The Dy. Cit, Circle-1(1)(2),, ... vs Cadila Healthcare Ltd.,, Ahmedabad on 3 March, 2017

IT (TP) Nos.519 and 898/A
and 694 and 747/A
Assessment years: 2009-10 and

Page

IN THE INCOME TAX APPELLATE TRIBUNAL
AHMEDABAD I BENCH, AHMEDABAD
[Coram: Pramod Kumar AM and S S Godara JM]

IT (TP) No. 898/Ahd/2014 and 694/Ahd/2015
Assessment year: 2009-10 and 2010-11

Cadila Healthcare Limited ....App
Zydus Tower, Opp ISKON Temple,
Satellite Cross Road, Ahmedabad 380 015
[PAN: AAACC6253G]

Vs.

Assistant Commissioner of Income Tax
OSD Range 1, Ahmedabad ....Responden

IT (TP) No. 519/Ahd/2014 and 747/Ahd/15
Assessment year: 2009-10 and 2010-11

Assistant Commissioner of Income Tax
OSD Range 1, Ahmedabad ....App

Vs.

Cadila Healthcare Limited ....Responden
Zydus Tower, Opp ISKON Temple,
Satellite Cross Road, Ahmedabad 380 015
[PAN: AAACC6253G]

Appearances by:
Mukesh Patel, and Hitesh Gajaria,
along with Jigar Patel and Prashant Maheshwari for the assessee
S T Bidari for the revenue

Date of concluding the hearing: December 8th, 2016
Date of pronouncing the order: March 3rd, 2017

O R D ER

Per Pramod Kumar, AM:

1. These four appeals, consisting of two sets of cross appeals i.e. for the assessment years 2009-10 and 2010-11, pertain to the same assessee, involve some common issues and were heard together. As a matter of convenience, therefore, all the four appeals are being disposed of by way of this consolidated order.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

2. We will first take up the appeal filed by the assessee for the assessment year 2009-10.

3. In the first ground of appeal, the assessee has raised the following grievance:

> That the learned Assessing Officer erred in law and on facts in making an addition of Rs.9,54,43,732/- as upward adjustment on international transactions involving the provisions of Transfer Pricing.

4. So far as this grievance of the assessee is concerned, the relevant material facts are as follows. The assessee before us is one of the leading pharmaceutical companies in India, and it has entered into a number of international transactions with its associated enterprises abroad. As a result of the scrutiny proceedings before the Transfer Pricing Officer, arm's length price adjustments were recommended in respect of (i) interest on loans to the AEs- Rs 5,00,35,270; (ii) guarantee fee charges- Rs 4,19,22,177; and (iii) liaison services- Rs 34,86,285. The background in which these ALP adjustments were made is set out below:

(i) Interest on loans to AEs: Rs 5,00,35,270

5. It was noticed by the TPO that on 9th October 2007, the assessee had advanced an optionally convertible loan to Zydus International Pvt Ltd, Ireland, for an amount of US $ 27 million. The tenure of this loan was five years and the lender had the option for repayment or for conversion of loan into equity at par with the company at any time during the tenure of the loan. In case of repayment, the cumulative interest payable by the borrower was LIBOR plus 290 basis points. It was under this arrangement that the assessee had exercised the conversion option on 30th September 2008 and the loan was converted into equity at par. It was further noticed that the assessee had also given another somewhat similar five year optionally convertible loan to the same Irish subsidiary, for an amount of US $ 8 million, on 26th December 2008. However, so far as this loan of US $ 8 million was concerned, the assessee did not exercise the conversion option during the relevant previous year, and interest rate on this loan, in case of repayment, was LIBOR plus 550 basis points.

