


CA Tarunkumar Singhal & Sunil Moti Lala, *Advocate*

INTERNATIONAL TAXATION
Case Law Update

A. HIGH COURT

1. 'On-spot' control and supervision exercised by the company to whom the employees are deputed is not the deciding factor for determining the real employer, rather the right to terminate the service of the employee is a relevant factor. Accordingly, Indian employer having deputed his employees to Kuwait based company was not liable to deduct TDS u/s. 195 on salary payments to such non-resident employees working outside India

Pr. CIT vs. Smt. Supriya Suhas Joshi – [TS-202-HC-2019(Bom)] – Income Tax Appeal No. 382 of 2017

Facts

(i) The assessee, a sole proprietor, had entered into an agreement with a Kuwait based company for providing manpower to the said company as per its requirements. As per the individual contract executed for supplying the person, the said company paid a fixed sum to the assessee, out of which the assessee remunerated the employee.

(ii) The AO opined that the assessee ought to have deducted TDS u/s. 195 while making payment to the deputed employees and thus made a disallowance u/s. 40(a)(ia) (sic).

(iii) The assessee contended that the persons deputed were in employment with the assessee and were only loaned to the Kuwait based company to carry out work as per the requirement of the said company and the payment to such deputed employees who were all non-residents were towards their salary. Accordingly, since payments of income chargeable under the head "Salaries", are specifically excluded from the scope of section 195, there was no liability to deduct tax under the said section. [N.B.- As evident from the Tribunal order, before lower authorities, it was also submitted that since the employees were working outside India and remunerations were paid to them from assessee's bank account situated outside India, no income had accrued / arisen in India so as to attract TDS provisions of section 192 as well as 195. However, there is no finding in the Tribunal order or the High Court order in this regard].

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(iv) The CIT(A) and the Tribunal accepted assessee's contention and decided in her favour.

(v) Aggrieved, the Revenue filed an appeal before the High Court.

Held

(i) On perusal of the contract, the Court held that the contract indicated that the deputed person was the employee of the assessee. It noted that (i) as per the preamble of the contract, the assessee had supplied Commissioning Engineer (employee) to the said company on deputation basis for its on-going project (ii) deputation charges of US $5500 per month was payable to the assessee, out of which US $4000 per month was paid to the employee and the balance was retained by the assessee.

(ii) The Court rejected Revenue's contention that looking to the supervision and control of the Kuwait based company over the employee, it must be held that he was under the employment of the said company and not that of the assessee. It held that the test of the extent of control and supervision of a person by the engaging agency are undoubtedly relevant factors while judging the question whether the person was an agent or an employee. However, in a situation where the person employed by one employer is either deputed to another or is sent on loan service, the question of dual control would always arise. In such circumstances, the mere test of on-spot control or supervision in order to decide the correct employer may not succeed.

(iii) The Court held that it was inevitable that in a case as the present one, the Kuwait based company would enjoy considerable supervising powers and control over the employee as long as the employee was working for it. Neverthless, the assessee continued to enjoy the employer-employee relationship with the said person. It supported the above conclusion by stating that for example, if the work of such person (employee) was found to be wanting or if there was any complaint against him, it would only be the assessee who could terminate the service.

(iv) Accordingly, it dismissed Revenue's appeal.

2. Amount received from an Indian company by the non-resident assessee on account of reimbursement of service tax paid by it is not taxable as it does not form part of the 'amount' specified in section 44BB(2)

DIT (International Tax) vs. Schlumberger Asia Services Ltd. [(2019) 104 taxmann.com 353 (Uttarakhand)] – IT Appeal Nos. 40 of 2012 & 44 of 2014 & Others.

Facts

(i) The assessees, being companies incorporated outside India, were non-residents within the meaning of the Act. They execute contracts all over the world, including in India, in connection with exploration and production of mineral oils. They entered into agreements with ONGC for giving rigs / plant & machinery on hire.

