IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

R/SPECIAL CIVIL APPLICATION NO. 23302 of 2019

With
CIVIL APPLICATION (FOR VACATING INTERIM RELIEF) NO. 1 of 2020
In R/SPECIAL CIVIL APPLICATION NO. 23302 of 2019

FOR APPROVAL AND SIGNATURE:

HONOURABLE MR. JUSTICE J.B.PARDIWALA

and
HONOURABLE MR. JUSTICE ILESH J. VORA

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1	Whether Reporters of Local Papers may be allowed to see the judgment ?	**NO**
2	To be referred to the Reporter or not ?	**YES**
3	Whether their Lordships wish to see the fair copy of the judgment ?	**NO**
4	Whether this case involves a substantial question of law as to the interpretation of the Constitution of India or any order made thereunder ?	**NO**

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HITACHI HI REL POWER ELECTRONICS PVT. LTD.
Versus
THE DEPUTY COMMISSIONER OF INCOME TAX CIRCLE 2(1)(1), AHMEDABAD

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Appearance:
MR B S SOPARKAR(6851) for the Petitioner(s) No. 1
MR MR BHATT SENIOR COUNSEL WITH MRS MAUNA M BHATT(174) for the Respondent(s) No. 1,2

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CORAM:**HONOURABLE MR. JUSTICE J.B.PARDIWALA**
and
HONOURABLE MR. JUSTICE ILESH J. VORA

Date : 19/08/2021

ORAL JUDGMENT

(PER : HONOURABLE MR. JUSTICE J.B.PARDIWALA)

1 By this writ application under Article 226 of the Constitution of India, the writ applicant has prayed for the following reliefs:

> *"(a) quash and set aside the impugned reference by Respondent No.1 to Respondent No.2 and the notice dated 20.12.2019 at Annexure 'A' to this petition.*
>
> *(b) pending the admission, hearing and final disposal of this petition, to stay implementation and operation of the impugned notice dated 20.12.2019 at Annexure 'A' to this petition and stay the assessment proceedings for AY 2017-18 undertaken by Respondent No.1;*
>
> *(c) any other and further relief deemed just and proper be granted in the interest of justice;*
>
> *(d) to provide for the cost of this petition"*

2 The case put up by the writ applicant, in his writ application, may be summarized as under:

3 The writ applicant is a limited company. It seeks to challenge the reference made by the respondent No.1 to the respondent No.2 under Section 92CA (1) of the Income Tax Act (for short, "the Act"), in relation to the computation of Arm's Length Price on the ground of being erroneous, illegal and contrary to law. The writ applicant further seeks to challenge the notice under Sections 92CA(2) and 92D(3) respectively issued by the respondent No.2 dated 20th December 2019, on the ground of being erroneous, illegal, contrary to law and without jurisdiction.

4 The writ applicant is engaged in the business of manufacturing Industrial Automation Solution, Rotating Machine Control, Power Controller, Uninterrupted Power Supply and Power Conditioning

products. In relation to A.Y. 2017-18, the writ applicant had availed an unsecured External Commercial Borrowing (ECB) rupee loan from the Hitachi International Treasury Limited, Singapore, for the purpose of working capital. This loan carries an interest at the rate of 7.19% per annum. The writ applicant filed Form 3CEB, wherein there is a requirement in clause 14 to make a disclosure about the loan or borrowing of money and the amount paid / received in the transaction.

5 In the aforesaid context, it is the case of the writ applicant that it had appropriately disclosed the transaction in the Form 3CEB.

6 The respondent No.1 issued a show cause notice dated 18th November 2019 under Section 142(1), which reads thus:

> *"1. During the previous year, assessee company has taken loan from Hitachi International Treasury limited to the tune of Rs. 20 Crores @ 7.19% interest. Further same was required to be reported in 3CEB but assessee has failed to do so. Therefore you are requested to show cause as to why penalty u/s 271AA of the Act should not be initiated in your case. In addition to that you are request to show cause as to why your case is not referred to TPO for determination of arm's length on such unreported transaction.*
>
> *2. On verification of the details submitted by you, it is noticed that certain Creditors are found ideal since last three years and no transactions or payment is being made. Accordingly you are requested to show cause as to addition of u/s 41 of the act should not be made on account of cession of liability.*
>
> *3. Please explain the Reason for lower deduction of TDS on payment made u/s 194(C) of the Act.*
>
> *4. On perusal of reply filed by you, it is noticed that you have not furnished the reply to point 25 in prescribed format. Please resubmit the same.*
>
> *5. On verification of ITR and computation of income, it is noticed that you have Claimed "Any other amount to be allowable as deduction" i.e. bad debt provision utilization of Rs. 2,23,09,526/-. Please show*

cause as why such deduction should not be disallowed as it is not debited to P&L account during the previous year.

6. On verification of computation of income it is noticed that you have claimed reversal of mark to market loss of Rs. 4,73,706/-. In this regard please provide copy of computation for FY 2015-16 in which such amount was disallowed.

7. During the previous year the company has utilized inventory provision of Rs. 97,80,041/-. Explain nature of such claim and supporting documentary evidences in support of such claim.

8. On perusal of tax audit report is is noticed that In clause 21(a) of TAR, auditors has reported that amount debited to P & L account being in the nature of capital, personnel etc. and in relation to amortization of lease hold land amount to Rs.2,27 ,240/-. Further on verification of computation of income it is noticed that the same has not been disallowed. Therefore, you are requested to show cause as why same should not be disallowed.

9. Please submit detailed break up of advances written off of Rs.1,97,076/-. Please show Cause as why to why it should not be disallowed.

10. On verification of the submission made by you it is noticed that there is mismatch in additions to fixed assets as reported in note 12 & 13 of the audited financial statement and per clause 18 of tax audit report. Please reconcile the same.

11. On perusal of clause 18 of the tax audit report, it is noticed that block of asset has been increased due to change in rate of exchange. Details of same area as under:

a) Building:1,13,32,654/-

b) F & F :-3,22,750/-

c) Plant & Machinery (15%): 90,74,176/-

d) Plant & Machinery (60%): 5,11,555

In this regard, you are requested to provide following:

1. Explain such large amount of details addition due to change in foreign exchange rate difference.

b) In audited financial statement value of fixed asset has decreased by Rs. 8,10,920/- due to exchange rate difference

c) Whether foreign exchange rate difference Loss of Rs.2,12,41,135/- debited to P & L account have disallowed or not in computation of total income, if such loss Is capital in nature.

d) Reason for huge foreign exchange loss in respect of block of building.

12. On verification of submission so made by assessee company and on verification of earlier years records, it is noticed that certain additions were made on recurring issues. Therefore, you are requested to show cause as to why similar additions/disallowances should not be made during the year is line of earlier years."

7 The writ applicant, vide its reply dated 25th November 2019, tried to explain to the respondent No.1 that the disclosure in Form 3CEB is appropriate and the same is not defined in any manner. The writ applicant, in its reply, stated that it had disclosed the factum of obtaining loan and the amount of interest paid / payable as well as the method used to determine the Arm's Length of the same. The writ applicant further clarified in its reply that there is no obligation of reporting the "loan transaction" amount in the Form 3CEB. Only the interest paid on such loan transaction will have a bearing on the profit / loss and the same is required to be reported at clause 14 of the Form 3CEB.