6. The TPO noted that the assessee did not provide for any interest on these loans. The TPO was of the view that the assessee should have charged, and provided for in the books of accounts, interest in respect of these loans. It was in this backdrop that the TPO put the assessee to notice as to why ALP adjustment in respect of interest on these loans not be made. The assessee explained that the convertible loan is at the option of the assessee at any time till the date of maturity, that it has been

used for acquisition of step down subsidiaries, that intrinsic value of the shares was much more than the conversion rate and that by not charging the interest, the assessee has kept its option of conversion intact which is beneficial to the company. None of these submissions, however, impressed the TPO. He was of the view that the mere fact that the loan has been converted into equity does not alter its character as loan as on the relevant point of time, and once that is so, the benchmarking of loan is to be done as per the prevailing market rate. It was also noted that while the Irish subsidiary, i.e. ZIPL, had received Rs 9.69 crores in the IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 relevant previous year as interest and dividend from the various entities to which the monies were given as capital or loan, which works out to exceptionally high operational income at 93%, the assessee has not been paid any interest. The TPO was also of the view that since conversion of this loan into equity has not taken place during the relevant previous year, this aspect of the matter is wholly irrelevant for levy of interest. It was also noted that "shares allotted will be of 100% subsidiary only, and as shares allotted will be of 100% subsidiary, paying low premium or high premium is not relevant as nobody else can take shares of subsidiary companies". The TPO further observed that "favourable conversion terms in 100% equity does not have any significance as it is only the assessee who can make investment in the subsidiary and use any mode of investment i.e. debt or equity". It was also noted that favourable conversion option is a misnomer since it does not carry any return to investor. It was also noted that these shares are not saleable in the open market and. As regards assessee's comparison with zero coupon convertible bonds in which entire premium is paid at the end of the term, it was noted that there is no quarrel with the proposition that the assessee can indeed issue such bonds, but once the assessee himself agrees that interest is payable on cumulative basis in the event of option of conversion not being exercised, all that is required to be done is to ascertain an arm's length interest on the said transaction. As regards the claim of the assessee that no arm's length price can be attributed when no income has arisen, it was observed that "Section 92 is not a substitute to Section 5; it is not a charging section, but it gives the TPO an authority to go behind a related party transaction which has an impact on the profits of the assessee ad if there has been a mispricing resulting into improper allocation of profits to the two parties, he has authority to change such an allocation". The TPO then observed that "on this case, ZIPL (i.e. the AE) has benefited unduly from this transaction as the balance sheet and profit and loss account of ZIPL indicates" and that 'the company has allowed significant fund to flow to the subsidiary under the garb of a convertible loan. The TPO then referred to the decision of US Supreme Court in the case of Pepsi Cola Bottling Co of Puerto Rico Inc (Docket Nos. 13676-09, 13677-09; order dated 20th September 2012) which is said to have come out with certain tests on whether the debentures are in the nature of debt or equity, he applied these tests on the facts of this case and concluded that the character of the instrument is predominantly debt rather than equity. His analysis was as follows:

7.4.6 The treatment of such instruments by the Reserve Bank of India gives an insight into their characterisation. All optionally convertible instruments are treated as loan as per the directions issued by RBI in this regard. As per the RBI Master Circular on Foreign Investment in India, the various types of instruments are defined as below:

"4. Type of instruments

> i) Indian companies can issue equity shares, fully and mandatorily convertible debentures and fully and mandatorily convertible preference shares subject to the pricing guidelines/valuation norms and reporting requirements amongst other requirements as prescribed under FEMA Regulations.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

ii) Issue of other types of preference shares such as, non- convertible, optionally convertible or partially convertible, have to be in accordance with the guidelines applicable for External Commercial Borrowings (ECBs).

iii) As far as debentures are concerned, only those which are fully and mandatorily convertible into equity, within a specified time would be reckoned as part of equity under the FDI Policy.

