature;

E. Capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable

securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;

F. Provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service;

G. A transaction of business restructuring or reorganization, entered into by an enterprise with an associated enterprise, irrespective of the fact that it has bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date;

The Explanation hence provides that transfer pricing provisions shall be applicable on all international transactions irrespective of the fact whether it has any bearing on the profit, income or losses or not. In addition to this, the capital/debt financing has also been included in the definition of international transaction. This amendment has been proposed with retrospective effect from assessment year 2002-03. The assessee has exceeded its authority and brief in misinterpreting the literality of the provisions for reasons best known to it and omitted to mention the transactions on COS issued to its international AEs

13. In computing the increase in brand value, the TPO also took note of brand value as per Millward Brown Optimor and adopted average of the brand value as per Interbrand as also Milward Brown Optimor. He then proceeded to compute the adjustment at Rs 62,20,34,587 on the basis of the following analysis:

Correlation with market capitalization

The market cap of HMC is a robust financial measure that indicates investor perceptions about overall performance and can be employed to benchmark its Brand value.

The non-linear regression using a third degree polynomial fit was carried out on the above with the market capitalization as the independent variable and the Brand Value as the dependent variable. This is to determine the relationship between the two variables statistically and in particular, determine the correlation. The results are as follows:

$$\text{Brand Value} = a + bx + cx^2 + dx^3 \dots$$

Where x = Market Capitalization; a = -1.09017.44; b = 18.95; C= 0.0001; d= 1.917x10⁽⁻⁸⁾

Correlation Coefficient = 35.24%; Standard Error= 444.52 USD

The correlation coefficient of 35.24% is in line with most brand research findings that show that brand value relates to market capitalization by about 30% to 40%.

It is determined that for the F.Y. 2009-10, the sales of HMC = USD 98,858,266 = INR 494291,33,00,000 approximately at INK 47.64113 to 1 USD.*

*[*Note on the USD/INK exchange rate: The additional Brand value was created by HMIL during the Financial Year 2009-10 and not just at the end of the Financial Year. The exchange rates employed need to be a figure that is representative of the year as a whole. Exchange rates vary during the year. The average rate is hence preferable over an extremity value like the year-end rate. Accepting a year end rate without reason indicates unwarranted bias towards and an undesirably iniquitous benefit being extracted by the assessee. The average monthly rates of INR per 1 US Dollar for Fin Year 2009-10 (source: <http://www.x-rates.com>) are as follows:*

Month	INR/USD	Month	INR/USD
April	49.96075	October	46.69925
May	48.49682	November	46.5612
June	48.49682	December	46.56873
July	48.3825	January	46.00664
August	48.24914	February	46.3173
Sept	48.31328	March	45.449033

The average of the Exchange rates = 47.64113INR / USD. This rate is applied.]

Using the above exchange rate of INR 47.64113 to 1 USD, Sales of HMC during the F.Y. 2009 - 10 = USD 9885,82,66,000 = INR 470971,95,02,000 approximately.*

The sales of HMIL during the F.Y. 2009 - 10 = INR 19622,50,00,000. This means that the sales of HM1L as a proportion of HMC = 4.166%

NB: In the assessment for the A.Y. 2009 - 10, the assessee had argued for adopting only the domestic sales (in India) in the computation of Brand value enhancement. The assessee has reiterated this argument this year too. The same is not accepted since the Hyundai brand is international and it is contribution of HMIL to this international brand that is being valued. The manufacturing activities of HMIL are aimed at an international market including India. Domestic sales in India alone will not capture the total value of the Hyundai" Brand enhanced by the business activities of HMIL. The proportion of International Sales of HMIL to the International Sales of HMC

will be the symmetric, fair and accurate proportion of HMIL's influence and impact on the Brand value. Taking the domestic sales of HMIL alone will be distort the computations prejudicially in favour of the assessee.

Increase in Market capitalization of HMC from 2008-09 to 2009 - 10 - 23.7896%. If this has a 35.24% correlation with Brand Value, Change in Brand value of HMC = 35.24% x 23.7896% = 8.38%

One issue that is to be reconciled is that the Brand value determining companies employ the calendar year as against the financial year employed in these proceedings under Section 92CA. To resolve this, ^ among other things, the assessee has submitted in its submissions dated 24.12.2013 that the brand value >f HMC has changed in the following manner from 2008 to 2010.

Year	2008	2009	2010
Brand Value (in USD)	4800,000,000	4600,000,000	5000,000,000
Change in Brand Value (USD)		(200,000,000)	400,000,000
Share increase/month		(16,666,667)	33,333,333

*[Total Decrease in Brand Value from 01.04.2009 to 31.12.2009 (9 months)
(150,000,000)*

*Total Increase in Brand Value from 01.01.2010 to 31.02.2010 (3 months)
100,000,000*

*Net decrease in brand value for the F.Y. 2009-10
(50,000,000)*

The above computations are rejected as being overly simplistic and based on erroneous logic as well as the rounded off data of one Brand Value organization (Interbrand) without consideration of the other factual and material facts of the case including a) increase in Market Capitalization and its correlation with increase in Brand value; and b) the creation of enhanced Brand value through increased manufacturing and sales of cars by HMIL

If calendar years are considered, increase in Brand Value of HMC (average of the Millward Brown and Interbrand values) actually increases from F.Y. 2009 to F.Y.2010 - USD 3976.957 millions - USD 3700.622 millions = USD 276.335 millions.

Therefore, increase in the Brand value of HMIL =

Proportion of Sales of HMIL over those of HMC x Change in Brand Value of HMC x USD/INR conversion rate = 4.166% x 276.335 millions x 47.64113 = INR 54,84,49,847.

However, this is only an increase of the Brand value of HMC from the calendar year 2009 to the calendar year 2010 and is NOT the same as the increase in Brand value from F.Y. 2008 - 09 to F.Y. 2009 - 10. This latter value is determined using the correlation coefficient between Market Capitalization (data available for financial years) and Brand values (data available for calendar years). The slight offset between the two types of annual timeframes selected has been adjusted for and smoothed out because a large number of years have been considered and statistical regression tools have been employed and only the correlation percentage between the two values generated from the analyses over 5 years is being adopted.

To recollect (all figures have been rounded off as appropriate):

- Increase in Market capitalization of HMC from 2008-09 to 2009 - 10 = 23.7896%. = USD 18255 millions - USD 14747 millions = USD 3508 millions. This change is approximately 23.7896%

- If this has a positive 35.24% correlation with Brand Value, Change in Brand value of HMC = 35.24% x 23.7896% = 8.38%. This means that if the Market cap of HMC increases by 23.7896%, its Brand value will increase by 8.38%

- This means that the increase in Brand value of HMC = 8.38% of the average brand value position of HMC during the F.Y.2009 - 10. This percentage is to be computed on the Brand value as it stands on 01.04.2009. This Brand value as on 01.04.2009 can be computed using the following proxy: "the weighted average employing 3 months weight of the Brand value as on 31.12.2008 - 9 months weight of the Brand value as on 31.12.2009 = $\frac{9}{12} \times 3857$ millions + $\frac{9}{12} \times 370$ millions = USD 3740 millions.

$8.38\% \times \text{USD } 3740 \text{ millions} = \text{USD } 313.41 \text{ millions} = \text{INR } 1493,12,19,897.$

If the Sales of HMIL and HMC are considered to be the respective drivers of their changes in Brand values, this converts to an increase in Brand value of HMIL of $4.166\% \times \text{INR } 1493,12,19,897 = 62,20,34,587.$

This means that the increase in Brand value of HMIL which needs to be compensated for is determined to be INR 62,20,34,587

14. When the Assessing Officer proposed an ALP adjustment of Rs 62,20,34,857, in the above background, assessee raised a grievance before the DRP but without any success. Accordingly, the said ALP adjustment was made by the Assessing

Officer in the impugned assessment order. Aggrieved, inter alia, by this ALP adjustment, the assessee is in appeal before us.

15. As for the assessment year 2011-12, while the broad approach remained the same and once again the TPO accepted that the AMP spending by the assessee at 1.68% of sales are much less than average of similar expenses by the comparables at 2.16% of sales (at page 15 of the TPO order), the methodology for computing the increase in brand value was more sophisticated. The TPO adopted Spearman's rank correlation coefficient, on the basis of Interbrand valuation, which quantified the adjustment at Rs 253.44 crores. It was in this backdrop that the Assessing Officer proposed an arm's length price adjustment of 253,43,00,000 in respect of compensation that the assessee should have received, from Hyundai Korea, for brand development. Aggrieved by this draft proposal, assessee carried the matter in appeal before the Dispute Resolution Panel but once again without any success. The Assessing Officer thus proceeded to make the ALP adjustment as recommended by the TPO. The assessee is not satisfied and is in appeal before us, inter alia, against the same.

16. We have heard the rival contentions, perused the material on record and duly considered facts of the case in the light of the applicable legal position.

17. The first question that we need to decide is whether the benefit accruing to the HMC Korea, as a result of increased brand value due to sale of Hyundai cars in India by the assessee company, constitutes an international transaction.

18. As we deal with this question, it is necessary to appreciate the fundamental fact that the issue in LG's case (*supra*) before the Special Bench was materially different from the issue in the case before us inasmuch as LG's case dealt with advertisement, marketing and promotion (AMP) expenses incurred by the assessee, which were in excess of similar expenses incurred by the comparables, and an inference was thus drawn that these excessive expenses were incurred for the benefit of the AE which was legal owner of the brand. That was a case in which the special bench had specifically noted that under Article 20 (Advertising, Marketing and Sales Promotion) of the agreement that the assessee company had with its AE, it was provided that **the licensee agrees to provide and make arrangements for advertising, marketing and sales promotion in the licensed territory for LG Products manufactured by the Licensor and those by the Licensee at their cost** and, on this basis, the special bench concluded as follows:

From the above Article it can be seen that it is the assessee who agreed to make arrangements for advertising, marketing and sale promotion in India for the LG products manufactured by it as well as LGK. The cost of such advertising, marketing and sale promotion in India was also agreed to be

exclusively borne by the assessee. It is not only the products manufactured by LGI for which the assessee has undertaken to incur AMP expenses but even for the products manufactured by LGK as well. When we view this Article, it is found that although there are sufficient hints but it falls short of decisively saying that there exists an express agreement for incurring of the AMP expenses in India by the assessee for creating marketing intangibles for and on behalf of the foreign AE.

13. Ex consequenti we hold that there is a 'transaction' between the assessee and the foreign AE for the promotion of brand LG in India, which is legally owned by the latter.

[Emphasis, by underlining, supplied by us]

19. The Special Bench then took note of Hon'ble Delhi High Court decision in the case of **Maruti Suzuki India Ltd Vs ADIT [(2010) 328 ITR 510 (Del)]**, wherein, according to the special bench, it was held that **"if the AMP expenses are incurred by a domestic entity which is an associated enterprise of foreign entity, then there is a requirement on the part of the foreign entity to compensate the domestic entity in respect of the advantage obtained by it in the form of brand building to the extent the expenses are more than what a similarly placed comparable independent domestic entity would have incurred+** The Special Bench then also observed that this decision still holds good in law as it has not been **"overruled, either impliedly or expressly"**. It was on the basis of this analysis that the Special Bench concluded, to quote its own words of majority view, **%the contention of the Id. AR that the judgment of the Hon'ble jurisdictional High Court has been reversed, is jettisoned.+** What follows thus is that unless the expenses incurred by the assessee on its AMP are excessive vis-à-vis what similarly placed comparables would have incurred, according to the special bench, then, to that extent, the foreign AE had an obligation to compensate the assessee company for the AMP expenses.