8 It appears that the respondent No.1, vide order passed by him dated 4th December 2019, overruled the objections raised by the writ applicant and proceeded to make a reference to the respondent No.2.

9 The respondent No.2 issued impugned notice dated 20th December 2019 under Sections 92CA(2) and 92D(3) respectively of the Act.

10 The writ applicant, being aggrieved with the reference made by the respondent No.1 to the respondent No.2 and also with the notice

issued by the respondent No.2 under Section 92CA(2) read with Section 92D(3) of the Act, is here before this Court with the present writ application.

- **SUBMISSIONS ON BEHALF OF THE WRIT APPLICANT:**

11 Mr. B. S. Soparkar, the learned counsel appearing for the writ applicant vehemently submitted that his client was not given an opportunity of hearing by the A.O. before disposing of the objections raised by his client and making a reference to the T.P.O. for the determination of the A.L.P. Mr. Soparkar submitted that the reference at the instance of the A.O. to the T.P.O. is solely on the ground that the writ applicant has failed to fully disclose his international transaction of loan of Rs.20 Crore. In other words, the writ applicant has not added the loan amount in column No.8 of the 3CEB report and in such circumstances, the A.O. is seeking to justify the reference made by him to the T.P.O. under para 3.3 (a) of the instruction 3/2016. However, Mr. Soparkar would vehemently submit that the A.O. has completely overlooked the jurisdictional requirement of a satisfaction in accordance with para 3.4 of the instruction 3/2016 that there ought to be an income or a potential of an income arising and/or being affected on determination of the A.L.P. of an international transaction or specified domestic transaction. Mr. Soparkar would submit that in the absence of such satisfaction being recorded as to the income or a potential of an income, the entire exercise undertaken by the A.O. could be termed as illegal and without jurisdiction. Mr. Soparkar would submit that in the case on hand, neither at the time of issue of show cause notice nor in the order disposing of the objections, there is any whisper of income or a potential income arising and/or being affected on the determination of the A.L.P. of an international transaction of the loan of Rs.20 Crore. Mr. Soparkar would submit that there is no satisfaction on the part of the A.O. that there is

any income arising on the determination of the A.L.P. of loan transaction and in such circumstances, it could be said that the A.O. had no jurisdiction to refer the matter to the T.P.O.

12 Mr. Soparkar further submitted that the transaction of loan being on the capital account, there cannot be any impact on income. He would argue that the writ applicant has disclosed the transaction of payment interest and the same has not been disputed. The transaction of loan separated from income is on the capital account and has no impact on the income and therefore, there is no question of computing the A.L.P. of loan *per se*. In such circumstances, the very basis of the reference to the T.P.O. is contrary to para 3.4 of the instruction 3/2016 and therefore, illegal.

13 Mr. Soparkar submitted that his client has truly and fully furnished all the necessary details of payment of interest on loan in the column No.14, which has impact on the income. He would argue that as such, there is no clause in the entire Form 3CEB (from clauses 11 to 25), wherein his client is obliged to declare the transaction of loan and determine the Arm's Length Price and therefore, the disclosure made by his client insofar as the transaction that has an impact on the income should be construed as full and true. Mr. Soparkar would argue that the requirement in para 3.3(a) of the C.B.D.T. circular No.3/2016 should be read with para 3.4 and if read together, the same would indicate that there is no failure on the part of his client to disclose any transaction that has impact on income. He would submit that the case of his client does no fall within the para 3.3(a) of the instruction.

14 In the last, Mr. Soparkar pointed out that the Form 3CEB has two parts: (i) the part 'A' captures initial information, and part 'B' relates to

computation of Arm's Length Price. It is submitted that the error on the part of his client in computing the amount in column No.8 would not give rise to the circumstances of referring the matter to the T.P.O. His client has fully disclosed the factum of loan and interest details in column Nos.10 and 14 respectively. The important part of Form 3CEB is part 'B' only and on that basis, the A.L.P. is determined / changed either by the A.O. or T.P.O., as the case may be. As there is no error or omission in part 'B', it would not have any impact on the A.L.P. to be determined and therefore, there is no failure on the part of his client to disclose any transaction that has impact on the income.

15 In such circumstances referred to above, Mr. Soparkar prays that there being merit in his writ application, the same be allowed and the reference made by the respondent No.1 to the respondent No.2 may be quashed and set aside including the notice dated 20th December 2019.

16 Mr. Soparkar, in support of his aforesaid submissions, has placed reliance on the following decisions:

[1] Indorama Synthetics (India) Ltd vs. Additional Commissioner of Income-tax reported in [2016] 71 taxmann.com 349 (Delhi)

[2] Alpha Nipon Innovatives Ltd. vs. Deputy Commissioner of Income-tax, Circle 1(1)(1)(1)&1 reported in [2016] 76 taxmann.com 166 (Gujarat)

[3] Mehsana District Co-operative vs. Deputy Commissioner of Income Tax [Special Civil Application No.19073 of 2017 decided on 6th March 2018]

- **SUBMISSIONS ON BEHALF OF THE REVENUE:**

17 Mr. M. R. Bhatt, the learned Senior Counsel assisted by Ms. Mauna Bhatt, the learned Senior Standing Counsel appearing for the Revenue has vehemently opposed the present writ application submitting that during the year under consideration, the writ applicant had obtained loan from the Hitachi International Treasury Limited to the tune of Rs.20 Crore at the rate of 7.19% and such transaction was required to be reported in the Form 3CEB. However, Mr. Bhatt would submit that the writ applicant failed in reporting the transaction of loan in the column No.8 of the Form 3CEB. In such circumstances, the A.O., having regard to the C.B.D.T. instruction No.3/2016 was justified in issuing the notice dated 18th November 2019 to the writ applicant calling upon the writ applicant to show cause as to why his case should not be referred to the T.P.O. for determination of the Arm's Length Price on such undisclosed transaction.

18 Mr. Bhatt would submit that pursuant to the C.B.D.T. instruction, more particularly, para 3.3(a), which provides for making reference to the T.P.O. in the event of none disclosure of only international transaction in the file of the account report, the objections raised by the writ applicant were disposed of by a speaking order dated 4th December 2019. The A.O., after recording due satisfaction to the effect that the assessee had entered into an international transaction and the same not being disclosed in the account report file proceeded to obtain the necessary approval of the Principal Commissioner of Income Tax – 2, Ahmedabad and refer the matter to the Transfer Pricing Officer. In such circumstances, according to Mr. Bhatt, the contention canvassed on behalf of the writ applicant that no show cause notice under Section 92CA(1) of the Act was issued to the writ applicant, is contrary to the

record. Mr. Bhatt would submit that the principles of natural justice have been duly complied with. There is no element of prejudice caused to the writ applicant inasmuch as the objections raised by the writ applicant were disposed of by a speaking order and the T.P.O. would otherwise provide adequate opportunity of hearing before making any transfer pricing adjustment.