(ii) The assessees filed their returns declaring income from charter hire of the rig / plant and machinery, to be used in the extraction or the production of mineral oils in India, and offered to pay tax under section 44BB(1) r.w.s. 44BB(2) of the Act. While doing so, the assessees did not include the amounts reimbursed to them by the ONGC (towards the service tax paid by them earlier to the Government of India) in their gross revenues for computing income under section 44BB of the Act.

(iii) The AO, however, included the said amount in the assessees' gross receipts, and subjected it to tax under section 44BB of the Act.

(iv) The question before the Court was whether the amount reimbursed to the assessee

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by ONGC, representing the service tax paid by the assessee to the Government of India, should be included in computing the amount referred to in section 44BB(2) of Act being amounts paid to non-resident assessees on account of provision of services and facilities in connection with, or supply of plant and machinery on hire used, in the prospecting for, extraction or production of mineral oils in India.

Held

(i) The Court held that service tax, collected by the assessee, did not fall within the scope of the amount received on account of 'provision of services and facilities', as specified in section 44BB(2) since reimbursement of service tax was not on account of services rendered but was a statutory duty imposed on the assessee. Accordingly, it held that service tax does not fall within the "amount" stipulated in section 44BB(1) of the Act since the assessee only collected service tax from ONGC and paid it to the Government and such reimbursement did not contain any element of profit or income in it.

(ii) It relied on the CBDT Circulars dated 28-4-2008 and 13-1-2014 directing that tax should be deducted at source only on the net amount paid towards rent (under section 194-I) or as fees for services rendered by the service provider (under section 194-J), i.e. the total amount paid less service tax, for the reason that service tax, on such payment, was not "income". The Court held that the Circulars issued by the CBDT reflected its understanding that service tax paid by the assessee was not "income" and thus service tax would not form part of the amounts referred to in Section 44BB(2) of the Act.

iii Accordingly, the Court decided the issue in favour of the assessees.

3. Though, ordinarily, the final culmination of the MAP could not be projected in the determination of ALP without any adjustment, however, since (i) the MAP had considered all relevant aspects and (ii) the APA for subsequent year also mentioned that MAP outcome applicable for US based transactions would be applicable for the non-US based transactions, Revenue could not argue the contrary in the impugned year (i.e., prior year)

PCIT vs. J.P. Morgan Services India Pvt. Ltd. [TS-228-HC-2019(Bom)-TP] – ITA No 4 & 170 of 2017

Facts

(i) The assessee-company was inter alia engaged in providing Information Technology Enabled Service (ITES) to its Associated Enterprise (AE) and 96% of its transactions were with US based AE and remaining 4% with non-US based AEs.

(ii) The US based AE had initiated Mutual Agreement Procedure (MAP) proceedings under Article 27 of the India-USA DTAA which culminated into an order being formally passed in this regard i.e., for 96% of transactions.

(iii) In appeal filed before the Tribunal, against the adjustment made by the TPO (and confirmed by the DRP) to the international transaction of rendering ITES to AEs, the assessee contended that the parameters which were considered for determining the ALP in the MAP proceedings for US based transactions should also be accepted for the non-US based transactions.

(iv) The Tribunal accepted the assessee's contention noting that no distinction had been made by assessee as well as the lower authorities between US and non-US transactions.

(v) Aggrieved, the Revenue filed an appeal before the High Court against the Tribunal's aforesaid approach of applying parameters

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of US based transactions to the non-US based transactions also.

Held

(i) At the outset, the Court held that in absence of any other material on record, it doubted if the final culmination of the MAP could be projected in the determination of ALP in the mechanism envisaged under the Act, that too, without any other adjustment or consideration.

(ii) However, noting that (i) the MAP had been drawn after consideration of relevant aspects giving rise to transfer pricing and (ii) in the Advance Pricing Agreement (APA) entered into between the assessee and the CBDT for subsequent year, it was specifically mentioned that outcome agreed under the MAP proceedings for international transactions with US based AEs would also be applicable for transactions with non-US based AEs, the Court held that it was wholly inappropriate to allow Revenue to argue the contrary in the impugned year.