20. In sharp contrast to this position in LG's case, in the present case, it is an undisputed position that **%the percentage of AMP expenses as a proportion of net sales is not an unreasonable high figure+** and that **%the arguments of the assessee that there is no excess over and above a market benchmark average in this financial year is accepted+** There were some reservations on the data submitted by the assessee in the assessment year 2009-10 for want of complete information, but then in the subsequent two assessment years, i.e. 2010-11 and 2011-12, the TPO has, upon examining requisite details, accepted the submission based on the same data on the same comparables.

21. Clearly, therefore, the facts in the case of LG's special bench decision are materially different and the TPO cannot thus derive any advantage from LG's special

bench decision. As a matter of fact, if the criterion laid down in LGs case is to be adopted, there cannot at all be any justification for making impugned ALP adjustment on account of brand promotion.

22. It is also important to bear in mind the fact that in the present case, the emphasis is all along on the benefit accruing to the parent company, on account of increased brand valuation, as a result of cars being sold by the assessee company in India, and not as a result of conscious brand promotion by the assessee company. The trigger for the impugned ALP adjustment is not the expense incurred by the assessee company, or any efforts made by the assessee company, for brand building for its principal, but the mere fact of the sale of cars made by the assessee company. No services are thus rendered by the company, unlike, for example, in LGs case where brand building was due to conscious and focused efforts of the Indian assessee company to do so. Yet, the case of the TPO is that the assessee should be compensated for the increase in brand valuation, proportionate to sale of cars by the assessee company vis-à-vis the global sale of cars of that brand, as this increase in the brand valuation is, to that extent, due to sale of cars by the assessee company.

23. A lot of emphasis is laid down by the learned counsel on the fact that even if bright line test, as laid down by the Special Bench decision in LGs case (supra), is to be adopted, no AMP adjustment is required to be made in this case. However, as we have seen in the foregoing discussion, neither the ALP adjustment is made, strictly speaking, in respect of the AMP expenses, nor, for that purpose, bright line test holds good in law anyway- as was specifically held by Honble Delhi High Court in the case of **Sony Ericsson Mobile Communications India Pvt Ltd [(2015) 374 ITR 118 (Del)]**. Nothing, therefore, turns on Special Benchs decision in LGs case (supra), which, in any event, is no longer good law in this respect.

24. As clarified by Honble Delhi High Court, in Sony Ericsson's case (supra), its earlier judgment in the case of Maruti Suzuki decision (supra), in view of subsequent legal developments, including the judicial observations of Honble Supreme Court on the said judgment, does not hold good in law either. To this extent also, the stand of the Special Bench in LGs case (supra) stands reversed now.

25. The legal arguments relied upon by the learned counsel on satisfying the bright line test, as also by the authorities below on the legal validity of foundational basis of the impugned addition, have thus no bearing on the decision on correctness of the impugned addition for brand promotion fees. To this extent, the legal analysis by both the parties does not meet our approval. There are, however, other issues raised by the learned representatives which, in our humble view, have merits worth being accepted. We will turn to those issues in a little while.

26. Let us, for the time being, now come back to the question as to whether the benefit accruing to Hyundai Korea, as a result of increased brand value due to sale of Hyundai cars in India by the assessee company, is an international transaction. It has been contention of the assessee all along that it does not constitute an international transaction.

27. We must bear in mind the fact that the short case of the revenue is that simply because the cars are sold by the assessee, the brand gets more visibility, and this visibility results in greater brand value of the Hyundai Korea. It is not the case of the revenue that such an accretion to brand value is on account of any conscious efforts of the assessee to this end- such as, for example, in the case of advertising, marketing and sales promotion. A lot of emphasis is placed on the fact that if the assessee, instead of using Ford name in the name of each of its brand of cars manufactured, was to use a name owned by the assessee, the advantage of adding value to a brand, as a result of sale of cars manufactured by the assessee, would have gone to the assessee, rather than going to the AE. It is this arrangement, for the benefit of the AE, which is stated to be international transaction.

28. The difference in these two kind of triggers to accretion in brand value is that while AMP is a conscious effort and an activity for achieving that goal, in case of brand building by increased market in India is by sales *simplicitor* is a subliminal exercise and by-product of the economic activity of selling the products in the Indian market.

29. There are two basic aspects of this arrangement being an international transaction- first, what is the true nature, and proximate cause, of this arrangement about the use of foreign brand name- is it a case of using foreign brand name to promote the brand name, or to benefit from the reputation that such a brand name; and- second, what is the scope of definition of international transaction under the Indian transfer pricing legislation, and whether this arrangement fits into the same.

30. To begin with, the question that we must ask ourselves is whether use of Hyundai name on the vehicles manufactured by the assessee is primarily a privilege of the assessee, for the benefit of itself- as an effective tool of marketing the products., or is it, as is the case of the revenue, essentially an obligation of the assessee, triggered by the benefit of its AE.

31. It is an undisputed position that the foreign AE owns a valuable brand, i.e. Hyundai, and this brand has a certain degree of respect and credibility all over the globe- including, of course, in the Indian market. When assessee uses this brand name in the name of the models of vehicles manufactured by the assessee, it does indeed amount to an advantage to the assessee. Let us put it like this. If the assessee makes the same car and markets it in the Indian market, without any

established brand name, the acceptability of the car by the Indian consumer will be little less vis-à-vis the situation in which the car is marketed with the foreign brand name. Any other view of the matter would mean that the foreign brand has no value- which is admittedly not the case. The use of Hyundai brand name in the cars manufactured by the assessee thus does indeed amount to a benefit to the assessee. In that sense, the use of brand name owned by the foreign AE is a privilege, a marketing compulsion and of direct and substantial benefits to the assessee.

32. The obligation of the assessee to use the brand name owned by the assessee is, therefore, not solely and proximately driven by the benefits to the AE, owning the brand name. The technology owned by the AE abroad is in the field of motor vehicles, and, with a view to ensure that the AE, owning this technology- which owns the brand name too, continues to be identified with the products manufactured with the use of its technology, it is a common commercial practice, and quite understandable a commercial practice too, that the use of AE's brand name in the name of motor vehicle is made mandatory. Such a clause in the technology use agreement is essentially with a view to protect the intellectual property owned by the foreign AE, and, even in arm's length transaction, fully justified. This business practice is fully justified on the grounds of commercial expediency, which inherently operates *de hors* the compulsions of intra AE relationship of the AEs- the impact of which is sought to be neutralized by the transfer pricing legislation.

33. Ironically, however, there can never be a comparable controlled price input for this kind of a transaction, because, the moment use of an intangible like this is involved, the entities entering into the transactions will become AEs under section 92A(2)(g) and, being a transaction between the AEs, the transaction will cease to be a valid input. For the sake of completeness, we may mention that, for the purposes of sub-section (1), two enterprises shall be deemed to be associated enterprises if, at any time during the previous year, if, *inter alia*, the manufacture or processing of goods or articles or business carried out by one enterprise is wholly dependent on the use of know-how, patents, copyrights, trade-marks, licences, franchises or any other business or commercial rights of similar nature, or any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process, of which the other enterprise is the owner or in respect of which the other enterprise has exclusive rights+.

34. Having held so, however, we must recognize the fact that the use of brand name, owned by the AE, in the motor vehicles manufactured by the assessee does amount to a benefit to the AE of the assessee, an incidental benefit thought, in the sense that increased visibility to this trade name does contribute to increase in brand valuation of the brand name. The question really is whether such an incidental benefit to the AE, even if there be any, can be treated as an international transaction under the Indian transfer pricing legislation.

35. Let us now turn to Section 92 B, which defines the expression international transaction as follows:

92B - Meaning of international transaction

(1) For the purposes of this section and sections 92, 92C, 92D and 92E, "international transaction" means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to anyone or more of such enterprises.

(2) A transaction entered into by an enterprise with a person other than an associated enterprise shall, for the purposes of subsection (1), be deemed to be a transaction entered into between two associated enterprises, if there exists a prior agreement in relation to the relevant transaction between such other person and the associated enterprise, or the terms of the relevant transaction are determined in substance between such other person and the associated enterprise.

Explanation: - For the removal of doubts, it is hereby clarified that — (inserted by the Finance Act 2012, though with retrospective effect from 1st April 2002)

(i) the expression "international transaction" shall include—

(a) the purchase, sale, transfer, lease or use of tangible property including building, transportation vehicle, machinery, equipment, tools, plant, furniture, commodity or any other article, product or thing;

(b) the purchase, sale, transfer, lease or use of intangible property, including the transfer of ownership or the provision of use of rights regarding land use, copyrights, patents, trademarks, licences, franchises, customer list, marketing channel, brand, commercial secret, know-how, industrial property right, exterior design or practical and new design or any other business or commercial rights of similar nature;

(c) capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of

marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;

(d) provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service;

(e) a transaction of business restructuring or reorganisation, entered into by an enterprise with an associated enterprise, irrespective of the fact that it has bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date;

(ii) the expression "intangible property" shall include —

(a) marketing related intangible assets, such as, trademarks, trade names, brand names, logos;

(b) technology related intangible assets, such as, process patents, patent applications, technical documentation such as laboratory notebooks, technical knowhow;

(c) artistic related intangible assets, such as, literary works and copyrights, musical compositions, copyrights, maps, engravings;

(d) data processing related intangible assets, such as, proprietary computer software, software copyrights, automated databases, and integrated circuit masks and masters;

(e) engineering related intangible assets, such as, industrial design, product patents, trade secrets, engineering drawing and schematics, blueprints, proprietary documentation;

(f) customer related intangible assets, such as, customer lists, customer contracts, customer relationship, open purchase orders;

(g) contract related intangible assets, such as, favourable supplier, contracts, licence agreements, franchise agreements, non-compete agreements;

(h) human capital related intangible assets, such as, trained and organised workforce, employment agreements, union contracts;

(i) location related intangible assets, such as, leasehold interest, mineral exploitation rights, easements, air rights, water rights;

(j) goodwill related intangible assets, such as, institutional goodwill, professional practice goodwill, personal goodwill of professional, celebrity goodwill, general business going concern value;

(k) methods, programmes, systems, procedures, campaigns, surveys, studies, forecasts, estimates, customer lists, or technical data;

(l) any other similar item that derives its value from its intellectual content rather than its physical attributes.'

36. As a plain reading of Section 92B(1) would show, an international transaction can be between two or more AEs, at least one of which should be a non-resident, and it can be of the following types:

- in the nature of purchase, sale or lease of tangible or intangible property,
- in the nature of provision of services,
- in the nature of lending or borrowing money, or
- in the nature of any other transaction having a bearing on the profits, income, losses or assets of such enterprises

37. An international transaction, in terms of the provisions of Section 92B, shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to anyone or more of such enterprises, but then this aspect of the matter is not really relevant because it is not a case of allocation of, apportionment of, or contribution to, any costs or expenses in connection with a benefit, service or facility. We need not, therefore, deal with this aspect of the matter in much detail. The same is the situation so far as the transactions in the nature of ~~lending~~ lending or borrowing of money included in the definition under section 92B, are concerned. There is no dealing in money in the present case, and, therefore, this limb of the definition is not at all relevant either.