19 Mr. Bhatt next submitted that indisputably, the writ applicant had entered into an international transaction with the associated enterprise namely the Hitachi International Treasury Limited. Section 92B of the Act defines the term "international transaction". The Explanation (i)(c) to Section 92B defines the term "international transaction" as under:

> *"(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;"*

20 Mr. Bhatt, referring to the aforesaid definition of the "international transaction" submitted that for the purposes of Chapter X, "loan" is the transaction which was required to be reported in the Form 3CEB. The writ applicant had availed loan from the associated enterprise. However, the writ applicant failed to report the said "transaction" i.e. the loan amount in the Form 3CEB. Mr. Bhatt pointed out that Section 92E of the Act read with Rule 10E of the Income Tax Rules mandates the person who has entered into an international transaction to furnish report from an Accountant in the Form 3CEB.

21 Mr. Bhatt pointed out that the Form 3CEB has been produced by the writ applicant from page 13 onwards of the memorandum of the writ application. The part A of Annexure to Form 3CEB, more particularly,

item No.8 requires the assessee – the writ applicant to provide the "Aggregate value of international transactions as per books of accounts". The writ applicant had reported an amount of Rs.50,14,114/-. However, the said figure does not include the loan amount of Rs.20 Crore taken from the Hitachi International Treasury Limited. Therefore, there is an admitted failure on the part of the writ applicant to disclose such amount of international transaction in the column No.8.

22 Mr. Bhatt next submitted that Part B of the said Form, more particularly, item No.14 requires the assessee to fill in the particulars in respect of lending or borrowing of money. There is no dispute between the parties that the assessee had entered into an international transaction as can be seen at page 17 wherein the writ applicant – assessee had remarked "Yes". Item 14 requires the writ applicant to provide details in respect of clauses (a) to (f) in respect of each Associated Enterprise and loan / advance. In the present case, the writ applicant failed to disclose the amount of loan taken from the Associated Enterprise in column (e) which requires the assessee to mention "amount paid / received or payable / receivable in the transaction", which is clear from page 18 wherein the assessee had only disclosed the interest paid and not the loan amount. It is submitted that the term "amount paid / received or payable / receivable in the transaction" relates to the international transaction in respect of lending or borrowing of money. Moreover, the assessee is required to provide details in respect of each loan / advance. Therefore, the writ applicant's contention that the said amount of loan is not required to be disclosed in Form 3CEB is factually incorrect and deserves no consideration.

23 Mr. Bhatt in the last submitted that the contention raised on behalf of the writ applicant that the transaction does not have impact on

income is self-serving and *dehors* the records. It is submitted that the Arm's Length Price on the interest paid would have bearing on the income of the writ applicant and therefore, the contention that the international transaction entered into by the writ applicant has no bearing on the income does not hold any merit. For the purpose of arriving at the conclusion that the method adopted by the assessee and the A.L.P. is in order, the basic figure required is of the loan amount.

- **ISSUE OF LIMITATION:**

24 Mr. Bhatt also submitted as regards the issue of limitation. He pointed out that this Court vide order dated 27th December 2019 was pleased to stay the Transfer Pricing proceedings and allowed the assessment proceedings to go on. Section 153 of the Act provides for the time limit to frame assessment. The time limit to frame assessment for A.Y. 2017-18 as per Section 153(1) was 31st December 2019. In view of Section 153(4), the time limit was extended by further 12 months as reference under Section 92CA(1) of the Act was made which expired on 31st December 2020. In view of the Covid-19 pandemic, the time limit to frame the assessment came to be extended till 31st March 2021 in light of the Taxation and Other Laws (Relaxation of Certain Provisions), Ordinance, 2020. Explanation 1(ii) to Section 153 provides for exclusion of the period during which the assessment proceeding is stayed by an order or injunction of any Court. The Act does not provide for any exclusion of period during which the Transfer Pricing proceedings are stayed. In the event, this Court quashes the reference made to the T.P.O., the assessment proceedings would get time barred.

25 Mr. Bhatt invited the attention of this Court to the decision of the Supreme Court in the case of VLS Finance Limited vs. CIT reported in 384 ITR 1. In the said case, the assessee had challenged the direction for

Special Audit under Section 142(2A) of the Act and the High Court had granted stay against such direction for special audit without any stay on the assessment proceedings. The Supreme Court held that the special audit is an integral part of the assessment proceedings i.e. without special audit it is not possible for the assessing officer to carry out the assessment and stay of the special audit may qualify as stay of the assessment proceedings itself and, therefore, would be covered by the said Explanation 1 to Section 158BE. Explanation 1 to Section 158BE is *pari materia* with Explanation 1 to Section 153 of the Act. Reliance has been placed on paras 19, 20, 21 and 23 respectively wherein the Supreme Court has held that the stay of special audit qualifies as stay of the assessment proceedings and therefore, the period for the said stay has to be excluded while counting the limitation period for assessing block assessment period.

26 Mr. Bhatt submitted that as per the Scheme of the Act, more particularly, Section 92CA(1) of the Act, where any assessee has entered into an international transaction or specified domestic transaction, the Assessing Officer may refer the computation of the arm's length price in relation to the said international transaction or specified domestic transaction to the Transfer Pricing Officer. The Transfer Pricing Officer after providing full opportunity to the assessee, is required to pass order under subsection (3) of Section 92CA determining the arm's length price in relation to the international transaction or specified domestic transaction. Upon receipt of the order passed by the Transfer Pricing Officer under sub-Section (3) of Section 92CA, the Assessing Officer proceeds to compute the total income of the assessee in conformity with the arm's length price determined by the Transfer Pricing Officer. Mr. Bhatt would submit that it is clear that the Assessing officer cannot frame assessment sans the order of the Transfer Pricing Officer.

27 Mr. Bhatt would submit that the Transfer Pricing proceedings is an integral part of the assessment proceedings and therefore, the period during which proceedings before the T.P.O. was stayed is required to be excluded for the purposes of computing limitation for framing assessment under Section 143(3) of the Act.

28 Mr. Bhatt, in support of his aforesaid submissions, has placed reliance on two decisions of this High Court:

(i) M/s. D. B. Corporation Limited vs. Deputy Commissioner of Income Tax – Circle and others [Special Civil Application No.5035 of 2016 decided on 10th August 2016]

(ii) M/s. Veer Gems vs. Assistant Commissioner of Income Tax – Circle 7 and others [Special Civil Application No.12648 of 2011 decided on 19th October 2011]

- **ANALYSIS:**

29 Having heard the learned counsel appearing for the parties and having gone through the materials on record, the following two questions fall for our consideration:

[1] Whether it was incumbent on the A.O. to have given the writ applicant an opportunity of being heard before making a reference to the T.P.O. under Section 92CA(1) of the Act?

[2] Whether the Assessing Officer could be said to have overlooked the jurisdictional requirement of a satisfaction in accordance with para 3.4 of the instruction No.3 of 2016 that

there ought to be an income or a potential of an income arising and/or being affected on determination of the A.L.P. of an international transaction or specified transaction? In the absence of recording of such satisfaction, as to the income or potential of an income, could it be said that the entire exercise undertaken by the A.O. is illegal?