(iii) Accordingly, it dismissed Revenue's appeal.

4. Rolta India Ltd. and KLG Systels Ltd. cannot be considered as comparable to a company engaged in IT enabled design engineering services as they are functionally different

Pr. CIT vs. Dona India Technical Centre Pvt. Ltd. [TS-315-HC-2019(Bom)-TP] – Income Tax Appeal No. 308 of 2017

Facts

(i) The assessee was engaged in the business of providing IT enabled design engineering services. The TPO included Rolta India Ltd. and KLG Systels Ltd. in the set of comparables while benchmarking the aforesaid services.

(ii) The assessee objected to such inclusion on the ground that functionality of the two companies was different since they were engaged in entirely differently areas.

(iii) The Tribunal accepted assessee's contention, following the Co-ordinate Bench decision in the case of *Behr India Ltd. vs. Addl. CIT [ITA No. 1376/PN/2010 & 568/PN/2013]* wherein it was held that Rolta India Ltd. and KLG Systels Ltd. had to be excluded as comparable as both these companies were functionally different than the concern providing IT enabled design engineering services. Thus, it held that the said companies were not comparable on account of distinct nature of business, functional dissimilarity, size and diversified products.

(iv) Aggrieved, the Revenue filed an appeal before the High Court.

Held

(i) The Court noted that on the facts of the case, the Tribunal had reached the conclusion that Rolta India Ltd and KLG Systels Ltd. were not comparable since they were functionally different.

(ii) Further, noting that Revenue had not filed an appeal against the Tribunal's earlier decision in the case of Behr India Ltd. (supra), on which reliance was placed by the Tribunal, the Court dismissed Revenue's appeal.

5. IRCA Management Consultancy Services Ltd. and Kinetic Trust Ltd. are comparable to a company engaged in providing non-binding investment advisory services

Pr. CIT vs. Temasek Holdings Advisors India Pvt. Ltd. [TS-316-HC-2019 (Bom)-TP] – Income Tax Appeal No. 304 of 2017

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Facts

(i) The assessee was *inter alia* engaged in providing non-binding investment advisory services to its AE. It had disclosed a mark-up margin of 21.4% with respect to the aforesaid international transaction and arrived at an arm's length margin of 14.84% based on 7 comparables selected by it.

(ii) During assessment, the TPO *inter alia* excluded IRCA Management Consultancy Services Ltd. and Kinetic Trust Ltd. (forming part of the aforesaid 7 comparables) from the set of comparable companies on the grounds that (i) IRCA Management Consultancy Services Ltd. - was engaged in various fields of advisory which the assessee was not performing and (ii) Kinetic Trust Ltd. - had a very low turnover.

(iii) The TPO had also added a 3% mark-up to the average of comparable margins determined by him on the ground that the assessee, in addition to investment advisory services, had also rendered portfolio management services and for such additional function it should have earned higher revenue.

(iv) The Tribunal accepted the assessee's contention for inclusion of the aforesaid two companies, holding that (i) providing advisory / consultancy services in various fields did not materially affect the revenue or net profits of IRCA Management Consultancy Services Ltd. and thus it was functionally comparable and (ii) Kinetic Trust Ltd., was functionally comparable and since the assessee as well as TPO had not applied turnover filter at the time of selection process, the same could not be used at a later stage as a tool for cherry picking.

(v) It also relied on the Co-ordinate Bench decision in the assessee's own case for earlier assessment years wherein also these companies were included in the set of comparables despite Revenue's opposition.

(vi) Further, the Tribunal deleted the 3% mark-up added by the TPO, noting that the asssessee had not performed any additional function which was not included in the investment advisory services.

(vii) Aggrieved, the Revenue filed an appeal before the High Court.