38. Coming back to the basic definition under section 92B, so far as intangibles are concerned, the relevant transaction, covered by the definition of international transactions, are only transactions of purchase, sale or lease of intangible properties. The brand name is an intangible but then all that definition deals with is sale, purchase or lease of intangibles, and there is no purchase, sale or lease of intangibles in this case at all. What is being claimed to be an international transaction does deal with an intangible, but it deals with increase in the value of the intangible as a by-product of the business model employed by the assessee and the AE and this increase in value is not on account of sale, purchase or lease of intangible. This part of the definition, by no stretch of logic, has any application on the facts of this case. Section i (b) to Section 92 B does add that the expression international transaction shall include the purchase, sale, transfer, lease or use of intangible property, including the transfer of ownership or the provision of use of rights regarding land use, copyrights, patents, trademarks, licences, franchises, customer list, marketing channel, brand, commercial secret, know-how, industrial property right, exterior design or practical and new design or any other business or commercial rights of similar nature+ but even under this, what appears to be, extended definition, the accretion to the value of intangibles is not covered. As we say, we must reiterate that so far as use of brand name under the technology agreement is concerned, the agreement has been examined by the TPO and it is not even the case of the TPO that the consideration paid for the transactions flowing from this agreement is not an arm's length consideration. The arrangement under the technology use agreement, which permits the assessee and binds the assessee to use the brand name of the AE on the products manufactured by the assessee, has been specifically held to be an arm's length transaction. An aspect covered by this agreement, therefore, cannot be subject matter of yet another benchmarking exercise. All that is to be seen is that an accretion to the value of brand name owned by the assessee, on the facts and in the circumstances of this case, amounts to an international transaction.

39. Undoubtedly, provision for services is included in the definition of international transaction under section 92B, but then accretion in brand value due to use of foreign AEs brand name in the name of assessee's products cannot be treated as service either. It is not that the brand name owned by the AE is used in the name of the assessee's products as a service to the AE; it is, as we have seen in our discussions earlier in this order, included as a privilege, a marketing compulsion and of direct and substantial benefits to the assessee+. A privilege to the assessee cannot be a service by the assessee.

40. In any event, a service has to be conscious activity and it cannot be a subliminal exercise- as is the impact on brand value in this case. A service, by definition, is an act of helping, or doing something on behalf of, someone. A passive exercise cannot be defined as a service. Every benefit accruing to an AE, as a result of dealing with another AE, is not on account of service by the other AE. What I benchmarked is not the accrual of benefit but rendition of service. All benefits are

not accounts or services by someone, just as all services do not result in benefits to the parties. The expressions benefit and service have different connotations, and what is truly relevant, for the purpose of definition of international transaction in Indian context, is service not the benefit. There is no rendition of service in the present context.

41. Of course, from the point of view of determination of arm's length price, mere rendition of service is also not sufficient; it should be intended to result in such a benefit as an independent enterprise would pay for. While on this aspect of the matter, we may usefully refer to discussions on special consideration for intra group services, in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. These discussions note that there are two fundamental issues with respect to the intra group services- first, whether intra group services have indeed been provided, and, second- if the answer to the first question is in positive, that charge to these services should be at an arm's length price. Dealing with the first question, which is relevant for the present purposes, these Guidelines (2010 version) state as follows:

7.6 Under the arm's length principle, the question whether an intra-group service has been rendered when an activity is performed for one or more group members by another group member should depend on whether the activity provides a respective group member with economic or commercial value to enhance its commercial position. This can be determined by considering whether an independent enterprise in comparable circumstances would have been willing to pay for the activity if performed for it by an independent enterprise or would have performed the activity in-house for itself. If the activity is not one for which the independent enterprise would have been willing to pay or perform for itself, the activity ordinarily should not be considered as an intra-group service under the arm's length principle.

42. In the present case, however, since no services are performed, the discussion about benefit of the services is academic. We have referred to the above discussions in the OECD Guidelines just to highlight the fact that even in situations in which benefit test is specifically set out in the definition of international transaction, the determination of arm's length price of a service has two components- first, of rendition of service; and- second, of benefit accruing from such services. When the first condition is not satisfied, as in the present case, the matter rests there, and there is no question of benchmarking the benefit in isolation. In our considered view, an incidental benefit accruing to an AE, therefore, cannot be benchmarked unless it is result of a specific service by the assessee.

43. That takes us to last component of definition of international transaction under section 92 B. This refers to a transaction in the nature of any other transaction having a bearing on the profits, income, losses or assets of such enterprises. An accretion in the brand valuation of a brand owned by the AE does not result in profit, losses, income or assets of the assessee company, and it cannot, therefore, result in an international transaction *qua* the assessee. Unless the transaction is such that it

affects profits, losses, income or assets of both the enterprises, it cannot be an international transaction between these two enterprises. If the assets of one of the enterprises are increased unilaterally, without any active contribution thereto by the other enterprise, such an impact on assets cannot, in our humble understanding, amount to an international transaction. The accretion in brand value of the AE's brand name is not on account of costs incurred by the assessee, or even by its conscious efforts, and it does not result in impact on income, expenditure, losses or assets of the assessee company. It is not, therefore, covered by the residuary component of definition of international transaction either.

44. As for the emphasis placed by the learned Departmental Representative, as also by the authorities below, on the exhaustive definition of intangibles in Explanation to Section 92B, we may only reiterate that this definition would have been relevant only in the event of there being any transaction in the nature of sale, purchase or lease of intangible assets but then, it is not even the case of the revenue, that there was any sale, purchase or lease of intangibles. In view of these discussions, as also bearing in mind entirety of the case, we are of the considered view that the accretion of brand value, as a result of use of the brand name of foreign AE under the technology use agreement- which has been accepted to be an arrangement at an arm's length price, does not result in a separate international transaction to be benchmarked. The impugned ALP adjustments of Rs 54,15,28,903, Rs 62,20,34,587 and Rs 253,44,00,000, for the assessment years 2009-10, 2010-11 and 2011-12 respectively, must, therefore, stand deleted. We hold so. Grievance of the assessee, with respect to ALP adjustments on account of accretion in brand value of the AE due to its use by the assessee, is thus upheld.

45. So far as the assessment year 2009-10 is concerned, ground no. 2 in the appeal filed by the assessee pertain to the above transfer pricing controversy. Ground no. 2 is thus allowed.

46. We may also add that ground no.1 in the assessee's appeal for the assessment year 2009-10 is general in nature and it does not call for any specific adjudication.

Tax withholding obligation from interest payments to Mauritian entities

47. In ground no. 3.1, the assessee is aggrieved of the disallowance of Rs 37,33,72,396 made by the Assessing Officer under section 40(a)(i) in respect of interest payment to HSBC (Mauritius) Ltd and Standard Chartered Bank (Mauritius) Limited. This issue is also relevant to the other assessment years but we shall take up the facts and figures with respect to the assessment year 2009-10 and the appeal filed by the assessee.

48. The relevant material facts, in brief, are as follows. The assessee has taken certain loans from two Mauritius based entities, namely HSBC (Mauritius) Ltd (HSBC-M, in short) and Standard Chartered Bank (Mauritius) Limited (SCB-M, in

short). It is in respect of these loans that the assessee paid interest said to be aggregating to Rs 37,33,72,296. The assessee was of the view that in the light of the provisions of article 11 of India Mauritius DTAA, the interest on these loans is not taxable in India. Accordingly, no tax was deducted at source. However, the Assessing Officer did not agree with the stand of the assessee. He took note of the fact that the related agreements were signed in India, at local offices of these banks affiliates, and the related discussions also took place there, the interest income was taxable in India. The AO further observed that %since the entire transaction has been carried out in Chennai, exchanging copies of agreement through the fax facility, it can be reasonably concluded that overseas bank transacted through the permanent establishment in Chennai and hence income accrued in Chennai+ and that %these local officials stood as guarantors for the transaction+. It was also noted that the %Standard Chartered Bank Chennai stood as a guarantee for the transaction between Hyundai Motor India Limited and Standard Chartered Bank Mauritius, which establishes the fact that there is a permanent establishment+It was in this backdrop that the Assessing Officer concluded that the assessee should have deducted tax at source from these interest payments in India. When the proposed, inter alia, this disallowance in the draft order, assessee raised the grievance before the DRP but without any success. The DRP conformed confirmed the stand of the Assessing Officer, and observed as follows:

We have considered the facts of the case. As regards Standard Chartered and HSBC banks we agree with the AO that the local branches of these banks acted as agent PE of the foreign office. It is also worth noticing that neither Standard Chartered nor HSBC is primarily a Mauritius based bank. The Mauritius subsidiaries have been interpolated just to avail the benefits of the DTAA. It is doubtful as to whether the Mauritius subsidiary of the group can be considered as bank and whether they are the beneficial owner of the interest received. In such circumstances the onus was on the assessee to establish that the transactions actually took place in Mauritius. Nothing of this sort has been established. It is apparent from the discussion in the AOs order that the entire transaction was carried out from India and the Mauritius subsidiary of these banks were like name lenders. The transactions were actually carried out in India on behalf of the parent by the local branches. We therefore agree with the AO that DTAA benefit will not be available to the interest income of HSBC and Standard Chartered. As regards the objection that the assessee was not allowed an opportunity to cross examine the bank employees etc, we find that the primary onus was on the assessee to establish that the entire transaction had taken place outside India and negotiations were directly with the foreign lenders. This has not been established by the assessee. We therefore confirm the disallowance as regards the interest paid to Standard Chartered and HSBC banks.

49. Accordingly, the Assessing Office proceeded with the above disallowance. The assessee is aggrieved and is in appeal before us.

50. We have heard the rival contentions, perused the material on record and duly considered facts of the case in the light of the applicable legal position.

51. We consider it appropriate to first set out the relevant provisions of the India Mauritius Double Taxation Avoidance Agreement [(1984) 146 ITR (St) 214], as they stood at the material point of time, which are as follows:

ARTICLE 5- PERMANENT ESTABLISHMENT

1. For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of the enterprise is wholly or partly carried on.

2. The term "permanent establishment" shall include-

- (a) a place of management;
- (b) a branch;
- (c) an office;
- (d) a factory;
- (e) a workshop;
- (f) a warehouse, in relation to a person providing storage facilities for other;
- (g) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources;
- (h) a firm, plantation or other place where agricultural, forestry, plantation or related activities are carried on;
- (i) a building site or construction or assembly project or supervisory activities in connection therewith, where such site, project or supervisory activity continues for a period of more than nine months.

3. Notwithstanding the preceding provisions of this article, the term "permanent establishment" shall be deemed not to include:

- (a) the use of facilities solely for the purpose of storage or display of merchandise belonging to the enterprise;
- (b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage or display;
- (c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;
- (d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or for collecting information for the enterprise
- (e) the maintenance of a fixed place of business solely-
 - (i) for the purpose of advertising,
 - (ii) for the supply of information,
 - (iii) for scientific research, or
 - (iv) for similar activities

which have a preparatory or auxiliary character for the enterprise.

4. Notwithstanding the provisions of paragraphs (1) and (2) of this article, a person acting in a Contracting State for or on behalf of an enterprise of the other Contracting State [other than an agent of an independent status to whom the provisions of paragraph (5) apply] shall be deemed to be a permanent establishment of that enterprise in the first-mentioned State if :

- (i) he has and habitually exercises in that first-mentioned State, an authority to conclude contracts in the name of the enterprise, unless his activities are limited to the purchase of goods or merchandise for the enterprise ; or
- (ii) he habitually maintains in that first-mentioned State a stock of goods or merchandise belonging to the enterprise from which he regularly fulfils orders on behalf of the enterprise.