30 On the first question i.e. as regards giving an opportunity of hearing, Mr. Soparkar has placed strong reliance on the decision of the Delhi High Court in the case of **Indorama Synthetics (India) Ltd (supra)**. Whereas Mr. Bhatt, the learned Senior Counsel appearing for the Revenue has placed reliance on the decision of this High Court in the case of **M/s. Veer Gems (supra)**. We first propose to look into the decision of the Delhi High Court in the case of **Indorama Synthetics (India) Ltd (supra).** We quote the relevant observations:

> *"12. To begin with it is required to be noticed that Chapter X contains provisions regarding determination of ALP of international transactions and specified domestic transactions. While Section 92C talks of computation of ALP, Section 92BA defines a specified domestic transaction. For the purpose of the present petitions, it is not necessary for the Court to examine if in fact the Petitioner did enter into an international transaction and whether IPL could be said to be the AE of the Petitioner. The main issue in these petitions is whether it was incumbent on the AO to have given the Petitioner an opportunity of being heard before making a reference to the TPO under Section 92 CA (1) of the Act?*
>
> *13. The relevant portions of Section 92CA of the Act, which deals inter alia with the procedure to be followed in the making of a reference by the AO to the TPO reads as under:*
>
> > *"Section 92CA:-*
> >
> > *(1) Where any person being the Assessee, has entered into an international transaction or specified domestic transaction in any previous year, and the Assessing Officer considers it necessary or expedient so to do, he may with the previous approval of the*

Principal Commissioner or Commissioner, refer the computation of the arm"s length price in relation to the said international transaction or specified domestic transaction under Section 92C to the Transfer Pricing Officer.

(2) Where a reference is made under sub-Section (1), the Transfer Pricing Officer shall serve a notice on the Assessee requiring him to produce or cause to be produced on a date to be specified therein, any evidence on which the Assessee may rely in support of the computation made by him of the arm"s length price in relation to the international transaction or specified domestic transaction referred to in sub-Section (1).

(2A) Where any other international transaction other than an international transaction referred under sub-Section (1), comes to the notice of the Transfer Pricing Officer during the course of the proceedings before him, the provisions of this Chapter shall apply as if such other international transaction is an international transaction referred to him under sub-section (1) (2B) Where in respect of an international transaction, the Assessee has not furnished the report under Section 92 E and such transaction comes to the notice of the Transfer Pricing Officer during the course of the proceeding before him, the provisions of this Chapter shall apply as if such transaction is an international transaction referred to him under sub-Section (1).

(2C) Nothing contained in sub-Section (2B), shall empower the Assessing Officer either to assess or reassess under Section 147 or pass an order enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the Assessee under Section 154, for any assessment year, proceedings for which have been completed before the 1st day of July 2012.

(3) On the date specified in the notice under sub-Section (2), or as soon thereafter as may be, after hearing evidence as the Assessee may produce, including any information or documents referred to in sub- section (3) of Section 92D and after considering such evidence as the Transfer Pricing Officer may require on any specified points and after taking into account all relevant materials which he has gathered, the Transfer Pricing Officer shall by order in writing, determine the arm"s length price in relation to the international transaction or specified domestic transaction in accordance with sub-section (3) of Section 92C and send a copy of his order to the Assessing Officer and to the Assessee."

14. Section 92CA reveals that there are certain jurisdictional perquisites for the making of a reference by the AO to the TPO. In the first place,

the AO has to be satisfied that the Assessee has entered into an international transaction or a specified domestic transaction. Where, as in the present case, the Assessee raises a threshold objection that it has not entered into any international transaction within the meaning of Section 92B of the Act, it is imperative for the AO to deal with such an objection. If the AO decides to nevertheless make a reference, he has to record the reasons, even prima facie, why he considers it necessary and expedient to make such a reference to the TPO.

15. What is referred to the TPO is the determination of the ALP of the said international transaction or specified domestic transaction. Therefore, the satisfaction to be arrived at by the AO regarding the existence of the international transaction or specified domestic transaction, even prima facie, is a sine qua non for making the reference to the TPO. Where such an Accountant's report is submitted by the Assessee in Form 3CEB, then there should be no difficulty for the AO to form an opinion, even a prima facie one, that it is necessary and expedient to make a reference to the TPO on the question of the determination of the ALP of such international transaction involving the Assessee.

16. CBDT's Instruction No. 3 of 2003 categorically states that in order to make a reference to the TPO, the AO has to satisfy himself that the Assessee has entered into an international transaction with its AE. One of the sources from which the factual information regarding the international transaction can be gathered is Form No. 3 CEB filed with the return which is in the nature of an Accountant's report containing the details of the international transaction entered into by the taxpayer during the AY in question. Where no such report in Form 3 CEB is filed by the Assessee, what will be the basis for the AO to record that it is necessary and expedient to refer the question of determination of the ALP of such transaction to the TPO? Where the AO is of the view that a transaction reflected in the filed return partakes of the character of an international transaction, he will put the Assessee on notice of his proposal to make a reference to the TPO under Section 92CA (1) of the Act. Before making a reference to the TPO, the AO has to seek approval of the Commissioner/Director as contemplated under the Act. Therefore, all transactions have to be explicitly mentioned in the letter of reference. The very nature of this exercise is such that the AO will first put the Assessee on notice of his proposing to make a reference to the TPO and seek information and clarification from the Assessee. If at this stage, the Assessee raises an objection as to the very jurisdiction of the AO to make the reference, then it will be incumbent on the AO to deal with such objection on merits.

17. While Section 92CA (1) does not itself talk about a hearing having to be given to the Assessee upon the latter raising an objection as to the jurisdiction of the AO to make a reference, such requirement appears to

be implicit in the very nature of the procedure that is expected to be followed by the AO. As already noticed, the AO has to record that he considers it necessary and expedient to make a reference. The AO has to deal with the objections raised by the Assessee. It is only thereafter that the AO can come to the conclusion, even prime facie, that it is necessary and expedient to make the reference. This has to be done prior to making a reference.

18. The further issue as far as the procedure to be followed is whether the AO is obliged to give the Assessee an opportunity of being heard prior to making the reference where an objection as to jurisdiction is raised by the Assessee in relation to the making a of reference?

19.1 In Vodafone India Services (P) Limited v. Union of India (supra), the Bombay High Court was seized of a similar question relating to AY 2009-

10.Vodafone India Services (P) Limited ["VISPL"] filed its return of income along with Form 3 CEB in which the transaction of issuance of equity shares by VISPL to its holding company (which it was undisputedly an AE) was declared as an international transaction. Also the ALP of the shares so issued, was determined. However, a notice was appended by the Accountant stating that the transaction of issue of equity shares did not affect the income of the Assessee and was being reported only as a matter of abundant caution.

19.2 The return was picked up for scrutiny by the AO. Thereafter, the AO, after obtaining the previous approval of the Commissioner of Income Tax ("CIT") referred all the transactions reported in Form 3 CEB to the TPO under Section 92CA (1) of the Act. The TPO then issued a show-cause notice (SCN) to VISPL on 14th December 2012, inter alia asking it to show cause why the issue price (including the premium) of the equity shares to its holding company as declared by VISPL should be accepted for the purposes of computing ALP under the Act.

19.3 In reply VISPL contended that the notice was completely without jurisdiction on the ground that provisions of Chapter X did not apply to issue of equity shares. Without prejudice, VISPL contested the SCN on merits. The TPO passed an order on 28th January 2013 negativing the above contentions of the Petitioner and proceeded to determine the ALP of the transaction in question. The AO then issued a draft assessment order under Section 143 read with Section 144-C(1) of the Act adding the entire income determined by the TPO to VISPL's income. VISPL then filed objections to the draft assessment order before the Dispute Resolution Panel ("DRP"). Objections were raised only with regard to the issues of valuation and quantification and not with regard to the issue of jurisdiction. A writ petition was later filed in the Bombay High Court challenging the jurisdiction of the AO to make a reference of the

above transaction to the TPO.