Further, the "Master Circular on External Commercial Borrowings & Trade Credits" states that, PART I EXTERNAL COMMERCIAL BORROWINGS (ECB) At present, Indian companies are allowed to access funds from abroad in the following methods:

> (i) External Commercial Borrowings (ECB) refer to commercial loans in the form of bank loans, buyers' credit, suppliers' credit, securitized instruments (e.g. floating rate notes and fixed rate bonds, non-convertible, optionally convertible or partially convertible preference shares) availed of from non-resident lenders with a minimum average maturity of 3 years.
>
> ii) Foreign Currency Convertible Bonds (FCCBs) mean a bond issued by an Indian company expressed in foreign currency, and the principal and interest in respect of which is payable in foreign currency.

Further, the bonds are required to be issued in accordance with the scheme viz., "Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depositary Receipt Mechanism) Scheme, 1993", and subscribed by a non-resident in foreign currency and convertible into ordinary shares of the issuing company in any manner, either in whole, or in part, on the basis of any equity related warrants attached to debt instruments. The ECB policy is applicable to FCCBs. The issue of FCCBs is also required to adhere to the provisions of Notification FEMA No. 120/RB-2004 dated July 7, 2004, as amended from time to time."

7.4.7 The above categorization clearly indicates that only fully and mandatorily convertible preference shares are to be treated at par with equity and would follow the route prescribed for 'Investments". Other categories of debentures/loans are in the nature of debts and are to be as per guidelines applicable for "External Commercial Borrowings". This categorisation gives us a tool to analyse the character of an instrument, whether inbound or outbound. In light of such clear guidelines, the averment made by the assessee that the convertible loans have passed muster of RBI are of no consequence. The assessee has produced no document to show that the loan has been accepted IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 b RBI to be in the nature of equity. Worse still, it clearly fails the test of equity in light ofthe guidelines issued by RBI. The contention of the assessee that RBI has different yardsticks for the inbound and outbound investments/loans is not borne out of the guidelines issued by it.

7.4.8 While funds advanced by the parents to their subsidiaries have to be examined for the purpose of intent in each case separately, the actual stated nature of the instrument is one of the main criteria for establishing its nature. Prima facie, an optionally convertible loan can be recalled at any time by the holder and the borrowing company is liable to pay the amount. The rules related to such remittances are less stringent as these instruments are treated as debts and not equity. On the contrary, repatriation of equity holding requires much elaborate mechanism and approvals in the resident state of the subsidiary.

7.4.9 The issue of convertible loan being hybrid instruments, in the nature of debt or equity has been debated at judicial forums in US. Acknowledging the importance of characterization of such instruments, the US Supreme Court, in their order in the case of Pepsi Cola Bottling Company of Puerto Rico Inc. Docket Nos.13676-09, 13677-09 on 20/9/2012, has come out with certain tests in order to find out whether the issue of debenture is in the nature of debt or equity. The issue of convertible loans by Cadila has been weighed on the scale specified by the US Supreme Court. It is seen that out of thirteen parameters specified by the Court, the instrument issued by Cadila falls in category of debt on ten parameters while in the remaining three parameters, no decision can be reached. However, in none of these tests, the instrument falls within the 'equity' category. In light of the predominantly 'debt' character of the instrument, it is liable to be treated as a debt and not equity.

Sr.No.	Test	Description	Assessee's Comments	TPO's comment
1	Names or labels given to the instruments	Name given to the instrument	In our case, the name of the instrument is convertible loan and is, hence, neutral	Optionally convertible l points toward
2	Presence or absence of a fixed maturity date	The presence of a fixed maturity date is virtually essential for a debt classification	The convertible loan is for a period of 5 years. Hence, the instrument takes the colour of a Loan.	Loan
3	Source of payments	A taxpayer willing to condition the repayment of an advance on the	We have the option to either convert the loan into equity at par	No relation w well being of AE before conversion. T