Held

(i) The Court dismissed Revenue's ground of appeal pertaining to inclusion of IRCA Management Consultancy Services Ltd. and Kinetic Trust Ltd. as comparable, noting that it had earlier also dismissed Revenue's appeal against the Tribunal's order for earlier year on the same issue.

(ii) It also dismissed Revenue's appeal against the deletion of 3% mark-up adopted by the TPO, relying on the Tribunal's finding that there was no evidence that the assessee had rendered any additional services.

B) Tribunal Decisions

6. India–UK DTAA – Taxability of Fees for Technical Services – Application of the Concept of "Make Available" – Tribunal accepts applicability of "make available" condition to development and transfer of technical plan or design – Held in favour of the assessee

Buro Happold Limited vs. DCIT [TS-76-ITAT-2019 (Mum)] Assessment Year : 2012–13

Facts

(i) The assessee, a company incorporated in the UK and a resident in the UK, is involved in the business of providing engineering design and consultancy services to Indian customers through its Indian affiliate, BHEI. As a part of such services, the assessee provides structural and MEP (Mechanical, Electrical and Public Health) engineering for various buildings. For the tax year under consideration, the assessee filed its return of income declaring NIL income.

(ii) In the course of assessment proceedings, the AO observed that the assessee had earned INR 10.9m by way of providing consulting engineering services to BHEI and had also received INR 10.1m from BHEI as a cost recharge towards common expenses incurred at the head office (HO expense).

(iii) The assessee submitted that since it had not made available any technical knowledge or skill to BHEI while providing engineering consultancy services, such amount would not qualify as FTS and has to be characterised as business income under the DTAA. Such business income cannot be brought to tax in India in the absence of a PE of the assessee in India. The assessee further submitted that the amount received towards HO expense is not taxable in India, since such amount is a part of cost allocation made on a cost-to-cost basis without any profit element.

(iv) The Revenue contended that:

- The services include supply of design/drawing to BHEI and the provision of other services are ancillary to the supply of designs and drawings. BHEI is responsible to the Indian customers and BHEI had sub-contracted certain specialised services (like master planning, acoustic engineering, environmental engineering etc.) to the assessee, in the absence of the necessary skills with BHEI.
- As per the DTAA, payment received for development and transfer of a technical plan or a technical design would be in the nature of FTS, irrespective of whether it also makes available technical knowledge, experience, skill, knowhow, etc. Furthermore, since the assessee provided technical/ engineering consultancy advice as well as technical design to BHEI, enabling it to further apply and re–apply such technology for rendering services to its customers in India, the condition of "making available" was satisfied.
- The cost recharge relates to and is ancillary to the provision of consulting engineering services which has been held to be in the nature of FTS and, hence, taxable in India.
- The CIT(A) agreed with the Tax Authority's contention on the premise that provision of a specific design and drawing requires application of mind by various technicians having knowledge in the field of architectural, civil, electrical and electronic and overseeing its implementation and execution at site in India by the assessee's technical personnel would amount to making available technical services.

Decision

On assessee's appeal, the Tribunal held in its favour as follows:

(i) The Tribunal held that the amount received towards consulting engineering services is not in the nature of FTS under the DTAA, since the assessee did not "make available" technical knowledge, experience, skill, knowhow or processes to BHEI, through the development and supply of a technical plan or a technical design. Such amount should be treated as "business profits" and in the absence of a PE of the assessee in India, it cannot be brought to tax. Similar conclusion applies in respect of cross-charge of HO expense which is in the nature of FTS.