19.4 While discussing the provisions of Chapter X of the Act and in particular Section 92CA thereof, the Bombay High Court observed as under:

> *"32. It is clear that in view of Section 92 (1), there must be income arising and/or affected or potentially arising and/or affected by an International Transaction for the purpose of application of Chapter X. This would appear to be in the nature of jurisdictional requirement and the Assessing Officer must be satisfied that there is an income or a potential of an income arising and/or being affected on determination of an ALP before he proceeds further in determining the ALP or referring the issue to the TPO to determine the ALP. In this case, we find that the Petitioner has from the very beginning been challenging the jurisdiction to apply Chapter X on the ground that no income arises and/or is affected or potentially arises and/or is affected on account of issue of its shares to its holding company. The Assessing Officer does not deal with this objection/issue before referring the matter to the TPO. The TPO does not deal with the above objection on the ground that in terms of Section 92CA, his mandate is only to compute the ALP in relation to the International Transaction. The TPO in the impugned order dated 28 th January 2012 meets the Petitioner"s objection by stating that the same would be dealt with by the Assessing Officer. However, when the same objection was raised before the Assessing Officer post the order of the TPO, the Assessing Officer does not consider the same in the impugned draft assessment order dated 22nd March 2013 on the ground that in view of Section 92CA (4), the Assessing Officer is obliged to pass an order in conformity with the ALP determined by the TPO. This jurisdictional issue has to be dealt with either by the TPO or the Assessing Officer when specifically raised by the Petitioner/Assessee.*

33. Normally when an accountant reports an international transaction under Section 92E there may be no dispute that there is an income arising and/or being affected or a potential of an income arising and/or being affected by an international transaction on determination of ALP. However when an Assessee challenges the above premise, then the issue must be decided. Such an issue must be dealt with at the very threshold that is before determination of ALP. This is so because in case it is held that in the International Transaction there is no income or potential of any income arising and/or being affected on determination of an ALP, the entire exercise of determining the ALP would become academic. In terms of Section 92CA (4), the Assessing Officer is bound to pass an order in conformity with the ALP determined by the TPO as

held by another Division Bench of this Court in the judgment dated 6th September 2013 in Vodafone II case. However, where the Assessing Officer is himself determining the ALP in terms of Section 94C (3) then in accordance with Section 94C (4) he would compute the income, having regard to the ALP. In such cases, where the Assessing Officer decides the ALP himself, it is open to him to consider the issue of income arising and/or being affected or not before commencing the proceedings under Chapter X or at the stage of passing an assessment order."

19.5 The Bombay High Court further observed that where the objection is raised about the applicability of Chapter X of the Act, "then the requirement for taking a decision after taking on board the objection becomes necessary. In the absence of it being considered at this stage, the same could only be considered by the DRP and as pointed out above, if considered at the very threshold by the Assessing Officer, it could save an elaborate exercise of determining the ALP which may turn out to be entirely academic." It is in the above circumstances, the Bombay High Court concluded that "grant of personal hearing before referring the matter to the TPO has to be read into Section 92CA (1) in cases where the very jurisdiction to tax under Chapter X is challenged by the Assessee."

19.6. While disagreeing with the view of the Gujarat High Court in Veer Gems (supra), the Bombay High Court set aside the order passed by the AO making a reference to the TPO. The Bombay High Court further explained the consequence of hearing being given to the Assessee by the AO before making a reference to the TPO and observed in para 40, as under:

> *"40. In our view, once the AO gives hearing to the Assessee before making a reference to TPO, the TPO would be bound by formation of opinion of AO that there was international transaction in the relevant year and that income arises or is affected by the international transaction and the TPO is bound to determine the ALP of the international transaction under consideration, since ultimately it is the duty and responsibility of AO to assess chargeable income of the Assessee on the basis of the provisions. Hence, there would be sufficient compliance with the principles of natural justice, if AO gives an opportunity of hearing to the Assessee. Normally when the Assessee files his return along with a copy of the Accountant"s report under Section 92E the applicability of Chapter X may be an admitted position. However we may add a caveat and that is: where the Assessee objects to the jurisdiction under Chapter X being exercised then hearing is required to be given by the Assessing Officer to the Assessee to consider whether it is necessary and expedient to refer the matter to the TPO as otherwise this*

objection would never be considered, as pointed out above and as in fact has happened in this case. In such cases where the applicability of Chapter X to the facts of the Assessee"s case is objected to, a hearing should be given to consider the Assessee"s objection but not otherwise."

19.7. However instead of remanding the matter to the AO, the Bombay High Court was of the view that the question must be considered by the DRP on merits.

20. This Court concurs with the view expressed by the Bombay High Court in Vodafone India Services (P) Limited v. Union of India (supra). It appears that the CBDT has specifically accepted the legal position as explained by the Bombay High Court in the aforementioned decision and has not gone by the decision by the Gujarat High Court in Veer Gems (supra). Instruction No. 15 of 2015 dated 16th October 2015 issued by the CBDT which sets out, inter alia, the procedure to be followed by the AO has since been replaced by Instruction No.3 of 2016 dated 10 th March 2016. Para 3.4 thereof reads as under:

"3.4 For cases to be referred by the AO to the TPO in accordance with paras 3.2 and 3.3 above, in respect of transactions having the following situations, the AO must, as a jurisdictional requirement, record his satisfaction that there is an income or a potential of an income arising and/or being affected on determination of the ALP of an international transaction or specified domestic transaction before seeking approval of the PCIT or CIT to refer the matter o the TPO for determination of the ALP:

(a) where the taxpayer has not filed the Accountant"s report under Section 92E of the Act but the international transactions or specified domestic transactions undertaken by it come to the notice of the AO;

(b) where the taxpayer has not declared one or more international transaction or specified domestic transaction in the Accountant"s report filed under Section 92E of the Act and the said transaction or transactions come to the notice of the AO; and

(c) where the taxpayer has declared the international transactions or specified domestic transactions in the Accountant"s report filed under Section 92E of the Act but has made certain qualifying remarks to the effect that the sais transactions or specified domestic transactions or they do not impact the income of the taxpayer.

> *In the above three situations, the AO must provide an opportunity of being heard to the taxpayer before recording his satisfaction or otherwise. In case no objection is raised by the taxpayer to the applicability of Chapter X [Section 92 to 92F] of the Act to these three situations, then the AO should refer the international transaction or specified domestic transaction to the TPO for determining the ALP after obtaining the approval of the PCIT or CIT. However, where applicability of Chapter X [Section 92 to 92F] to these three situations is objected to by the taxpayer, the AO must consider the taxpayer"s objections and pass a speaking order so as to comply with the principles of natural justice. If the AO decides in the said order that the transaction in question needs to be referred to the TPO, he should make a reference after obtaining the approval of the PCIT or CIT."*

31 Thus, it appears that the Delhi High Court disagreed with the decision of this High Court rendered in the case of **M/s. Veer Gems (supra)** on the issue whether the A.O. must provide an opportunity of being heard to the taxpayer before recording his satisfaction or otherwise. The Delhi High Court relying on the decision of the Bombay High Court in **Vodafone India Services (P) Ltd (supra)** held that an opportunity of hearing must be given. Whereas, this High Court in **M/s. Veer Gems (supra)** took the view that having regard to the provisions under Chapter X, the A.O. is not obliged in any manner to hear the assessee. The only obligation on the part of the A.O. is to consider the objections of the assessee and only thereafter make a reference to the T.P.O. to compute the Arm's Length Price.