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

		financial well being of the receiving company acts as a capital investor and not as a creditor expecting to be repaid regardless of the company's success or failure. We understand that if the repayment is possible only out of corporate earnings, the transaction has the appearance of equity contribution but if the repayment is not dependent upon earnings, the transaction reflects a loan.	or opt for repayment. In case of repayment which can be exercised any time during the tenure of the loan not exceeding five years, we would get interest retrospectively. Thus, it can be that we have considered the financial well being of the AE. Thus the nature of instrument is in the nature of Equity s per this test.	time of conversion, in nature of loan.
4	Right to enforce payments	A definite obligation to repay an advance, including interest thereon, suggests a loan obligation. We understand that if a instrument does not provide its holder with any means to ensure payment of interest, it is strong indication of a equity contribution rather than debt.	In our case, if we exercise the option of repayment, there is a definite obligation on ZIPL to repay the loan along with interest. Thus the nature of the instrument is in the nature of a Loan as per this test.	The amount can be redeemed any time. In nature of Loan.
5	Participation in management	The right of the entity advancing funds to	This test flows in favour of Equity since we hold	The loan does not enable any participation in the

IT (TP) Nos.519 and 898/Ahd/2014
and 694 and 747/Ahd/2015
Assessment years: 2009-10 and 2010-11

	as a result of the advances	participate in the management of the receiving entity's business demonstrates that the advance may not have been bonafide debt and instead was intended as an equity investment.	100% share holding in XIPL and can participate in their management, if we choose to.	management of the company. Assessee happens to be parent so it is participating in management characterisation in nature of Loan.
6	Status of the advances in relation to regular corporate creditors	Whether an advance is subordinate to obligations to other creditors bears on whether the taxpayer advancing the funds was acting as a creditor or an investor. We understand that taking a subordinate position to other creditors may suggest an equity investment.	As stated earlier, ZIPL is an investment company which makes investments in various overseas subsidiaries in furtherance of our growth strategy. Accordingly, the convertible loan given in shareholders capacity will always be subordinated to the loans if any were taken by ZIPL from third parties. Hence, as per the said test, since the convertible loan takes a subordinate position to other creditors it flows in favour of Equity.	Character of Loan. Wrong to hold that it is given in shareholding capacity. No subordination attached to the loan. On demand, payable at par with other loans.
7	Intent of the parties	The inquiry of a court in resolving the debt equity issue is primarily	The intent of the parties is clear from the fact that with respect to the	None of the convertible loans during the present period have been

IT (TP) Nos.519 and 898/Ahd/2014
and 694 and 747/Ahd/2015
Assessment years: 2009-10 and 2010-11

		directed at ascertaining the intent of the parties. The intent of the parties, in turn, may be reflected by their subsequent acts, the manner in which the parties treat the instruments is relevant in determining their character.	convertible loan of USD 27 Mn it has been converted into equity in the year under consideration. As per this test, the instrument takes the character of Equity. With respect of the loan of USD 8 Mn the intention will manifest only in subsequent years. Hence this factor is Neutral.	converted. Hence, the intention will manifest in future. However, for the present, non-conversion reveals a loan character for the amounts.
8	Identity of interest between creditor and stockholder	If advances are made by stockholders in proportion to their respective stock ownership, an equity capital contribution is indicated. We understand that the test applies when there is a consortium of lenders.	Not Applicable to the facts of our case.	Not made in proportion to stockholders. Character of loan.
9	"thinness" of capital structure in relation to debt	The purpose of examining the debt to equity ratio in characterising an advance is to determine whether a corporation is so thinly capitalised that repayment would be unlikely. We understand that loan to a thinly capitalised	We submit that the capital of ZIPL at the time the loan of USD 27 Mn was granted was INR 119.33 crores as compared to the loan of INR 120.25 crores. Thus, this test flows towards Loan.	Loan. The AE is sufficiently capitalised.