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(ii) The Tribunal observed as follows:

a) A careful reading of the FTS Article of the DTAA clarifies that the words "development and transfer of a technical plan or technical design" is to be read in conjunction with "make available technical knowledge, experience, skill, knowhow or processes".

b) As per the rule of *ejusdem generis,* the words "or consists of the development and transfer of a technical plan or technical design" will take colour from "make available technical knowledge, experience, skill, knowhow or processes".

c) Technology is considered to have been made available when the recipient of such technology is competent and authorised to apply the technology contained therein independently as an owner, without recourse to the service provider in the future.

d) The technical designs/drawings/plans supplied by the assessee are project-specific and cannot be used by BHEI in any other project in the future. Thus, the assessee has not made available any technical knowledge, experience, skill, knowhow or processes while developing and supplying the technical drawings/designs/plans to BHEI.

(iii) Reliance was placed on the Pune Tribunal decision in the case of *Gera Developments Pvt. Ltd. [(2016) 160 ITD 439 (Pune)]* in the context of the FTS Article under the India-US DTAA, wherein it was held that mere passing of project-specific architectural, drawings and designs with measurements does not amount to making available technical knowledge, experience, skill, knowhow or processes. Unless there is transfer of technical expertise skill or knowledge along with drawings and designs and if the assessee cannot independently use the drawings and designs in any manner whatsoever for commercial purpose, the payment received cannot be treated as FTS.

7. Section 56(2)(viia) – Rule 11UA – Section 28(iv) – Levy of MAT – Decision on taxability of composite scheme of arrangement which includes demerger and amalgamation in favour of the assessee

M/s. Aamby Valley Ltd. vs. ACIT [TS-80-ITAT-2019 (Del.)] Assessment Year 2012-13

Facts

(i) The assessee belongs to Sahara Group of companies. The assessee is engaged in the business of construction as developers, colonisers and contractors in the field of residential and commercial complexes, townships together with all allied infrastructure. The assessee is also engaged in the business of running of resorts and other hospitality services, etc.

(ii) The assessee had a 100 per cent subsidiary which in turn had eight subsidiaries and three step-down subsidiaries. The assessee along with wholly owned subsidiary and the Special Purpose Vehicles (SPVs) and step-down subsidiaries filed a composite scheme of arrangement before the Bombay High Court for demerger of various business undertakings from the assessee (along with all related assets, liabilities, employees, development rights, licenses, permits and registration etc.) to the SPVs and the step-down subsidiaries and amalgamation of the WOS with the assessee with effect from 31st March, 2011 (appointed date) on a going concern basis. The scheme was sanctioned by the High Court *vide* its order dated 20th January, 2012.

(iii) Pursuant to the amalgamation, the assessee received the shares of SPVs which were recorded in the books of the assessee at fair value. The excess credit arising out of the recording of assets and liabilities at fair values was credited to a general reserve. The assessee did not offer any income in its return of income since according to the assessee there was no income or gain arising out of the said composite scheme of arrangement and amalgamation.

(iv) The Assessing Officer (AO) observed that the assessee had received the shares of SPV's without consideration or inadequate consideration. The AO made the addition for the same under the provisions of Section 56(2)(viia) of the Act. The value of the shares was determined in accordance with Rule 11UA of the Income-tax Rules, 1962 (the Rules) by taking the FMV as on 31st March, 2012 ignoring the fact that the scheme was operative from 31st March, 2011.

(v) The Dispute Resolution Panel (DRP) upheld the order of the AO. Further, the DRP held that increase in general reserve on account of fair valuation of shares received on amalgamation, represent business profits and was taxable under Section 28(iv) of the Act. The DRP held that the amount carried to any reserve is required to be added back to the book profit since the creation of reserve was not routed through P&L account. Merely because it was not passed through the P&L account, it should not escape the requirement of Minimum Alternate Tax (MAT).