32 We may now look into the decision of this High Court rendered in the case of **M/s. Veer Gems (supra)**. We quote the relevant observations:

> *"13. We do not find any provision under Chapter-X, which would require the Assessing Officer to hear the assessee, consider his objections and only thereafter make a reference to the TPO to compute the arm's length price. As already observed, it is true that the question of reference to the TPO would arise only in the case where there has*

been an international transaction between the assessee and the associated person. Such a question in a given case may also be highly disputed question. However, we do not find that under the scheme of the provision contained in Section-X of the Act, the Assessing Officer is obliged to grant hearing to the assessee, invite and consider the objections with respect to the question whether during the previous year relevant to the assessment year under consideration, there had been any international transaction between the assessee and the associated enterprise before making a reference to the TPO. Such opinion the Assessing Officer would have to form on the basis of available material on record and such opinion would be having ad-hoc finality in the sense that for the purpose of reference to the TPO and till the stage that the TPO passes an order under sub-section (3) of Section 92CA of the At, such issue would be closed.

14. Before making any such reference, sub-section (1) of Section 92C itself provides certain inbuilt safeguards. Firstly, the Assessing Officer has to consider it necessary or expedient to make a reference to the TPO and secondly the reference has to be made with the previous approval of the commissioner. Thus, not only the Assessing Officer before making a reference should be satisfied that with respect to an international transaction entered into by the assessee, it is necessary or expedient to refer the computation of arm's length price to the TPO, such opinion of the Assessing Officer would have to be approved by the Commissioner, before the same can be acted upon. This is one more filter provided by the statute to ensure that the reference is made only in appropriate cases with approval of the higher authority.

15. While framing the assessment in terms of the report submitted by the TPO under sub-section (3) of Section 92CA of the Act, there is nothing to prevent the Assessing Officers from considering the objections of the assessee that, in fact, there had been no international transaction between the assessee and any other person. If the assessee succeeds in establishing such fact, naturally the Assessing Officer would have to drop the entire proceedings in connection with the international transaction.

16. Counsel for the assessee, however, submitted that by virtue of newly substituted sub-section (4) of Section 92CA of the Act, the order passed by the TPO under sub-section (3) of Section 92CA of the Act, is now binding on the Assessing Officer and the Assessing Officer has to proceed to compute the total income in conformity with the arm's length price so determined by the TPO. He pointed out that previously sub-section (4) of Section 92CA of the Act only required the Assessing Officer to compute the total income of the assessee having regard to the arm's length price determined under sub-section (3) of Section 92CA of the Act by the TPO.

17. To our mind, this statutory change has no significant effect on our interpretation recorded hereinabove. By virtue of newly substituted sub-section (4) of Section 92CA of the Act, the Assessing Officer is now bound by the order of the TPO on the computation of the arm's length price of an international transaction, the Assessing Officer is not and cannot be stated to be bound by the opinion of the TPO with respect to the question whether there had, in fact, been an international transaction between the assessee and the associated person during the period under consideration. The TPO is not called upon to and, as held by us, is not competent to decide this issue. This issue is within the sole jurisdiction of the Assessing Officer.

18. The assessee has one more opportunity to contest the question of presence or absence of an international transaction. Under Section 144C of the Act, the Assessing Officer has to forward a draft of the proposed order of assessment to the eligible assessee. The eligible assessee, includes any person in whose case, variation arises as a consequence of the order of the TPO passed under sub-section (3) of Section 92CA of the Act. Thus, in every case of variation of income pursuant to such order of the TPO, the Assessing Officer has to, at the first instance, forward a draft of the proposed order of assessment to the assessee. Under sub-section (2) of Section 144C of the Act, on receipt of such a draft order, the assessee has an option either to file his acceptance of the variation of the assessment or file his objection to any such variation with the Dispute Resolution Panel and also the Assessing Officer. Sub-section (5) of Section 144C of the Act provides that if any objections are raised by the assessee before the Dispute Resolution Panel, the Panel is authorized to issue such direction as it thinks fit for the guidance of the Assessing Officer. Under subsection (6) of Section 144C of the Act, such directions will have to be issued after considering various details provided in Clauses (A) to (G) thereof. Sub-section (8) of Section 144C of the Act provides that the Dispute Resolution Panel may confirm, reduce or enhance the variations proposed on the draft order. Sub-section (11) of Section 144C of the Act provides that no direction under sub-section (5) shall be issued unless an opportunity is given to the assessee and the Assessing Officer. Sub-section (13) of Section 144C of the Act provides that upon receipt of directions issued under sub-section (5) of Section 144C of the Act, the Assessing Officer shall in conformity with the directions complete the assessment proceedings. Section 144C of the Act, thus, provides for complete dispute resolution mechanism to an eligible assessee. He has an option either to accept the variation proposed by the Assessing Officer or to raise objections before the Dispute Resolution Panel. The Dispute Resolution Panel has wide powers of issuing directions under subsection (5) of Section 144C of the Act and to confirm, reduce or enhance the variations proposed under subsection (8) of Section 144C of the Act. Under subsection (13) of Section 144C of the Act, such directions are binding upon the Assessing Officer."

33 It goes without saying as judicial decorum and propriety demand that the judgement rendered by a Coordinate Bench of this Court is binding to us. It would not have taken a minute for us to reject the contention raised by Mr. Soparkar as regards the opportunity of hearing not being given to his client by following the dictum as laid by this High Court in **M/s. Veer Gems (supra).** However, we take notice of something in the judgement rendered by the Delhi High Court in the case of **Indorama Synthetics (supra)** and should not ignore the same. The Delhi High Court has noted in para 20 of its judgement that the C.B.D.T. has accepted the legal proposition as explained by the Bombay High Court in **Vodafone India Services (P) Ltd's case (supra)** and has not given by the decision of the Gujarat High Court in **M/s. Veer Gems's case (supra)**. The Delhi High Court proceeded to note in para 20 that the instruction No.15 of 2015 dated 16th October 2015 issued by the C.B.D.T., which sets out, inter alia, the procedure to be followed by the A.O. has since been replaced by the instruction No.3 of 2016 dated 10th March 2016. The Delhi High Court, thereafter, proceeded to quote para 3.4 of the instruction No.3 of 2016, after referring to para 3.4 of the instruction, the Delhi High Court concluded that the A.O. must provide an opportunity of being heard to the taxpayer before recording his satisfaction or otherwise.

34 If the C.B.D.T. itself has accepted the dictum as laid by the Bombay High Court in **Vodafone India Services (P) Ltd (supra)** and followed by the Delhi High Court in **Indorama Synthetics (supra)**, then, we see no good reason to take the view that no opportunity of hearing is required to be given to the taxpayer by the A.O. before recording his satisfaction or otherwise. Undoubtedly, in the case on hand, a show cause notice was issued by the A.O. and reply was filed by the assessee i.e. the writ

applicant and considering the reply, the A.O., thereafter, proceeded to pass the order of reference to the T.P.O. We are of the view that an opportunity of hearing should have been given by the A.O. before he proceeded to overrule all the objections and refer the matter to the T.P.O.