IT (TP) Nos.519 and 898/Ahd/201
and 694 and 747/Ahd/2015
Assessment years: 2009-10 and 2010-11

		company would be indicative of equity rather than a loan.		
10	Ability of the corporation to obtain credit from outside sources	The touchstone of economic reality is whether an outside lender would have made the payments in the same form and on the same terms. We understand that if it is not possible to get the funding from an outsider lender on similar terms, the instrument would take the character of equity.	ZIPL is an investment company. We maintain that it would not have been possible to get funding from outside lenders on the terms and conditions that prevailed between us and ZIPL. A lender would neither wait to receive interest after 5 years nor would he be interested in converting the loan to Equity and bear risks of an Entrepreneur. Hence this test also suggests that the instrument was Equity.	Equity
11	Use to which advances were put	Whe re a corporation uses an advance of funds to acquire capital assets, the advance is more likely to be characterised as equity.	Since the loan has been given to fund acquisitions and/or for capital transactions, the same may be characterised as Equity.	The purpose is for working capital requirements as well as acquisitio Acquisition is the business of ZIPL. So the amount utilised towards business. Character of loan.
12	Failure to debtor to repay	The repayment of an advance may support its characterisation	As stated in the said decision, till the time of actually exercising any option, it is	Assessee would have all means to recover in case of non-payment.

IT (TP) Nos.519 and 898/
and 694 and 747/A
Assessment years: 2009-10 and

		as bona fide debt	premature to finally arrive at a conclusion whether it is in the nature of debt or equity. Thus, this test is neutral in our case.	Character o
13	Risk involved in making advances	A significant consideration in the inquiry is whether the funds were advanced with reasonable expectations of repayment regardless of the success of the venture or were placed at the risk of the business. Several factors show the uncertainty of repayment like long and conditional maturity dates.	Since the purpose of the funding was in furtherance of the inorganic growth strategic of Cadila the risk was comparatively higher and hence as per this test, the instrument takes the character of Equity.	Equity

As explained above, on 10 counts, the loan comes out as a loan and only on three counts, it can be adopted as equity. The dominant nature of the convertible loan is loan and not equity.

7. On this basis, the TPO concluded that the transaction was of debt rather than that of equity. He thus proceeded to make an ALP adjustment, by computing interest @ 7.02% in respect of the first loan, and interest @ 9.62% in respect of the second loan. The ALP adjustment was finally quantified at Rs 5,00,35,270. Aggrieved by the addition proposed by the Assessing Officer, on the basis of above findings of the TPO, assessee did raise an objection before the DRP but without any success. In a brief operative order, the DRP confirmed the action of the TPO by observing as follows:

> We have considered the facts of the case. We agree with the TPO that until actually converted, the debentures would count as loans IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 and hence interest should have been charged on the same. Further implicating fact is that on the

> same amount the borrower has earned huge income. This fact is also mentioned in the TPO's order. The TPO has referred to RBI circulars etc regarding ECBs etc. The TPO has also convincingly discussed all the issues relevant to the issue. We, therefore, reject the assessee's arguments and confirm the adjustment.

8. The Assessing Officer thus proceeded to make the impugned adjustment of Rs 5,00,35,270. The assessee is aggrieved and is in appeal before us.

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

10. There is no dispute that the transactions in question are not of the transactions of lending money to the associated enterprises. The amounts advanced to the AEs are attached with the obligation of the AEs to issue share capital, in case the assessee exercise option for the same, on certain conditions, which are admittedly more favourable, and at an agreed price, which is admittedly much lower, vis-à-vis the conditions and prices which independent enterprise would normally agree to accept. The lending is thus in the nature of quasi capital in the sense that substantive reward, or true consideration, for such a loan transaction is not interest simplictor on amount advanced but opportunity to own capital on certain favourable terms. Contrast this reward of owning the capital in the borrower entity with interest simplictor, which is typically defined as "the reward of parting with liquidity for a specified period" (Prof Keynes) or as "a payment made by the borrower of capital by virtue of its productivity as a reward for his capitalist's abstinence" (Prof Wicksell). However, in the case of transactions like the one before us, there is something much more valuable which is given as a reward to the lender and that valuable thing is the right to own capital on certain favourable terms. Therefore, the true reward, as we have noted earlier, is the opportunity and privilege to own capital of the borrower on certain favourable terms. It is for this reason that the transactions before us belong to a different genus than the act of simply giving the money to the borrower and fall in the category of 'quasi capital'.