5. An enterprise of a Contracting State shall not be deemed to have a permanent establishment in the other Contracting State merely because it carries on business in that other State through a broker, general commission agent or any other agent of an independent status, where such persons are acting in the ordinary course of their business. However, when the activities of such an agent are devoted exclusively or almost exclusively on behalf of that enterprise, he will not be considered an agent of an independent status within the meaning of this paragraph.

6. The fact that a company, which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other Contracting State (whether through a permanent establishment or otherwise) shall not, of itself, constitute either company a permanent establishment of the other.

ARTICLE 7- BUSINESS PROFITS

1. The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment.

2. Subject to the provisions of paragraph (3) of this article, where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the profits which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment. Where the correct amount of profits attributable to a permanent establishment cannot be readily determined or the determination thereof presents exceptional difficulties, the profits

attributable to the permanent establishment may be estimated on a reasonable basis.

3. In determining the profits of a permanent establishment, there shall be allowed as deductions expenses which are incurred for the purposes of the business of the permanent establishment including executive and general administrative expenses so incurred, whether in the State in which the permanent establishment is situated or elsewhere.

4. No profits shall be attributed to a permanent establishment by reason of the mere purchase by that permanent establishment of goods or merchandise for the enterprise.

5. For the purposes of the preceding paragraphs, the profits to be attributed to the permanent establishment shall be determined by the same method year by year unless there is good and sufficient reason to the contrary.

6. Where profits include items of income which are dealt with separately in other articles of this Convention, then the provisions of those articles shall not be affected by the provisions of this article.

ARTICLE 11- INTEREST

1. Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, subject to the provisions of paragraphs 3 and 4 of this Article, such interest may also be taxed in the Contracting State in which it arises and according to the laws of that State.

3. Interest arising in a Contracting State shall be exempt from tax in that State provided it is derived and beneficially owned by:

(a) the Government or a local authority of the other Contracting State;

(b) any agency or entity created or organised by the Government of the other Contracting State; or

(c) any bank carrying on a bona fide banking business which is a resident of the other Contracting State.

4. Interest arising in a Contracting State shall be exempt from tax in that Contracting State to the extent approved by the Government of that State if it is derived and

beneficially owned by any person (other than a person referred to in paragraph 3) who is a resident of the other Contracting State provided that the transaction giving rise to the debt-claim has been approved in this regard by the Government of the first mentioned Contracting State.

5. The term "interest" as used in this Article means income from debt-claims of every kind whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and, in particular, income from Government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures. Penalty charges for late payment shall not be regarded as interest for the purpose of this Article.

6. The provisions of paragraphs 1, 2, 3 and 4 shall not apply if the recipient of the interest, being a resident of a Contracting State, carries on business in the other Contracting State in which the interest arises, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the debt-claim in respect of which the interest is paid is effectively connected with such permanent establishment/or fixed base. In such case, the provisions of Article 7 or Article 14, as the case may be, shall apply.

7. Interest shall be deemed to arise in a Contracting State when the payer is that Contracting State itself, a political sub-division, a local authority or a resident of that State. Where, however, the person paying the interest, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment in connection with which the indebtedness on which the interest is paid was incurred, and such interest is borne by that permanent establishment, then such interest shall be deemed to arise in the Contracting State in which the permanent establishment is situated.

8. Where, by reason of a special relationship between the payer and the recipient or between both of them and some other person, the amount of the interest paid, having regard to the debt-claim for which it is paid, exceeds the amount which would have been agreed upon by the payer and the recipient in the absence of such relationship, the provisions of this article shall apply only to the last-mentioned amount. In that case, the excess part of the payments shall remain taxable according to the law of each Contracting State, due regard being had to the other provisions of this Convention 6. The provisions of paragraphs (1), (2), (3) and (4) shall not apply if the recipient of the interest, being a resident of a Contracting State, carries on business in the other Contracting State in which the interest arises, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the debt-claim in respect of which the interest is paid is effectively connected with such permanent establishment or fixed base. In such case, the provisions of article 7 or article 14, as the case may be, shall apply.

7. Interest shall be deemed to arise in a Contracting State when the payer is that Contracting State itself, a political sub-division, a local authority or a resident of that State. Where, however, the person paying the interest, whether he is a resident of a

Contracting State or not, has in a Contracting State a permanent establishment in connection with which the indebtedness on which the interest is paid was incurred, and such interest is borne by that permanent establishment, then such interest shall be deemed to arise in the Contracting State in which the permanent establishment is situated.

8. Where, by reason of a special relationship between the payer and the recipient or between both of them and some other person, the amount of the interest paid, having regard to the debt-claim for which it is paid, exceeds the amount which would have been agreed upon by the payer and the recipient in the absence of such relationship, the provisions of this article shall apply only to the last-mentioned amount. In that case, the excess part of the payments shall remain taxable according to the law of each Contracting State, due regard being had to the other provisions of this Convention.

52. We find that there is no dispute about the fact that both the lender banks belong to MNEs which have global presence all over the world and that the lending was done by the Mauritius based entities, which are tax residents in Mauritius, and that the funds lent by them belonged to the respective entities. The case of the revenue is confined to the claim that since there was some ground work done by the local affiliates of these lenders in India and since these local affiliates based in India stood as guarantors to the borrowings by the assessee, the interest income should be deemed to have accrued to the Indian PEs of such Mauritius based lenders.

53. This claim of the revenue is, however, incorrect for more reasons than one.

54. As a plain look at the definition of fixed place permanent establishment, under article 5(1) of Indo Mauritius tax treaty would show, permanent establishment would mean a fixed place of business through which the business of the assessee is wholly or partly carried on. There is nothing more than mention about affiliates of the global MNE group to which the SCB-M and HSBC-M belong, but that per se cannot lead to the conclusion that SCB-M and HSBC-M had PE in India. As regards the existence of Agency PE, as is obliquely suggested by the DRP, it is important to bear in mind the fact that it is a condition precedent that either such an agent **has and habitually exercises in that first-mentioned State, an authority to conclude contracts in the name of the enterprise, unless his activities are limited to the purchase of goods or merchandise for the enterprise** or **he habitually maintains in that first-mentioned State a stock of goods or merchandise belonging to the enterprise from which he regularly fulfils orders on behalf of the enterprise**. In the present case, at best first condition comes into play and it cannot be revenue's case that the Chennai affiliate office has, and it habitually exercises, the authority to conclude contracts in the name of the Mauritian affiliates because in such a case there would not have even been need for the contacts to be signed by the Mauritian entities as is the undisputed factual position in the present case. A plain look at Article 5(4) and Article 5(5) of the applicable treaty would show, the DAPE can come into play only in a situation in which an agent acts on

behalf of the principal in the other contracting state, in the ordinary course of their business, when the activities of such an agent are devoted exclusively or almost exclusively on behalf of that enterprise, and when the agent has and habitually exercises authority to conclude the contracts in the name of enterprise. It is, and it cannot be, anybody's case that Standard Chartered Bank Chennai branch was acting exclusively, or almost exclusively, for SCB- Mauritius, or that SCB-Chennai has, and habitually exercises authority to conclude contracts on behalf of SCBN-M. The sweeping observations made by the authorities below are devoid of any legally sustainable merits. It is not the case of the revenue that the existence of the PE is because of any other specific deeming fiction or under any specific part of the definition which justifies the conclusion that mere presence of these affiliates in India, and the fact of some role being played by these affiliates, results in creation of PE in India and the income being attributed to such PE. In any event, having perused the definition of PE as reproduced earlier in this order, we find that if at all the HSBC-M and SCB-M can be said to have PE in India, it can only be under the basic definition under article 5(1), i.e. what is popularly known as fixed place PE. In terms of the provisions of art. 5(1), i.e., the basic rule a PE is said to exist in the other Contracting State when an enterprise of one of the Contracting States has a fixed place of business in that other Contracting State, through which business is carried out wholly or partly. An analysis of this definition shows that there are three criteria embedded in this definition- physical criterion i.e., existence of physical location, subjective criterion i.e., right to use that place, and functionality criterion i.e., carrying out of business through that place. It is only when these three conditions are satisfied, a PE under the basic rule can be said to have come into existence.

55. As observed by a Co-ordinate Bench in the case of Western Union Financial Services Inc. vs. ADIT (2007) 104 ITD 34 (Del), "a PE should project in the foreign enterprises in India (the other Contracting State)". In the case of CIT vs. Visakhapatnam Port Trust (1983) 144 ITR 146 (AP), Hon'ble Andhra Pradesh High Court, after an elaborate survey of worldwide judicial precedents and technical literature on this issue, had observed that, "in our opinion, the words postulate the existence of substantial element of enduring or permanent nature of a foreign enterprise in another country which can be attributed to a fixed place of business in that country". Their Lordships further added that "it should be of such a nature that it would amount to a virtual projection of foreign enterprise of one country into the soil of another country". Incidentally, the treaty definition of basic clause, which came up for consideration of their Lordships, was exactly the same as in the case before us.

56. Coming back to the three tests in the definition of PE, the physical test, i.e., place of business test, requires that there should be a physical location at which the business is carried out. However, mere existence of a physical location is not enough. This location should also be at the disposal of the foreign enterprise and it must be used for the business of foreign enterprise as well. A place of business should be at the disposal of the foreign enterprise for the purpose of its own

business activities. This place has to be owned, rented or otherwise at the disposal of the assessee, and a mere occasional factual use of place does not suffice. This approach is accepted by a Special Bench of this Tribunal in the case of Motorola Inc. vs. Dy. CIT (2005) 95 ITD 269 (Del)(SB) wherein, inter alia, it was observed as follows:

".....The OECD Commentary on Double Taxation Conventions refers to a fixed place as a link between the place of business and a specific geographical point. It has to have certain degree of permanence. It is emphasized that to constitute a fixed place of business the foreign enterprise must have at its disposal certain premises or part thereof. Philip Baker, in his commentary on Double Taxation Conventions (Third Edition), states that the fixed place is very much that of a physical location, i.e., one must be able to pinpoint to a physical location at the disposal of the enterprise through which the business is carried on. On the other hand, possession of a mailing address in a State without an office, telephone listing or bank account-has been held not to constitute a PE. Further, the fixed place of business need not be owned or leased by the enterprise provided it is at the disposal of the enterprise in the sense of having some right to use the premises for the purposes of its business and not solely for the purpose of project undertaken on behalf of the owner of the premises."

(Emphasis supplied by us now).

57. It is thus necessary that, in order to give a positive finding about existence of the PE, not only that there should be a physical location through which the business of the foreign enterprise is carried out, but also such a place should be at the disposal of the foreign enterprise in the sense that foreign enterprise should have some sort of a right to use the said physical location for its own business.