35 In the aforesaid context, our attention has been drawn to instruction No.2 of 2015 dated 29th January 2015 issued by the C.B.D.T. The same reads thus:

"Instruction No.2/2015

F.No.500/15/2014/APA-I
Government of India
Ministry of Finance
Department of Revenue
Central Board of Direct Taxes
Foreign Tax & Tax Reserch – I Division
APA-I Section

New Delhi, Dated the 29th January, 2015

To
All Principal CcsIT/DsGIT and CcsIT/DsGIT

Madam / Sir

Subject Acceptance of the Order of the Hon'ble High Court of Bombay in the case of Vodafone India Services Pvt. Ltd – reg.

In reference to the above cited subject, I am directed to draw your attention to the decision of the High Court of Bombay in the case of Vodafone India Services Pvt Ltd for AY 2009-10(WP No.871/2014), wherein the Court has held, inter alia, that the premium on share issue was on account of capital account transaction and does not give rise to income and hence, not liable to transfer pricing adjustment.

2 It is hereby informed that the Board has accepted the decision of the High Court of Bombay in the above mentioned Writ Petition. In view of the acceptance of the above judgment, it is directed that the ratio of decidendi of the judgment must be adhered to by the field officers in all cases where this issue is involved. This may also be brought to the notice of the ITAT, DRPs and CsIT (Appeals).

3 This issues with the approval of Chairperson CBDT.

(Anchal Khandelwal)
Under Secretary to the Govt. of India"

36 Having answered the first question posed by us in favour of the assessee, we could have close the judgement at this stage and remitted the matter to the A.O. to consider all the questions a fresh after giving an opportunity of hearing to the assessee. However, we would like to say something as regards the second question also posed by us. We first look into some relevant part of the instruction No.3 of 2016 dated 10th March 2016. We quote the same as under:

"SECTION 92C OF THE INCOME-TAX ACT, 1961 - TRANSFER PRICING - COMPUTATION OF ARM'S LENGTH PRICE - GUIDELINES FOR IMPLEMENTATION OF TRANSFER PRICING PROVISIONS - REPLACEMENT OF INSTRUCTION NO.15/2015

INSTRUCTION NO.3/2016 [F.NO.500/9/2015-APA-II], DATED 10-3-2016

The provisions relating to transfer pricing are contained in sections 92 to 92F in Chapter X of the Income-tax Act, 1961. These provisions came into force w.e.f. Assessment Year 2002-2003 and have seen a number of amendments over the years, including the insertion of Safe Harbour and Advance Pricing Agreement provisions and the extension of the applicability of transfer pricing provisions to Specified Domestic Transactions.

2. In terms of the provisions, any income arising from an international transaction or specified domestic transaction between two or more associated enterprises shall be computed having regard to the Arm's Length Price. Instruction No. 3 was issued on 20th May, 2003 to provide guidance to the Transfer Pricing Officers (TPOs) and the Assessing Officers (AOs) to operationalise the transfer pricing provisions and to have procedural uniformity. Due to a number of legislative, procedural and structural changes carried out over the last few years, Instruction No. 3 of 2003 was replaced with Instruction No, 15/2015, dated 16th October, 2015. After the issuance of Instruction No. 15/2015, the Board has received some suggestions and queries, which have been examined in detail. Accordingly, this Instruction is being issued to replace Instruction No. 15 of 2015. This Instruction is

applicable for both international transactions and specified domestic transactions between associated enterprises. The guidelines on various issues are as follows:

3. Reference to Transfer Pricing Officer (TPO)

3.1 The power to determine the Arm's Length Price (ALP) in an international transaction or specified domestic transaction is contained in sub-section (3) of section 92C. However, section 92CA provides that where the Assessing Officer (AO) considers it necessary or expedient so to do, he may refer the computation of ALP in relation to an international transaction or specified domestic transaction to the TPO or proper administration of the Income-tax Act, the Board has decided that the AO shall henceforth make a reference to the TPO only under the circumstances laid out in this Instruction.

3.2 All cases selected for scrutiny, either under the Computer Assisted Scrutiny Selection [CASS] system or under the compulsory manual selection system (in accordance with the CBDT's annual instructions in this regard -for example. Instruction No. 6/2014 for selection in F.Y 2014-15 and Instruction No. 8/2015 for selection in F.Y 2015-16), on the basis of transfer pricing risk parameters [in respect of international transactions or specified domestic transactions or both] have to be referred to the TPO by the AO, after obtaining the approval of the jurisdictional Principal Commissioner of Income-tax (PCIT) or Commissioner of Income-tax (CIT). The fact that a case has been selected for scrutiny on a TP risk parameter becomes clear from a of the reasons for which a particular case has been selected and the same are invariably available with the jurisdictional AO. Thus, if the reason or one of the reasons for selection of a case for scrutiny is a TP risk parameter, then the case has to be mandatorily referred to the TPQ by the AO, after obtaining the approval of the jurisdictional PCIT or CIT.

3.3 Cases selected for scrutiny on non-transfer pricing risk parameters but also having international transactions or specified domestic transactions, shall be referred to TPOs only in the following circumstances:

(a) here the AO comes to know that the taxpayer has entered into international transactions or specified domestic transactions or both but the taxpayer has either not filed the Accountant's report under section 228 at all or has not disclosed the said transactions in the Accountant's report filed;
(b) where there has been a transfer pricing adjustment of Rs. 10 Crore or more in an earlier assessment year and such adjustment has been upheld by the judicial authorities or is pending in appeal; and

(c) where search and seizure or survey operations have been carried

out under the provisions of the Income-tax Act and findings regarding transfer pricing issues in respect of international transactions or specified domestic transactions or both have been recorded by the Investigation Wing or the AO.

3.4 For cases to be referred by the AO to the TPO in accordance with paragraphs 3.2 and 3.3 above, in respect of transactions having the following situations, the AO must, as a jurisdictional requirement, record his satisfaction that there is an income or a potential of an income arising and/or being affected on determination of the ALP of an international transaction or specified domestic transaction before seeking approval of the PCIT or CIT to refer the matter to the TPO for determination of the ALP:

where the taxpayer has not filed the Accountant's report under section 92E of the Act but the international transactions or specified domestic transactions undertaken by it come to the notice of the AO;

where the taxpayer has not declared one or more international transaction or specified domestic transaction in the Accountant's report filed under section 92E of the Act and the said transaction or transactions come to the notice of the AO; and

where the taxpayer has declared the international transactions or specified domestic transactions in the Accountant's report filed under section 92E of the Act but has made certain qualifying remarks to the effect that the said transactions are not international transactions or specified domestic transactions or they do not impact the income of the taxpayer.

In the above three situations, the AO must provide an opportunity of being heard to the taxpayer before recording his satisfaction or otherwise. In case no objection is raised by the taxpayer to the applicability of Chapter X [Sections 92 to 92F] of the Act to these three situations, then AO should refer the international transaction or specified domestic transaction to the TPO for determining the ALP after obtaining the approval of the PCIT or CIT. However, where the applicability of Chapter X [Sections 92 to 92F] to these three situations is objected to by the taxpayer, the AO must consider the taxpayer's objections and pass a speaking order so as to comply with the principles of natural justice. If the AO decides in the said order that the transaction in question needs to be referred to the TPO, he should make a reference after obtaining the approval of the PCIT or CIT."