11. As for the connotations of 'quasi capital', in the context of determination of arm's length price under transfer pricing regulations, we may refer to the observations made by a coordinate bench of this Tribunal- speaking through one of us (i.e. the Accountant Member), in the case of Soma Textile & Industries Ltd Vs ACIT [(2015) 154 ITD 745 (Ahd)], as follows:

> 5. ....The question, however, arises as to what are the connotations of expression 'quasi capital' in the context of the transfer pricing legislation.
>
> 6. Hon'ble Delhi High Court, in the case Chryscapital Investment Advisors India Ltd Vs ACIT [(2015) 56 taxmann.com 417 (Delhi)], has begun by quoting the thought provoking words of Justice Felix Frankfurter to the effect that "A phrase begins life as a literary expression; its felicity leads to its lazy IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 repetition; and repetition soon establishes it as a legal formula, undiscriminatingly used to express different and sometimes contradictory ideas". The reference so made to the words of

Justice Frankfurter was in the context of the concept of "super profits" but it is equally valid in the context of concept of "quasi capital" also. As in the case of the super profits, to quote the words of Their Lordships, "many decisions of different benches of the ITAT indicate a rote repetition (in the words of Felix Frankfurter J, quoted in the beginning of this judgment a "lazy repetition") of this reasoning, without an independent analysis of the provisions of the Act and the rules", the same seems to be the position with regard to "quasi capital". There are several decisions of this Tribunal, including in the cases of Perot Systems TSI Vs DCIT [(2010) 130 TTJ 685 (Del)]., Micro Inks Ltd Vs ACIT [(2013) 157 TTJ 289 (Ahd)], Four Soft Pvt Ltd Vs DCIT [(2014)149 ITD 732 (Hyd)], Prithvi Information Solutions Pvt Ltd Vs ACIT [(2014) 34 ITR (Tri) 429 (Hyd)] , which refer to the concept of 'quasi capital' but none of these decisions throws any light on what constitutes 'quasi capital' in the context of transfer pricing and its relevance in ascertainment of the arm's length price of a transaction. Lest we may also end up contributing to, as Hon'ble Delhi High Court put it, "rote repetition of this reasoning without an independent analysis of the provisions of the Act and the Rules", let us take briefly deal with the connotations of 'quasi capital', and its relevance, under the transfer pricing regulations.

7. The relevance of 'quasi capital', so far as ALP determination under the transfer pricing regulation is concerned, is from the point of view of comparability of a borrowing transaction between the associated enterprises.

8. It is only elementary that when it comes to comparing the borrowing transaction between the associated enterprises, under the Comparable Uncontrolled Price (i.e. CUP) method, what is to be compared is a materially similar transaction, and the adjustments are to be made for the significant variations between the actual transaction with the A E and the transaction it is being compared with. Under Rule 10B(1)(a), as a first step, the price charged or paid for property transferred or services provided in a comparable uncontrolled transaction, or a number of such transactions, is identified, and then such price is adjusted to account for differences, if any, between the international transaction and the comparable uncontrolled transactions or between the enterprises entering into such transactions, which could materially affect the price in the o pen market. Usually loan transactions are benchmarked on the basis of interest rate applicable on the loan transactions simplictor which, under the transfer pricing regulations, cannot be compared with a transaction which is something materially different than a loan simplictor, for example, a non-refundable loan which is to be converted into equity. It is in this context that the loans, which are in the nature of quasi capital, are treated differently than the normal loan transactions.