Decision

On assessee's appeal, the Tribunal held in its favour as follows:

(i) Re: Year of taxability

a) The Tribunal held that all the assets of the amalgamating company would vest in the assessee amalgamated company with effect from the appointed date which is 31st March, 2011. The transferor-company carrying on business and holding the assets on behalf of the transferee-company from the appointed date and the scheme would be effective from the appointed date.

b) The determination of the FMV of the assets of the demerged undertaking as well as recording of the entries in respect of the transfer and vesting of the assets in the SPVs will not change the appointed date as well as date of transfer and vesting of the properties for all the intending purposes because the transfer would be valid from the appointed date only.

c) Accordingly, transaction of the composite scheme of arrangement and amalgamation takes place in the previous year relevant to the AY 2011-12 and no transaction took place in the previous year relevant to assessment year under appeal, i.e. AY 2012-13. Therefore, no addition could be made in assessment year under appeal under any of the provisions of law.

(ii) Re: Taxability of amount credited to general reserve as business profits.

a) For taxability of net increase in general reserve within the provisions of Section 28(iv) of the Act, it is necessary that benefit or perquisite must arise from carrying on the business or profession. If any benefit or perquisite does not arise from the business or profession carried on by the assessee, the provisions of Section 28(iv) of the Act cannot be applied. The intention of the Legislature is not to apply the provisions of Section 28(iv) to a case where there is an increase in the general reserve arising due to the recording of the shares in the balance sheet of the assessee at their market

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value. When a company is amalgamated with the other company, the activity cannot be regarded as a business transaction.

b) Relying on the decision of the Supreme Court in the case of *Godhra Electricity Co. Ltd. vs. CIT [1997] 225 ITR 746 (SC)* it was observed that an increase in general reserve did not give rise to any real income to the assessee. It is capital in nature. The general reserve arisen was due to the recording of investments held by the amalgamating company at its FMV. It did not give rise to any real income to the assessee.

(iii) Taxability under the provisions of Section 56(2)(viia) of the Act

a) The provisions of Section 56(2)(viia) of the Act were brought into the statute to curb bogus capital building and money laundering to prevent the practice of transferring unlisted shares at prices much below their market value. For the transfer of shares, there must be a transferor and transferee and transferred assets, i.e., shares. In the case of amalgamation, it cannot be said that there is a transfer of shares as there is only statutory vesting of the assets by virtue of the amalgamation scheme.

b) In the instant case, due to the composite scheme of arrangement and amalgamation, it cannot be said that there was no consideration or inadequate consideration. In fact, due to the arrangement, the assessee transferred the assets of various undertakings to SPVs and in consideration thereof, acquired the shares of SPVs through a subsidiary and through this process, the shares of subsidiary held by the assessee got substituted with the shares of various SPVs which were being earlier held by the subsidiary.

c) The market value of the shares received by the assessee is not higher than the market value of the undertaking (which was transferred by the assessee to various SPVs) to qualify for the provisions of Section 56(2)(viia) of the Act.

d) Section 56(2)(viia) of the Act excludes the transaction of business reorganisation and amalgamation which are not regarded as a transfer under the provisions of Section 47 of the Act. The exemption to the shareholder was available only if the consideration for amalgamation was received in the form of shares of the amalgamated company. However, this condition of allotment of shares could not be complied with in a scenario where the amalgamated company itself is a 100 per cent shareholder of the amalgamating company, thereby leading to ambiguity on the applicability of the amalgamation exemption provision.

e) To remove this ambiguity, the exemption provisions were amended by the Finance Act 2012, by specifically inserting the clause that issuance of shares by the amalgamated company is not required to fall within the amalgamation exemption provision where the amalgamated company itself is a 100 per cent shareholder of the amalgamating company. The Tribunal observed that the amendment to remove defect was retrospective in nature and it was clarificatory in nature and it is applicable from AY 2011-12, even though the amendment was made with effect from AY 2013-14.

f) The Tribunal held that provisions of Section 56(2)(viia) of the Act could not be applied in respect of the transaction undertaken by the assessee as it was covered under Section 47(vii) of the Act.

g) Without prejudice to the above, the Tribunal held that if an addition was made under Section 56(2)(viia) of the Act, the balance sheet as on 31st March, 2011 has to be considered for the purpose of determining the value of the property under Rule 11UA of the Rules.