37 We may now look into the following:

"Press Information Bureau
Government of India
Cabinet

28 January 2015

Acceptance of the order of the High Court of Bombay in the case of Vodafone India Services Private Limited

The Union Cabinet, chaired by the Prime Miniser Shri Narendra Modi, in a major decision, has decided to accept the order of the High Court of Bombay in the case of Vodafone India Services Private Limited (VISPL) dated 10.10.2014. This is a major correction of a tax mater which has adversely affected investor sentiment.

Based on the opinion of Chief Commissioner of Income-tax (International Taxation), Chairperson (CBDT) and the Attorney General of India, the Cabinet decided to:

i. accept the order of the High Court of Bombay in WP No.871 of 2014 dated 10.10.2014 and not to file SLP against it before the Supreme Court of India.

ii. accept of orders of Courts / IT AT / DRP in cases of other taxpayers where similar transfer pricing adjustments have been made and the Courts / IT AT / DRP have decided in favour of the taxpayer.

The Cabinet decision will bring grater clarity and predictability for taxpayers as well as tax authorities, thereby facilitating tax compliance and reducing litigation on similar issues. This will also set at rest the uncertainty prevailing in the minds of foreign investors and taxpayers in respect of possible transfer pricing adjustments in India on transactions related to issuance of shares, and thereby improve the investment climate in the country.

The cabinet came to this view as this is a transaction on the capital account and there is no income to be chargeable to tax. So applying any pricing formula is irrelevant.

VISPL is a wholly owned subsidiary of a non-resident company, Vodafone Tele-Services (India) Holdings Limited, Mauritius. On 21.8.2008, VISPL issued shares (at a premium of Rs.8509/-) which resulted in VISPL receiving a total consideration of Rs.246.39 crore

from Vodafone Mauritius, on issue of shares and this was shown as "Capital Receipts" in the books of accounts. VISPL reported this transaction as an "International Transaction" and stated that this transaction does not affect its income.

The Transfer Pricing Officer (TPO), vide order dated 28.10.2013, determined the Arm's Length Price of the shares issued by VISPL on the basis of Net Asset Value, at Rs.53,775/- per share and made an upward adjustment of Rs.1,308.91 crore. In addition, the difference Rs.1,308.91 crore between the transaction price and the Arm's Length Price was treated as 'deemed loan' given by VISPL to the holding company; and interest that would have been payable on the loan in an arm's length transaction was computed at Rs.88.35 crore. In total, transfer pricing adjustment of Rs.1,397.26 crore was proposed by the TPO for Assessment year 2009-10. the matter was agitated by VISPL at the stage of Draft AO itself and therefore the tax payable could not be crystallized. However, the tax rate of 33 percent was applicable for Assessment Year 2009-10.

The DRP, on 11.2.2014, held that the premium determined by the TPO, to the extent not received, is an income arising from issue of shares, and that the AO and the TPO have jurisdiction.

VISPL filed a 2nd Writ Petition in the High Court of Bombay. The High Court on 10.10.2014, has amongst other things observed:

a) "Section 92(2) of the Act deals with a situation where two or more AEs enter into an arrangement whereby they receive a benefit, service or facility then the allocation, apportionment or contribution towards the cost or expenditure is to be determined in respect of each AE having regard to ALP. It would have no application in the cases like the present one, where there is no occasion to, allocate, apportion or contribute any cost and/or expenses between the petitioner and the holding company."

b) The crucial words "shall be chargeable to income tax" which are found in Section 42(2) of the 1922 Act are absent in Chapter X of the Act…. Therefore it is clear that the deemed income which was charged to tax under Section 42(2) of 1922 Act was done away with under this Act."

c) The tax can be charged only on income and in the absence of any income arising, the issue of applying the measure of Arm's Length Pricing to transactional value / consideration itself does not arise."

d) If its income which chargeable to tax, under the normal provisions of the Act, then alone Chapter X of the Act could be invoked. Sections 4 and 5 of the Act brings / charges to tax total income of the previous year. This would take us to the meaning of the word income under the Act as defined in Section 2(24) of the Act. The amount received on issue of shares is admittedly a capital account transaction not separately brought within the definition of income, except in cases covered by Section 56(2)(viib) of the act. Thus such capital account cannot be brought to tax as already discussed herein above while considering the challenge to the grounds as mentioned in impugned order."

e) The issue of shares at a premium is on capital account and gives rise to no income. The submission on behalf of the revenue that the shortfall in the ALP as computed for the purposes of Chapter X of the Act is misplaced. The ALP is meant to determine the real value of the transaction entered into between AEs. It is a re-computation exercise to be carried out only when income arises in case of an international transaction between AEs. It does not warrant re-computation of a consideration received / given on capital account.

The Bombay High Court quashed the reference dated 11.7.2011 by the AO to the TPO, order dated 28.1.2013 of the TPO, draft AO dated 22.3.2013 of the AO and order dated 11.2.2014 of the DRP on the preliminary issue of jurisdiction to tax, setting them aside as being without jurisdiction, null and void."

38 The following is discernible from the aforesaid:

[a] The tax can be charged only on income and in the absence of any income arising, the issue of applying the measure of Arm's Length Pricing to the transactional value / consideration itself would not arise.

[b] If income is noticed, chargeable to tax under the normal provisions of the Act, then, alone Chapter X of the Act could be invoked.

39 We find substance in the contention raised by Mr. Soparkar that the A.O. could be said to have overlooked or rather ignored the

jurisdictional requirement of a satisfaction in accordance with para 3.4 of the instruction No.3 of 2016 referred to above that there ought to be an income or potential of an income arising and/or being affected on determination of the A.L.P. of an international transaction or specified domestic transaction. In the absence of such satisfaction being recorded in the order disposing of the objections, the reference to the T.P.O. would also be without jurisdiction. We take notice of the fact that in the objections, a specific plea in this regard was taken, however, we do not find a word in this regard in the order disposing of the objections. On this issue, the only reply of the learned Senior Counsel appearing for the Revenue is that the same is self-serving and adherence the record. In other words, the only argument is that the Arm's Length Price on the interest paid would have bearing on the income. We are not convinced with such stance of the Revenue.

40 For all the foregoing reasons, we allow the present writ application. The impugned reference by the respondent No.1 to the respondent No.2 is hereby quashed and set aside and the notice dated 20th December 2019 (Annexure : 'A' to this writ application) is also quashed and set aside. The proceedings are remitted to the A.O. for fresh consideration of the matter and the issues as discussed in the present order. The A.O. shall give an opportunity of hearing to the assessee and thereafter, proceed to pass a reasoned order or a speaking order dealing with the objections in accordance with law.

41 Let the aforesaid exercise be undertaken within a period of four weeks from the date of receipt of the writ of this order. We clarify that on the point of limitation, we agree with the Revenue as discussed above.

42 In view of the final disposal of the writ application, the connected

Civil Application would not survive and the same stands disposed of.

(J. B. PARDIWALA, J)

(ILESH J. VORA,J)

CHANDRESH