9. The expression 'quasi capital', in our humble understanding, is relevant from the point of view of highlighting that a quasi-capital loan or advance is not a routine loan transaction simplictor. The substantive reward for such a loan transaction is not interest but opportunity to own capital. As a corollary to IT (TP) Nos.519 and

898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 this position, in the cases of quasi capital loans or advances, the comparison of the quasi capital loans is not with the commercial borrowings but with the loans or advances which are given in the same or similar situations. In all the decisions of the coordinate benches, wherein references have been made to the advances being in the nature of 'quasi capital', these cases referred to the situations in which (a) advances were made as capital could not subscribed to due to regulatory issues and the advancing of loans was only for the period till the same could be converted into equity, and (b) advances were made for subscribing to the capital but the issuance of shares was delayed, even if not inordinately. Clearly, the advances in such circumstances were materially different than the loan transactions simplicitor and that is what was decisive so far as determination of the arm's length price of such transactions was concerned. The reward for time value of money in these cases was opportunity to subscribe to the capital, unlike in a normal loan transaction where reward is interest, which is measured as a percentage of the money loaned or advanced.

12. It is thus quite clear that the considerations for extending a loan simplictor are materially distinct and different from extending a loan which is given in consideration for, or mainly in consideration for, option to convert the same into capital on certain terms which are favourable vis-à-vis the terms available, or, to put it more realistically, hypothetically available, to an independent enterprise. On a conceptual note, the entire purpose of the exercise of determination of arm's length price is to neutralize the impact of intra AE relationship in a transaction, the right comparable for such a transaction of quasi capital is a similar transaction of lending money on the same terms i.e. with an option to convert the loan into capital on materially similar terms. However, what the authorities below have held, and wrongly held for that reason, is that a quasi capital transaction like one before us can be compared with a simple loan transaction where sole motivation and consideration for the lender is the interest on such loans. In the case before us, the consideration for having given the loan is, as we have noted earlier, opportunity and privilege of owning capital of the borrower on certain favourable terms. If at all the comparison of this transaction was to be done with other loan transaction, the comparison should have been done with other loans giving rise to similar privilege and opportunity to the lender. The very foundation of impugned ALP adjustment is thus devoid of legally sustainable basis.

13. Let us, at this stage, take note of the US Tax Court decision, relied upon by the TPO, in the case of Pepsi Cola Bottling Co of Puerto Rico Inc (Docket Nos. 13676-09, 13677-09; order dated 20th September 2012). It has been referred to by the TPO as decision of the US Supreme Court but in fact it is a decision of the US Tax Court, broadly at the same level of judicial hierarchy as this Tribunal. This decision deals with the limited question whether a particular transaction is required to be treated as debt or as equity. The precise question, which came up for consideration of the US Tax Court, were (1) whether advance agreements issued by PepsiCo's Netherlands subsidiaries to certain PepsiCo domestic subsidiaries and PPR are more appropriately characterized as debt than as equity; and, (2) if the advance agreements are characterized as debt, whether, and to what extent payments on the advance agreements constitute original issue discount, relating to IT (TP) Nos.519 and

898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 contingent payment debt instruments under section 1.1275-4(c), Income Tax Regulations. This provision is a deduction provision and not a provision relating to determination of arm's length price. Nothing, therefore, turns on this decision. In any event, it is nobody's case that the transaction before us is of the debt. The case of the assessee is that since in consideration of this transaction, the assessee is entitled to own the capital at certain admittedly favourable terms, the true reward of this debt is the availability of such an option, and, therefore, it cannot be compared with a debt simplictor for the purpose of determining arm's length price. Nothing, therefore, turns on this decision, and whatever be its persuasive value, or lack thereof, the authorities below were in error even in relying upon this decision