58. The third and final test for existence of PE under the basic rule is the functionality test i.e., the fixed place of business should be used for the purposes of business of the foreign enterprise. As observed by the Special Bench of this Tribunal in the case of Motorola Inc. (supra), such a use should not be confined to mere doing the work for owner of the enterprise owning that physical location and must extend to carrying on of the business of the foreign enterprise. The business carried out at that place should be such as to amount to, as was observed by Honble Andhra Pradesh High Court in the case of Visakhapatnam Port Trust (supra), "virtual projection of enterprise of one country into soil of another country". The PE must project the foreign enterprise of which it is claimed to be PE. It is in this sense that the business must be carried on at the physical location in the other country. It is also important to bear in mind that when such a physical location has come into play as an end result of business having been carried out, such as a barge in territorial waters of the other country upon having given such barges on hire to a resident of the other country. in the case of a person who is engaged in the business of giving barges on hire, the business cannot be said to have been carried

out on such place qua that business activity. It was so held by a Co-ordinate Bench in the case of Addl. Director of IT (International Taxation) vs. Valentine Maritime (Mauritius) Ltd. [(2010) 130 TTJ (Mumbai) 417] wherein it was held that that "by no stretch of logic, when an assessee is in the business of hiring out the barges, a barge so hired out cannot be viewed as a place of carrying on its business, which, as we understand, is limited to, qua that barge, the barge having been so hired out".

59. In the light of the above legal position, with which we are in considered agreement, when we examine the facts of the present case, we donot find that the mere occasional use of the office of Indian affiliate, even if there be any, cannot result in PE of the foreign companies coming into existence. It is also not the case of the revenue that the three Mauritian companies, to which interest payments have been made, had any right to use the offices of its affiliates in Chennai. Therefore, even if it is assumed that there was indeed a place at which the Mauritian entities carried on any work, it cannot be treated as PE of these Mauritian companies, under the basic PE clause under article 5(1), unless it is demonstrated that these entities had any right to use these facilities at Chennai. As regards the functionality tests, i.e test regarding projection of the foreign enterprise, there is nothing to demonstrate that there was any projection of these Mauritian entities in India. The three tests, i.e. physical criterion i.e., existence of physical location, subjective criterion i.e., right to use that place, and functionality criterion i.e., carrying out of business through that place must be satisfied so as to result in creation of PE under the basic PE clause but none of these tests are satisfied on the facts of the present case. As for the onus to demonstrate the satisfaction of these conditions precedents for existence of PE, as is the settled legal position, this onus lies with the revenue. Of course, the assessee has to comply with the reasonable requisitions for information sought by the revenue, but it is duty of the revenue authorities to demonstrate existence of the PE. As we deal with this aspect of the matter, it is also important to bear in mind the fact that, as observed in Special Bench decision in the case of Motorola Inc. vs. Dy. CIT (2005) 96 TTJ (Del)(SB) 1, "DTAA is only an alternate tax regime and not an exemption regime" and, therefore, "the burden is first on the Revenue to show that the assessee has a taxable income under the DTAA, and then the burden is on the assessee to show that that its income is exempt under DTAA". It is, therefore, revenue to demonstrate as to how PE of the foreign company exists in India The mere presence of affiliate offices in India, of the MNE group to which the HSBC-M and SCB-M belong, cannot lead to the conclusion that there is a PE of HSBC-M and SCB-M. Revenue has thus not discharged its burden. In any event, based on the material before us, there does not seem to be a PE of these entities in India. We are, therefore, unable to approve the case of the revenue on this point.

60. It is also important to bear in mind that the satisfaction of existence of PE under article 5 is not an end in itself. The next thing to examined is whether any part of the income is attributable to PE under article 7. It is so for the simple reason that even if PE is found to exist under article 5, only so much of profits can be brought to tax as are attributable to the assessee. Just because a foreign enterprise has a PE in India, it does not mean that all the profits accruing to the foreign enterprise are

taxable in India, but the manner in which the authorities below have approached the issue in appeal, such an assumption is implicit in their approach. There are no findings in this regard at all. It is important to bear in mind the fact that even when PE is found to exist in India, in order to invoke disallowance under section 40(a)(i), it is to be further shown as to how the interest income belongs to the PE. The mere existence of the PE cannot by itself lead to the conclusion that the interest income belongs to the PE. While on this issue, we may usefully refer to the following observations made by a coordinate bench in the case of ADIT Vs Epcos AG [(2009) 28 SOT 412 (Pune)]:

It is also important to bear in mind that a non-resident company having a PE in India, by itself, does not lead to taxability in India; there must be some profit attributable to such a PE which alone could be taxed in India because of the existence of the PE. When the PE carries on an activity which does not serve overall purpose of the foreign enterprise, or which does not contribute to profits of the enterprise, the existence of such a PE is wholly academic and does not have any tax implications in the source jurisdiction. To that limited extent, there is an inherent contradiction in the OECD approach inasmuch as on one hand PE provides threshold limits for triggering taxation in the source country, on the other hand the existence of the PE is decided *de hors* the activity in the absence of which taxability of profits in the source country cannot be triggered at all. On the face of it, when a PE is not engaged in a critical activity having some contribution to overall profits of the enterprise or a revenue generating activity, the exercise to ascertain whether or not a PE is in existence is a meaningless ritual and an empty formality.

61. Once we find that the provisions of article 5 and article 7 donot come into play, as is the situation in this case, the next thing to be examined is the scope of article 11. Article 11(1) provides that ~~%~~interest arising in a contracting state and paid to the resident of the other contracting state may be taxed in that other state+. In effect thus interest income is not taxable in source jurisdiction but only in residence jurisdiction. There is, of course, a rider in article 15(6) which provides that, *inter alia*, article 11(1) ~~%~~shall not apply if the recipient of the interest, being a resident of a contracting state, carried on business in the other contracting stare in which interest arises, through a permanent establishment situated therein+. The treaty protection of article 11(1) can thus indeed be denied when recipient of interest has a PE in the source country and the business is being carried on through such PE in the source country. As we have seen in our analysis earlier, this condition is clearly not satisfied on the facts of this case.

62. There is more armoury in store for the revenue. It has been emphasized by the Assessing Officer that the Mauritian entities are part of the global MNE groups and the Mauritian companies, as they apprehend, could at best be front companies or conduit companies, not the beneficial owners.

63. Nothing, however, turns on this plea of the revenue. The apprehension of the revenue authorities are once again devoid of any legally sustainable merits. It is not even pointed out by the revenue authorities as to which entity is the beneficial owner of the interest, and, as such, the SCB-M is acting as conduit for whom. The allegation are vague and unsubstantiated. There is no support whatsoever, save and except for the wild apprehensions of the revenue authorities, that the SCB-M has acted as a conduit. As is elementary in law, such vague allegations and considerations cannot meet any judicial approval. Nobody can be expected to prove a negative, as is the settled legal position in India, and, therefore, these entities cannot be even expected to establish that the beneficial owners of such interest income are not some other group entities. The doubts expressed by the DRP with regard to beneficial owner of the interest income are devoid of any legally sustainable basis. No case has been made out by the revenue for the beneficial owner of interest income being entities other than Mauritian entities in question. In terms of Article 11(3), interest arising in a Contracting State (i.e. India, in this case) shall be exempt from tax in that State (i.e. India) provided it is derived and beneficially owned by, *inter alia*, by any bank carrying on a bona fide banking business which is a resident of the other Contracting State (i.e. Mauritius). There is no dispute that Mauritian entities in question were carrying out banking business in Mauritius, and there is nothing on record to show, or even indicate, that the beneficial owner of interest income were not these Mauritian entities. In addition to this undisputed position, neither a case has been made for existence of any PE nor for business having been carried out through such a PE. All that is established is the presence of some of the affiliates of the MNE group to which the recipient of interest income belongs, and some peripheral role played by such affiliates, but these facts donot establish, or even indicate, existence of the PE. The protection of article 11(1) cannot, therefore, be declined on the facts of the present case. We are, therefore, of the considered view that the income embedded in these interest payments was not taxable in India. Accordingly, the assessee did not have any tax withholding obligations, under section 195, in respect of these payments, and, as a corollary thereto, disallowance under section 40(a)(i) was not justified.

64. In view of the above discussions, as also bearing in mind entirety of the case, we uphold the plea of the assessee and delete the impugned disallowance of Rs 37,33,396 under section 40(a)(i) of the Act.

65. Ground no. 3.1 is thus allowed.

66. In ground no. 3.2, the assessee is aggrieved of the Assessing Officer treating the export incentives on account of Focus Market Scheme and Focus Products scheme, amounting to Rs 19,81,20,560, as income of the year before us.

67. We find that this issue is covered, in favour of the assessee, by a decision of the coordinate bench in assessee's own case for the assessment year 2007-08 wherein the coordinate bench has concluded as follows;

In the case of the assessee, the export incentive towards target plus scheme is bestowed as a reward in order to encourage the accelerating growth in exports. The incentive on target plus scheme is nothing but an entitlement for a duty credit based on incremental exports which should be substantially higher than the general annual export target that is fixed. The incentive on focus market scheme is to offset high freight cost and other externalities to select international market with a view to enhance India's export competitiveness in those countries. It is pertinent to note that the assessee will be entitled to such benefit only after verification of the claim of the assessee by relevant governmental authorities and issuance of licence by such governmental authorities. Therefore, the facts of the assessee's case are similar to the facts decided by the Hon'ble Apex Court cited supra. Therefore, respectfully following the decision of Hon'ble Supreme Court, we hereby hold that the notional income computed by the assessee cannot be treated as taxable income of the assessee during the relevant previous year. However, the same shall be taxed in the previous year in which the assessee has received the licences and derived such income. Thus, this issue is also decided in favour of the assessee.

68. We see no reasons to take any other view of the matter than the view so taken by the coordinate bench in assessee's own case. Respectfully following the same, we uphold the grievance of the assessee. The assessee gets the relief accordingly.

69. Ground no. 3.2 is thus allowed

70. In ground no. 3.3, the assessee is aggrieved of the disallowance of Rs 49,63,29,426.

71. So far as this grievance of the assessee is concerned, the relevant material facts are like this. During the course of assessment proceedings, the Assessing Officer noted that the assessee has worked out an unrealized loss of Rs 49,63,29,426 on purchase of assets in India with the ECB loan of USD 100 million from Export Import Bank of Korea. It was claim of the assessee that section 43A applied only in the context of assets acquired outside India, this loss may be allowed as deduction under section 37(1). It was also pointed out that in the assessment years 2008-09, 2010-11 and 2011-12, the income offered to tax, on the same account, amounting to Rs 16.01 crores, Rs 25.69 crores and Rs 78.79 crores respectively has been accepted. The Assessing Officer did not agree. He relied upon Hon'ble Supreme Court's judgment in the case of CIT Vs Woodward Governor

India Pvt Ltd [(2009) 312 TR 254 (SC)] and held that the loss due to fall in value of foreign exchange cannot be adjusted in the value of asset. He was of the view that this is a notional loss and that too in capital field. He declined to allow the same. Aggrieved, assessee carried the matter before the DRP. In its brief order, the DRP held as follow:

We donot find anything wrong in AO's reliance on the Supreme Court decision in Woodward Governor's case. Merely restatement of the foreign currency loan cannot be considered a business transaction resulting into loss, particularly when no repayment was made during the year. The transaction even then will be capital in nature. Hence, we reject this objection.

72. The Assessing Officer thus proceeded to make the disallowance of Rs 49,63,29,426 aggrieved by which the assessee is in appeal before us.

73. We have heard the rival contentions, perused the material on record and duly considered facts of the case in the light of the applicable legal position.