(iv) Taxability for the purpose of MAT

Relying on the decision of the Supreme Court in the case of *Apollo Tyres Ltd. vs. CIT [2002] 255 ITR 373 (SC)*, it was held that the net reserve in the general reserve for which the addition was made was not debited to the profit and loss account and it was directly credited to general reserve, such amount cannot be added to the profits while computing book profits under the provisions of MAT.

8. Mumbai Tribunal – Territorial nexus must for Section 9 taxability; Restores profit attribution of agency-commission

Fox International Channel Asia Pacific Ltd. vs DCIT [TS-84-ITAT-2019(Mum)] Assessment Year : 2010–11

Facts

(i) The assessee, a foreign company (tax resident of Hong Kong) was engaged in distribution of satellite television channels and sale of advertisement air time for the channel companies at global level. Assessee was not a channel owner but is a service provider to group companies like Star Movies, Star World, etc. The channel companies had appointed the assessee as an agent to sell the advertisement air time on the channels, to distribute the channels in the territories where the channels were being broadcast and to procure syndication revenues in respect of the contents of the channels.

(ii) In the relevant year the assessee earned revenue from management fee, advertising fee, agency commission and other income in the nature of royalty and being a non-resident company, it was not required to maintain India Specific Financial Statement.

(iii) In course of assessment proceedings, the Assessing Officer (AO), noticing that the assessee earned revenue from international transaction with its Associated Enterprise (AE) in India made a reference to the Transfer Pricing Officer (TPO) for determining the arm's length price (ALP) of the international transactions. The consolidated profit computed as a percentage of total revenue earned by the channel companies from India during the 12 months period from April 2009 to March 2010, resulted in an overall profit rate of 28.17%. After verification, the TPO accepted PSM as the most appropriate method. He also noted that though under PSM there is no need to further benchmark the profitability against the comparables, however, with a view to demonstrate its *bona fide* and clear all doubts, the assessee had compared its profitability with nine external comparables, whose average margin worked out to 7.28%. Out of the 9 comparables, TPO shortlisted 5 and arrived at a mean margin of 23.81%. Noting assessee's margin to be higher, TPO concluded that no adjustment is required to be made to the value of the international transaction entered into by the assessee.

(iv) TPO accepted assessee's determination of ALP at ₹ 252.59 crore under PSM as per TP-analysis, however found that in the computation of income, it offered to tax in India an amount of ₹ 227.80 crore. Accordingly, he held that the differential amount of ₹ 24.79 cr, should be treated as adjustment to the ALP. In pursuance of TPOs order, AO passed draft assessment order making an upward TP-adjustment of the differential amount of ₹ 24.79 crore.

(v) Assessee filed its objections with DRP submitting that the amount of ₹ 24.79 crore represents agency commission fee towards services provided outside India and received outside India and hence, cannot be treated as income u/s. 7 or 9 and is not chargeable to tax in India. It was submitted, since the agency commission fee is not an income chargeable to tax under the provisions of the Act, it cannot be considered as an international transaction u/s. 92B(1) and therefore, the TPO had no jurisdiction to take cognizance of such transactions and carry out adjustment. DRP observed that in view of *Explanation* below section 9(2), income of a non-resident shall be deemed to accrue or arise in India whether or not the non-resident has a residence or place of business or business connection in India or has rendered services in India. Thus, DRP upheld TPO's adjustments.

(vi) Before ITAT, assessee submitted that ALP of an international transaction has to be determined purely on the basis of income sourced from India. Assessee further submitted that TPO found the consolidated profit of 28.17% of the specified AEs in respect of India / Global Revenue to be at ALP and hence, has not proposed any adjustment to the arm's length price. He submitted that latching on to a mistake committed in Annexure-1 to the transfer pricing study report while mentioning "arm's length profit attributable to India", the Transfer Pricing Officer has actually considered the global profit of the assessee amounting to ₹ 252 crore. Assessee submitted that the income of ₹ 227.80 crore offered by the assessee represents the arm's length price profit attributable to India. Assessee submitted that the observations of the DRP that the assessee has admitted the amount of ₹ 252.59 crore as the profit attributable to India is a total misconception of fact and on a wholly wrong reading of the transfer pricing study report and that assessee has at no stage admitted that the profit attributable to India is ₹ 252.59 crore.