74. We find that the issue in appeal is squarely covered by a coordinate bench decision in the case of Cooper Corporation Pvt Ltd Vs DCIT [(2016) 159 ITD 165 (Pune)], wherein the coordinate bench, in a very well reasoned and analytical order, has, *inter alia*, observed as follows:

10. The central issue involved in the present case is whether provision for loss in the hands of assessee on account of restatement of outstanding foreign currency loans necessitated by fluctuation in foreign exchange would be allowable as business loss or a loss of capital nature in the facts narrated above. While as per the revenue, the increased liability due to exchange fluctuation correspond with carrying costs of the fixed assets and thus capital in nature, the assessee seeks to submit that the loss is revenue in nature.

10.1 On consideration of facts, it is noticed that certain loans were held in Indian currency in the earlier years. The Assessee entered into an agreement with the lenders to convert the loans in foreign currency equivalents to take advantage of the lower rate of interest rate applicable to later. The assessee has factually demonstrated that the conversion into foreign currency loans have actually benefited the Assessee in terms of saving of interest costs. We also notice that there is no dispute on the fact that the acquisition of capital assets / expansion of projects etc. from the term loans taken are already complete and the assets so acquired have been put to use. As a consequence, the loss occasioned from foreign currency loans so converted is a post facto event subsequent to capital assets having been put to use. We simultaneously notice that there is no adverse finding from the Revenue

about the correctness or completeness of accounts of assessee on the touchstone of section 145 of the Act. In other words, the profits/gains from the business have been admittedly computed in accordance with generally accepted accounting practices and guidelines notified.

10.2 The assessee has inter alia applied AS-11 dealing with effects of the changes in the exchange rate to record the losses incurred owing to fluctuation in the foreign exchange. AS-11 enjoins reporting of monetary items denominated foreign currency using the closing rate at the end of the accounting year. It also requires that any difference, loss or gain, arising from such conversion of the liability at the closing rate should be recognized in the profit & loss account for the reporting period. In the same vain, CBDT notification S.O. 892(E) dated 31-03-2015 referred to also inter alia deals with recognition of exchange differences. The notification also sets out that the exchange differences arising on foreign currency transactions have to be recognized as income or business expense in the period in which they arise subject to exception as set out in Section 43A or Rule 115 of the Income Tax Rules, 1962 as the case may be.

10.3 The contention of the revenue that the loss is only contingent and notional and subsisting has been examined. As per section 209 of the Companies Act, 1956, the Assessee being a company is required to compulsorily follow mercantile system of accounting. S. 211 of the Companies Act, 1956 also, in terms, mandates that accounting standards as applicable is required to be followed while drawing statement of affairs. S. 145 of the Income Tax Act, 1961 similarly casts obligation to compute business income either by cash or mercantile system of accounting. Thus, in view of the various provisions of the Companies Act and Income Tax Act, it was mandatory to draw accounts as per AS 11. Thus, in our considered view, the loss recognized on account of foreign exchange fluctuation as per notified accounting standard AS 11 is an accrued and subsisting liability and not merely a contingent or a hypothetical liability. A legal liability also exists against the assessee due to fluctuation and loss arising therefrom. Actual payment of loss is an irrelevant consideration to ascertain the point of accrual of liability. As a corollary, the revenue has committed error in holding the liability as notional or contingent.

10.4 Copious reference has been made to S. 43A by Assessee as well as revenue. Thus, it would be pertinent to examine the issue on the touchstone of S. 43A of the Act. Section 43A, to the extent relevant in the context, reads as under:

Notwithstanding anything contained in any other provision of this Act, where an assessee has acquired any asset in any previous year from a country

outside India for the purposes of his business or profession and, in consequence of a change in the rate of exchange during any previous year after the acquisition of such asset, there is an increase or reduction in the liability of the assessee as expressed in Indian currency (as compared to the liability existing at the time of acquisition of the asset) at the time of making payment—

(a) towards the whole or a part of the cost of the asset; or

(b) towards repayment of the whole or a part of the moneys borrowed by him from any person, directly or indirectly, in any foreign currency specifically for the purpose of acquiring the asset along with interest, if any,

the amount by which the liability as aforesaid is so increased or reduced during such previous year and which is taken into account at the time of making the payment, irrespective of the method of accounting adopted by the assessee, shall be added to, or, as the case may be, deducted from—

(i) the actual cost of the asset as defined in clause (1) of section 43; or

(ii) the amount of expenditure of a capital nature referred to in clause (iv) of subsection (1) of section 35; or

(iii) the amount of expenditure of a capital nature referred to in section 35A; or

(iv) the amount of expenditure of a capital nature referred to in clause (ix) of subsection (1) of section 36; or

(v) the cost of acquisition of a capital asset (not being a capital asset referred to in section 50) for the purposes of section 48,

and the amount arrived at after such addition or deduction shall be taken to be the actual cost of the asset or the amount of expenditure of a capital nature or, as the case may be, the cost of acquisition of the capital asset as aforesaid:

Provided that where an addition to or deduction from the actual cost or expenditure or cost of acquisition has been made under this section, as it stood immediately before its substitution by the Finance Act, 2002, on account of an increase or reduction in the liability as aforesaid, the amount to be added to, or, as the case may be, deducted under this section from, the

actual cost or expenditure or cost of acquisition at the time of making the payment shall be so adjusted that the total amount added to, or, as the case may be, deducted from, the actual cost or expenditure or cost of acquisition, is equal to the increase or reduction in the aforesaid liability taken into account at the time of making payment

A bare reading of the aforesaid provision of Section 43A, which opens with a non-obstante and overriding clause, would show that it comes into play only when the assets are acquired from a country outside India and does not apply to acquisition of indigenous assets. Another notable feature is that S. 43A provides for making corresponding adjustments to the costs of assets only in relation to exchange gains/ losses arising at the time of making payment. It therefore deals with realised exchange gain/ loss. The treatment of unrealised exchange gain/ loss is not covered under the scope of S. 43A of the Act. It is thus apparent that special provision of S. 43A has no application to the facts of the case. Therefore, the issue whether, the loss is on revenue account or a capital one is required to be tested in the light of generally accepted accounting principles, pronouncements and guidelines etc.

10.5 Before we delineate on the allowability of loss based on generally accepted accountancy principles, it may be pertinent to examine whether the increased liability due to fluctuation loss can be added to the carrying costs of corresponding capital assets with reference to S. 43(1) of the Act. Section 43(1) defines the expression 'actual cost'. As per S. 43(1), actual cost means actual cost of the assets to the assessee, reduced by that portion of the costs as has been met directly or indirectly by any other person or authority. Several Explanations have been appended to S. 43(1). However, the section nowhere specifies that any gain or loss on foreign currency loan acquired for purchase of indigenous assets will have to be reduced or added to the costs of the assets. Thus, viewed from this perspective also, such increased liability cannot be bracketed with cost of acquisition of capital assets save and except in terms of overriding provisions of S. 43A of the Act.

10.6 We also simultaneously note here that the Hon'ble Supreme Court in the case of CIT vs. Tata Iron and Steel Co. Ltd. (1998) 22 ITR 285 held that cost of an asset and cost of raising money for purchase of asset are two different and independent transactions. Thus, events subsequent to acquisition of assets cannot change price paid for it. Therefore, fluctuations in foreign exchange rate while repaying installments of foreign loan raised to acquire asset cannot alter actual cost of assets. The relevant operative para is reproduced hereunder.

"Coming to the question raised, we find it difficult to follow how the manner of repayment of loan can affect the cost of the assets acquired by the assessee.

What is the actual cost must depend on the amount paid by the assessee to acquire the asset. The amount may have been borrowed by the assessee, but even if the assessee did not repay the loan it will not alter the cost of the asset. If the borrower defaults in repayment of a part of the loan, the cost of the asset will not change. What has to be borne in mind is that the cost of an asset and the cost of raising money for purchase of the asset are two different and independent transactions. Even if an asset is purchased with non-repayable subsidy received from the Government, the cost of the asset will be the price paid by the assessee for acquiring the asset. In the instant case, the allegation is that at the time of repayment of loan, there was a fluctuation in the rate of foreign exchange as a result of which, the assessee had to repay a much lesser amount than he would have otherwise paid. In our judgment, this is not a factor which can alter the cost incurred by the assessee for purchase of the asset. The assessee may have raised the funds to purchase the asset by borrowing but what the assessee has paid for it, is the price of the asset. That price cannot change by any event subsequent to the acquisition of the asset. In our judgment, the manner or mode of repayment of the loan has nothing to do with the cost of an asset acquired by the assessee for the purpose of his business. We hold that the questions were rightly answered by the High Court. The appeals are dismissed. There will be no order as to costs. “

Thus, it is evident the variation in the loan amount has no bearing on the cost of the asset as the loan is a distinct and independent transaction as in comparison with acquisition of assets out of said loan amount borrowed. Actual cost of the corresponding fixed asset acquired earlier by utilizing the aforesaid loan will not undergo any change owing to such fluctuation.

10.7 The issue is also tested in the light of provision of S. 36(1)(iii) governing deduction of interest costs on borrowals. As stated earlier, manner of utilization of loan amount has nothing to do with allowability of any expenditure in connection with loan repayment. Both are independent and distinct transactions in nature. Similar analogy can be drawn from S. 36(1)(iii) of the Act which also reinforces that utilization of loan for capital account or revenue account purpose has nothing to do with allowability of corresponding interest expenditure. A proviso inserted thereto by Finance Act, 2003, also prohibits claim of interest expenditure in revenue account only upto the date on which capital asset is put to use. Once the capital asset is put to use, the interest expenditure on money borrowed for acquisition of capital asset is also treated as revenue expenditure. As also noted, S. 43A specifically and categorically calls for adjustments in cost of assets for loss or gain arising out of foreign currency fluctuations in respect of funds borrowed in foreign currency for acquisition of foreign assets. However, the same rationale of a deeming provision of S. 43A cannot be applied to loss or gain arising from foreign currency loss utilized for purchase of indigenous assets. Needless to say, impugned currency fluctuation loss has emanated from foreign currency

loans. Besides AS-11, the claim of exchange fluctuation loss as revenue account is also founded on the argument that the aforesaid action was taken to save interest costs and consequently to augment the profitability or reduce revenue losses of the assessee. The impugned fluctuation loss therefore has a direct nexus to the saving in interest costs without bringing any new capital asset into existence. Thus, the business exigencies are implicit as well explicit in the action of the Assessee. The argument that the act of conversion has served a hedging mechanism against revenue receipts from export also portrays commercial expediency. Thus, We are of the opinion that the plea of the assessee for claim of expenditure is attributable to revenue account has considerable merits.

10.8 Section 145 of the Income Tax Act deals with method of accounting and states that business income inter-alia has to be computed in accordance with cash or mercantile system of accounting. Sub-section (2) thereof authorizes the Central Government to notify accounting standards to be followed for determination of business income. Section 211 of the Companies Act also similarly casts a duty on a company to give a true and fair view of the profit and loss of the company for the financial year. It also requires the company to adhere the accounting standards for preparation of profit in the Profit & Loss Account and the Balance Sheet. A conjoint reading of section 145 of the Act and section 211 of the Companies Act leaves no room for doubt that the Assessee is obliged to follow the accounting standards prescribed to determine business income under the head "business or profession". We notice that the Hon'ble Supreme Court in the case of Woodward Governor India (P) Ltd. (supra) has observed that AS-11 is mandatory in nature. In the light of observations made in Woodward Governor India (P) Ltd. (supra), we are of the view that loss arising on foreign exchange fluctuation loss has been rightly accounted for as a revenue expense in the Profit & Loss account in accordance with accounting fiat of AS-11.

10.9 We find that the decision in the case of Sulej Cotton Mills Ltd. (supra) relied upon by the Ld. Departmental Representative is of no assistance to the Revenue. The Hon'ble Supreme Court therein stated the principle of law that where any profit or loss arises to an assessee on account of depreciation in foreign currency held by him on conversion from another currency, such profit and loss would ordinary be trading loss if the foreign currency held by the assessee on revenue account as trading asset or as a part of circulating capital embargo in business. However, if the foreign currency is held as a capital asset, the loss should be capital in nature. The aforesaid principle of law is required to be applied to the facts of case to determine whether the foreign currency is held by the assessee on revenue account or as a part of circulating capital. In the present case, fluctuation loss inflicted upon the assessee bears no nexus or relation to the acquisition to the assets. The action of the assessee is tied up to its underlying objective i.e. saving in interest costs, hedging its revenue receipts etc. which are undoubtedly on

revenue account. Thus, the loss generated in impugned action bears the character of revenue expenditure. Similarly, decision of the Apex Court in the case of Tata Iron and Steel co. (supra) also weighs in favour of the assessee. We also note that reliance placed by the CIT(A) on Elecon Engineering Co. Ltd. (supra) is misplaced. The decision concerns applicability of S. 43A in the facts of that case and thus clearly distinguishable.

11. For the aforesaid reasons, in the absence of applicability of section 43A of the Act to the facts of the case and in the absence of any other provision of the Income Tax Act dealing with the issue, claim of exchange fluctuation loss in revenue account by the Assessee in accordance with generally accepted accounting practices and mandatory accounting standards notified by the ICAI and also in conformity with CBDT notification can not be faulted. No inconsistency with any provision of Act or with any accounting practices has been brought to our notice. Otherwise also, in the light of fact that the conversion in foreign currency loans which led to impugned loss, were dictated by revenue considerations towards saving interest costs etc. we have no hesitation in coming to the conclusion that loss being on revenue account is an allowable expenditure under S. 37(1) of the Act.

75. We are in considered agreement with the views so expressed by the coordinate bench. Respectfully following the same, we uphold the grievance of the assessee and delete this disallowance of Rs . 49,63,29,426.

76. Ground no. 3.3 is thus allowed.

77. In ground no. 3.4, the assessee has raised a grievance against the Assessing Officer~~s~~ making a disallowance of Rs 3,88,626 of depreciation on account of reduction of capital subsidy granted by SIPCOT form the cost of assets.

78. Learned representatives agree that identical issue, in respect of the assessment year 2007-08, was remitted to the file of the DRP for fresh adjudication on the nature of the subsidy. Whatever are the findings of the DRP for the assessment year 2007-08 will be equally valid for this assessment year as well. We, therefore, remit the matter to the file of the Assessing Officer for examining the matter afresh in the light of those findings of the DRP. While so deciding the matter, the Assessing Officer will give a due opportunity of hearing to the assessee.

79. Ground no. 3.4 is thus allowed for statistical purposes.

80. The assessee has raised an additional ground of appeal that %subsidy received from the Government of Tamilnadu in the form of refund of output VAT is a

capital receipt not chargeable to tax+ and to that extent the stand of the authorities below is incorrect and needs to be vacated.

81. While there cannot indeed be any objection to the appellant raising any new issue before the Tribunal, in view of the decision of Hon'ble Supreme Court in the case of NTPC Ltd Vs CIT [(1998) 229 ITR 383 (SC)], with the consent of the parties, this matter is required to be remitted to file of the Assessing Officer for adjudication de novo on merits, in accordance with the law, by way of a speaking order and after giving a fair and reasonable opportunity of hearing to the assessee. We, therefore, accept the additional ground of appeal but remit the matter to the file of the Assessing Officer for fresh adjudication in the light of above observations. Ordered, accordingly.

82. Additional ground of appeal is thus allowed for statistical purposes in the terms indicated above.

83. The appeal filed by the assessee for the assessment year 2009-10 is thus partly allowed in the terms indicated above.

84. We now turn to the appeal filed by the Assessing Officer for the assessment year 2009-10.

85. Ground no. 1 is general in nature and does not call for any adjudication.

86. In ground no. 2, the Assessing Officer has raised the following grievance:

The DRP erred in deleting the disallowance of provision for warranty of Rs. 111,75,06,775/-. The DRP failed to appreciate the fact that the actual warranty expenses incurred by the assessee are far less than the provision created and the excess provisions are written back at the end of the warranty period. The assessee arrived at the figure of warranty provision by multiplying the provision rate per car which will lead to an absurd inference that each car manufactured by the assessee is liable to be defective. Further this does not reflect the actual warranty expenditure incurred by the assessee over the past several years. The assessee has not satisfied the rationale laid down by the hon'ble Supreme Court in the case of Rotork Control. During the course of assessment proceedings, the Apex Court rationale for incurring such a quantum of warranty expenses have not been brought out. The assessee has not produced details of warranty estimates based on their historical data. Moreover the warranty period is 2 years for domestic and 5 years for exports. Warranty estimates for exports are not known. The assessee has also not produced the details of warranty expenses incurred the earlier years. The assessee has made only a step wise analysis of how warranty provision is

made. Thus assessee company has failed to establish any scientific basis or basis on historic trend for creating warranty provision. Hence the provision is only on ad hoc basis made summarily.

87. As learned representatives fairly agree this issue is now covered by the judgment dated 29th October 2013 in assessee's own case for the assessment year 2002-03. The SLP filed by the revenue, against the said order, also stands dismissed by Hon^{ble} Supreme Court on 28.11.2014. The matter has thus attained finality. In this view of the matter, we confirm the relief granted by the DRP and decline to interfere in the matter.

88. Ground no. 2 is thus dismissed.

89. In ground no. 3, the Assessing Officer has raised the following grievance:

The DRP erred in deleting the disallowance of guarantee charges. Guarantee charges incurred on account of external commercial borrowings are capital in nature and these charges are not in the nature of interest charges.

90. This issue also, as learned representatives agree, stands covered in favour of the assessee by Hon^{ble} Supreme Court's decision in the case of ACIT Vs Akkamamba Textiles Ltd [(1997) 227 ITR 464 (SC)] whereby Their Lordships confirmed the order of Hon^{ble} AP High Court holding that guarantee commission paid to the bank etc for purchase of machinery is a revenue expenditure. In the present case, guarantee charges paid upto the date on which the assets are put to use are capitalized, and post capitalization of assets, the guarantee charges are claimed as revenue expenditure. These payments have been accepted as transactions for arm's length consideration and there are no ALP adjustments in the same. The genuineness of the guarantee commission is not in dispute either. We, therefore, uphold the relief granted by the DRP, by deleting the disallowance of Rs 1,37,37,537, and decline to interfere in the matter.

91. Ground no. 3 is thus dismissed.

92. In ground no. 4, the Assessing Officer has raised the following grievance:

The DRP erred in deleting the disallowance of depreciation claimed on assets used for office purpose. These assets were actually installed in the workstations/car service centers attached to the Regional offices from where service income is generated. Though factory licenses have been obtained in respect of the said assets, they are not used in factories involved

in manufacturing activities. They have been installed only in the workstations/car service centers attached to the Regional offices which are involved in generating service income (as stated by the assessee company itself). These assets are not connected to manufacturing activity and hence are not eligible for additional depreciation.

93. On this issue also, learned representatives fairly agree that the same is covered, in favour of the assessee, by a decision of this Tribunal in assessee's own case for the assessment year 2007-08. Learned Departmental Representative, however, dutifully relies upon the stand of the authorities below.

94. We see no reasons to take any other view of the matter than the view so taken by us in assessee's own case for the assessment year 2007-08. Respectfully following the same, we uphold the grievance of the assessee and direct the Assessing Officer to delete this depreciation disallowance as well.

95. Ground no. 4 is also thus dismissed.

96. In the result, the appeal filed by the Assessing Officer for the assessment year 2009-10 is thus dismissed.

97. We now take up the appeal of the assessee for the assessment year 2010-11.

98. Ground no. 1 is general in nature and does not call for any specific adjudication.

99. In ground no. 2, the assessee is aggrieved of the Assessing Officer making an addition of Rs 62,20,34,587 in respect of ALP adjustment for notional receipt on account of brand promotion fees. For the detailed reasons set out earlier in this order, and subject to the directions set out therein, we have deleted this adjustment.

100. Ground no. 2 is thus allowed.

101. In ground no. 3.1, the assessee is aggrieved of the disallowance of Rs 12,33,54,430 made by the Assessing Officer under section 40(a)(i) in respect of interest payment to HSBC (Mauritius) Ltd and Standard Chartered Bank (Mauritius) Limited.

102. As for this ground of appeal, learned representatives fairly agree that whatever is the fate of similar ground of appeal for the assessment year 2009-10 will be the fate of this ground. Vide our order above, we have upheld the plea of the assessee on this point and deleted the identical disallowance. The observations so

made apply mutatis mutandis for this year as well. Respectfully following the view so taken, we delete this disallowance of Rs 12,33,54,430.

103. Ground no. 3.1 is allowed.

104. In ground no. 3.2, the assessee is aggrieved of the Assessing Officer treating the export incentives on account of Focus Market Scheme and Focus Products scheme, amounting to Rs 26,80,00,000, as income of the year before us.

105. While dealing with identical grievance of the assessee for the assessment year 2009-10, and for the reasons set out earlier in this order, we have upheld the plea of the assessee. We see no reasons to take any other view of the matter for this assessment year. Respectfully following the view so taken we uphold the plea of the assessee and delete the impugned disallowance.

106. Ground no. 3.2 is thus allowed

107. In ground no. 3.3, the assessee has raised a grievance against the Assessing Officer making a disallowance of Rs 3,30,332 of depreciation on account of reduction of capital subsidy granted by SIPCOT from the cost of assets.

108. Learned representatives agree that identical issue, in respect of the assessment year 2007-08, was remitted to the file of the DRP for fresh adjudication on the nature of the subsidy. Whatever are the findings of the DRP for the assessment year 2007-08 will be equally valid for this assessment year as well. We, therefore, remit the matter to the file of the Assessing Officer for examining the matter afresh in the light of those findings of the DRP. While so deciding the matter, the Assessing Officer will give a due opportunity of hearing to the assessee.

109. Ground no. 3.4 is thus allowed for statistical purposes.

110. In ground no. 3.4, the assessee is aggrieved of the Assessing Officer making a disallowance of Rs 1,99,56,723 under section 14A of the Act

111. Learned representatives fairly agree that this issue is also covered, in favour of the assessee, by decision of the coordinate bench in assessee's own case for the assessment year 2007-08. As there was no tax exempt in the relevant previous year, the disallowance was deleted for this short reason alone. That is the approach consistently adopted by several coordinate benches as well. We see no reasons to take any other view of the matter. Respectfully following the same, we uphold the grievance of the assessee and delete the impugned disallowance of Rs 1,99,56,723.

112. Ground no. 3.4 is thus allowed.

113. No other issue was pressed before us.

114. The appeal of the assessee for the assessment year 2010-11 is thus partly allowed in the terms indicated above.

115. We now take up revenue's appeal for the assessment year 2010-11.

116. Ground no. 1 is general and it does not call for any specific adjudication.

117. In ground no. 2, the Assessing Officer is aggrieved of the DRP's directions to delete the disallowance of Rs 1,25,86,642 on account of guarantee charges paid by the assessee to Hyundai Motor Co, Korea, in respect of external commercial borrowings made by the assessee.