(vii) Assessee submitted, it is not the duty of the TPO to see what income is deemed to accrue or arise in to India, which is the job of the AO. It was further submitted that, under PSM, profit attributable to the income sourced from India has to be split and once the TPO has concluded that the margin shown by the assessee @ 28.17% is at arm's length and no adjustment to the arm's length price is required, he should not have recommended any further adjustment on the basis of global income.

viii) Assessee relied on a host of rulings in support of its contention that the agency fee commission of ₹ 24.79 crore being received outside India on services rendered outside India is not taxable in India and that the duty of the TPO is to determine the arm's length price only. Assessee further relied on Co-ordinate Bench decision in assessee's own case for AY 2007-08 wherein it was held that PSM will apply to India sourced income and thus, income earned / received for services rendered outside India cannot be brought to tax in India.

Decision

On Appeal, the Tribunal held in favour of the assessee as under:

(i) ITAT observed that in coming to his conclusion that the profit attributable to the Indian operations of the assessee is ₹ 252.59 crore and not ₹ 227.80 crore as offered by the assessee in the ROI, TPO has solely relied on Annexure - I to the TP study report wherein revised computation of consolidated net profit compared to the total India / Global Revenues earned by the channel companies and the overall profitability for the period FY 2009-10 has been reflected and an amount of ₹ 252.59 crore has been shown as the ALP attributable to India in case of the assessee.

(ii) ITAT rejected DRP's observation that section 9 can even bring to tax net income which does not accrue or arise in India but accrues or arises outside India as *Explanation* to

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section 9(2) of the Act, inserted by Finance Act 2010, with retrospective effect from 1st June 1976, has widened the scope of section 9 to the extent that the income of non-resident shall be deemed to accrue or arise in India whether or not the non-resident has a residence or place of business or business connection in India or the non-resident has carried on business operation in India.

(iii) ITAT observed that if the provisions of section 9 was read as a whole, it would be clear that as per *Explanation* 1 to section 9(1)(i), in case of an assessee whose business operations were not exclusively carried out in India, the amount of income which will be deemed to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India. Therefore, the income which is deemed to accrue or arise in India must have a territorial nexus.

(iv) ITAT noted that agency / marketing commission paid to non-residents agent outside India and for services rendered outside India is not taxable in India. Moreover, on careful reading of the provision contained in *Explanation* below section 9(2), it would be clear that it will not be applicable to the agency commission earned by the assessee.

(v) ITAT noted Revenue's claim that assessee itself has admitted that the profit attributable to India is ₹ 252.59 cr while assessees claimed that the profit attributable to India is ₹ 227.80 cr and placed reliance on its transfer pricing study report. ITAT observed that the actual profit attributable to India is a purely factual issue which has to be demonstrated by the assessee through proper documentary evidences / books of account, and hence, for the limited purpose of verifying this fact, ITAT restored the issue to the AO to examine assessee's claim. ITAT clarified that in the event, the claim of the assessee that actual profit attributable to India is ₹ 227.80 crore is found to be correct, no further adjustment can be made to the arm's length price since the TPO himself has concluded that the profit margin of the international transaction shown by the assessee is higher than the average margin of the comparables.

(vi) Finally, ITAT stated that since, there is no dispute between the parties with regard to the most appropriate method selected by the assessee as well as profit margin shown and the dispute is only with regard to the factual issue relating to the actual profit attributable to India under PSM, it is not necessary to deal with assessee's contention regarding powers of the TPO to determine the profit attributable to India.

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