118. Vide our findings for the assessment year 2009-10, earlier in this order, we have confirmed the stand so taken by the DRP on this point, and thus decided the issue in favour of the assessee. We see no reasons to take any other view of the matter for this assessment year. Respectfully following our view for the assessment year 2009-10, and for the detailed reasons set out therein, we approve the stand of the DRP and decline to interfere in the matter.

119. Ground no. 2 is thus dismissed.

120. In ground no. 3, the Assessing Officer is aggrieved of the DRP's directions to delete the addition of Rs 5,87,350 in respect of additional depreciation.

121. As learned representatives fairly agree, this issue is also covered, in favour of the assessee, by a coordinate bench decision for the assessment year 2007-08. Respectfully following the same, we confirm the relief granted by the DRP and decline to interfere in the matter.

122. Ground no. 3 is thus dismissed.

123. In ground no. 4, the Assessing Officer is aggrieved of the DRP's directions to delete the disallowance of Rs 159,00,60,000 on account of warranty provision.

124. Vide our findings for the assessment year 2009-10, earlier in this order, we have confirmed the stand of the DRP on this point. We see no reasons to take any other view of the matter for this assessment year. Respectfully following our view for the assessment year 2009-10, and for the detailed reasons set out therein, we approve the stand of the DRP and decline to interfere in the matter.

125. Ground no. 4 is thus dismissed.

126. The appeal filed by the Assessing Officer for the assessment year 2010-11 is thus dismissed.

127. We will now take up the assessee's appeal for the assessment year 2011-12

128. Ground nos. 1 and 2 are general and do not call for any specific adjudication.

129. The first issue raised in this appeal, vide ground no. 3 to 8, is not pressed and is dismissed as such.

130. In the second issue raised in this appeal, vide ground nos. 8 to 26, the assessee is aggrieved of the Assessing Officer making an addition of Rs 253.44 crores in respect of ALP adjustment for notional receipt on account of brand promotion fees. For the detailed reasons set out earlier in this order, and subject to the directions set out therein, we have deleted this adjustment. The assessee must succeed on this point for this assessment year as well.

131. Ground nos 8 to 26 are thus allowed.

132. In the the third issue raised in this appeal, vide ground nos. 27 to 31, assessee has raised a grievance against the Assessing Officer's making a disallowance of Rs 2,80,782 of depreciation on account of reduction of capital subsidy granted by SIPCOT from the cost of assets.

133. Learned representatives agree that identical issue, in respect of the assessment year 2007-08, was remitted to the file of the DRP for fresh adjudication on the nature of the subsidy. Whatever are the findings of the DRP for the assessment year 2007-08 will be equally valid for this assessment year as well. We, therefore, remit the matter to the file of the Assessing Officer for examining the matter afresh in the light of those findings of the DRP. While so deciding the matter, the Assessing Officer will give a due opportunity of hearing to the assessee.

134. Ground nos, 27 to 31 are thus allowed for statistical purposes.

135. In the fourth issue raised in this appeal, the assessee is aggrieved of the disallowance of Rs 4,06,32,673 under section 43B of the Act, in respect of performance reward which is said to be distinct from bonus

136. So far as this grievance of the assessee is concerned, only a few material facts need to be taken of. During the course of scrutiny assessment proceedings, the Assessing Officer noticed that the assessee has debited performance reward, i.e. bonus, amounting to Rs 4,06,32,673 but, as per the tax audit report, this amount has remained outstanding as at the end of the relevant previous year. On these facts, the Assessing Officer required the assessee to show cause as to why the said deduction not be disallowed under section 43B. It was explained by the assessee that since bonus was not a statutory bonus under the Payment of Bonus Act, the disallowance under section 43 B does not come into play. The Assessing Officer, however, was of

the view that the provisions of Section 43B (c) were not confined to bonus under the Payment of Bonus Act, and, as such, the disallowance under section 43B would indeed come into play. Aggrieved, assessee raised a grievance before the DRP but without any success. It was in this backdrop that the Assessing Officer disallowed Rs 4,06,32,673 on account of, what assessee terms as, performance reward. The assessee is aggrieved and is in appeal before us.

137. We have heard the rival contentions, perused the material on record and duly considered facts of the case in the light of the applicable legal position.

138. We find that this issue is covered against the assessee by direct decision, on this point, by Hon'ble Uttarakhand High Court, in the case of CIT Vs Kisan Sahkari Chini Mills Ltd [(2009) 318 ITR 218 (Uttarakhand)]. No direct decisions, in favour of the assessee and on this point, have been brought to our notice. In this view of the matter, we uphold the stand of the Assessing Officer and decline to interfere in the matter.

139. Ground nos. 32 to 34 are thus dismissed.

140. The assessee has raised an additional ground of appeal that %subsidy received from the Government of Tamilnadu in the form of refund of output VAT is a capital receipt not chargeable to tax+ and to that extent the stand of the authorities below is incorrect and needs to be vacated.

141. While there cannot indeed be any objection to the appellant raising any new issue before the Tribunal, in view of the decision of Hon'ble Supreme Court in the case of NTPC Ltd Vs CIT [(1998) 229 ITR 383 (SC)], with the consent of the parties, this matter is required to be remitted to file of the Assessing Officer for adjudication de novo on merits, in accordance with the law, by way of a speaking order and after giving a fair and reasonable opportunity of hearing to the assessee. We, therefore, accept the additional ground of appeal but remit the matter to the file of the Assessing Officer for fresh adjudication in the light of above observations. Ordered, accordingly.

142. Additional ground of appeal is thus allowed for statistical purposes in the terms indicated above.

143. The appeal of the assessee for the assessment year 2011-12 is thus partly allowed in the terms indicated above.

144. We now take up appeal of the Assessing Officer for the assessment year 2011-12.

145. In the first ground of appeal, the Assessing Office has raised grievance against deletion of disallowance of Rs 1,35,21,777 on the ground that there was no tax exempt income in this year.

146. Learned representatives fairly agree that this issue is also covered, in favour of the assessee, by decision of the coordinate bench in assessee's own case for the assessment year 2007-08. As there was no tax exempt in the relevant previous year, the disallowance was deleted for this short reason alone. That is the approach consistently adopted by several coordinate benches as well. We see no reasons to take any other view of the matter. Learned DRP has simply followed the order of the Tribunal on this issue, and granted the impugned relief. Respectfully following the same, we uphold the relief, of deleting the disallowance of Rs 1,35,21,777, granted by the DRP and decline to interfere in the matter.

147. Ground no. 1 is thus dismissed.

148. In ground no. 3.2, the assessee is aggrieved of the Assessing Officer treating the export incentives on account of Focus Market Scheme and Focus Products scheme, as income of the year before us.

149. We find that this issue is covered, in favour of the assessee, by a decision of the coordinate bench in assessee's own case for the assessment year 2007-08 wherein the coordinate bench has concluded as follows;

In the case of the assessee, the export incentive towards target plus scheme is bestowed as a reward in order to encourage the accelerating growth in exports. The incentive on target plus scheme is nothing but an entitlement for a duty credit based on incremental exports which should be substantially higher than the general annual export target that is fixed. The incentive on focus market scheme is to offset high freight cost and other externalities to select international market with a view to enhance India's export competitiveness in those countries. It is pertinent to note that the assessee will be entitled to such benefit only after verification of the claim of the assessee by relevant governmental authorities and issuance of licence by such governmental authorities. Therefore, the facts of the assessee's case are similar to the facts decided by the Hon'ble Apex Court cited supra. Therefore, respectfully following the decision of Hon'ble Supreme Court, we hereby hold that the notional income computed by the assessee cannot be treated as taxable income of the assessee during the relevant previous year. However, the same shall be taxed in the previous year in which the assessee has received the licences and derived such income. Thus, this issue is also decided in favour of the assessee.

150. The DRP has simply followed the above stand of the Tribunal, and rightly so. We see no reasons to take any other view of the matter than the view so taken by the coordinate bench in assessee's own case. Respectfully following the same, we uphold the relief granted by the DRP. We decline to interfere in the matter.

151. Ground no. 2 is thus dismissed.

152. In ground no. 3, the Assessing Officer is aggrieved of the DRP's directions to delete the addition in respect of additional depreciation on assets deployed in the regional offices.

153. As learned representatives fairly agree, this issue is also covered, in favour of the assessee, by a coordinate bench decision for the assessment year 2007-08. Respectfully following the same, we confirm the relief granted by the DRP and decline to interfere in the matter.

154. Ground no. 3 is thus dismissed.

155. In ground no. 4, the Assessing Officer is aggrieved of depreciation being allowed @ 60% in respect of UPS, Printers and Scanners, and thus treating the same at par with the computers.

156. Having heard the rival contentions, and having perused the material on record, we find this issue is also covered in favour of the assessee by Hon'ble Delhi High Court's judgment in the case of CIT Vs BSES Yamuna Powers Ltd [(2013) 358 ITR 45 (Del)] wherein Their Lordships have, inter alia, observed that we are in agreement with the view of the Tribunal that computer accessories and peripherals such as, printers, scanners and server, etc., form an integral part of the computer system. In fact, the computer accessories and peripherals cannot be used without the computer. Consequently, as they are the part of the computer system, they are entitled to depreciation at the higher rate of 60 per cent+. In this view of the matter, we approve the conclusions arrived at by the DRP and decline to interfere in the matter.

157. Ground no. 4 is thus dismissed.

158. In ground no. 5, the Assessing Officer is aggrieved of learned DRP granting relief in respect of guarantee charges of Rs 1,87,44,188 paid to its parent company in respect of external commercial borrowings.

159. Vide our findings for the assessment year 2009-10, earlier in this order, we have confirmed the stand so taken by the DRP on this point, and thus decided the issue in favour of the assessee. We see no reasons to take any other view of the matter for this assessment year. Respectfully following our view for the assessment year 2009-10, and for the detailed reasons set out therein, we approve the stand of the DRP and decline to interfere in the matter.

160. Ground no. 5 is thus dismissed.

161. In ground no. 6, the Assessing Officer is aggrieved that the DRP holding that the claim of deduction for provision for warranty is admissible.

162. As learned representatives fairly agree, and as has been stated in the DRP order itself, this recurring issue is now covered in favour of the assessee, in assessee's own case for the assessment years 2009-10 and 2010-11, by Honble High Courts decision dated 29th October 2013. We, therefore, confirm the relief granted by the DRP on this point as well, and decline to interfere in the matter.

163. Ground no. 6 is thus dismissed.

164. The appeal of the Assessing Officer is thus dismissed.

165. In the result, while CO of the assessee is dismissed, all the three appeals filed by the assessee are partly allowed in the terms indicated above, all the three appeals filed by the revenue are dismissed. Pronounced in the open court today on the 27th day of April, 2017

Sd/-
G Pavan Kumar
(Judicial Member)

Sd/-
Pramod Kumar
(Accountant Member)

Chennai, the 27th day of April, 2017.

Copies to: (1) *The appellant* (2) *The respondent*
 (3) *CIT* (4) *DRP*
 (5) *DR* (6) *Guard File*

By order

Sr Private Secretary
Income Tax Appellate Tribunal
Chennai benches, Chennai