14. We have noted that, as noted by the TPO, it is wholly immaterial as to whether or not the assessee, by the virtue of this transaction, is entitled to subscribe to capital of the AE on certain concessional terms, because, in any case, the AE is a wholly owned subsidiary of the assessee and none else can subscribe to the AE's capital. What has been overlooked, however, in this process of reasoning is that the very concept of arm's length price is based on the assumption of hypothetical independence between AEs. Essentially, what is, therefore, required is visualization of a hypothetical situation in which AEs are independent of each other, and, as such, impact of intra AE association on pricing of transaction is neutralized. Once we do so, as is the compulsion of hypothesis involved in arm's length price, the fact that normally a parent company has a right to subscribe to the capital of the subsidiary at such price as suits the assessee is required to be ignored. An arm's length price is hypothetical price at which independent enterprises would have entered the transaction, and, as such, the impact of intra AE association cannot have any role to play in determination of arm's length price. The stand so taken by the TPO, which has met the approval of the DRP as well, does not, therefore, meet our approval.

15. As regards the stand of the authorities below that Irish subsidiary has shown huge profits and high operational profits @ 93%, and this fact shows that the assessee should have charged interest on commercial rates, we are unable to even understand, much less approve, this line of reasoning. It is incomprehensible as to what role profits earned from the funds raised can have in determining arm's length consideration of raising the funds, unless profit sharing is implicit in the consideration for raising the funds itself- which is neither the normal commercial practice nor the case before us. The cost of raising funds is determined much before the returns from funds so raised is even known. To hold that cost of funds raised should have been higher because the returns from funds employed by the enterprise is higher is putting cart before the horse. In the commercial world, interest does not represent any participation of profits, and it does not vary because of the profits made by the borrower from monies so raised. In any event, while determining arm's length price of a transaction, it is immaterial as to what 'benefit' an AE subsequently derives from such a transaction. What is to be determined is the consideration of a transaction in a hypothetical situation, in which AEs are independent of each other, and not the benefit that AEs derive from such transactions. It is not even the case of the authorities below that in the event of hypothetically dealing with an independent enterprise, no independent enterprise would not have given him an interest free loans even if there was an option, coupled with such a deal, to subscribe to the IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 capital of the AE on the terms as

offered by the AE to the assessee. Unless that happens, there is not even a prima facie case made out for an ALP adjustment.

16. We have also noted that, in any event, whenever the assessee's right to exercise the option of converting the loan into equity comes to an end, the assessee is entitled to interest on the commercial rates. It is not even the case of the authorities below that the interest so charged by the assessee, in a situation in which the right to exercise the option has come to an end, is not an arm's length price. Keeping in mind all these factors, as also entirety of the case, we deem it fit and proper to delete the arm's length price adjustment of Rs 5,00,35,270 in respect of interest which, according to the revenue authorities, should have charged on the optionally convertible loan granted to the AEs.

(ii) Corporate guarantee charges: Rs 4,19,22,177

17. The next arm's length price adjustment, impugned in appeal before us, with respect to guarantee charges, which, according to the revenue authorities, the assessee ought to have charged in respect of the corporate guarantees issued by the assessee for the benefit of its AEs.

18. The relevant material facts in this regard are like this. The assessee had provided certain corporate guarantees to the bankers, in respect of borrowings by its associated enterprises. During the relevant previous year, the assessee issued corporate guarantees, inter alia, to BNP Paribas in respect of Zydus Healthcare Brazil Ltd (Guarantee amount: US $ 1 million; Period: 365 days) and Quimica E Pharmaceutica Brazil (Guarantee amount: US $ 2.60 million; Period: 365 days), to Standard Chartered Bank in respect of Simayala Pharmaceuticals Pty South Africa (Guarantee amount: US $ 1 million; Period: 237 days) and Citibank in respect of Zydus Pharma Inc USA (Guarantee amount: US $ 4 million; Period: 365 days). So far as these corporate guarantees are concerned, the assessee charged guarantee commission @ 1% from the respective AEs. The assessee also issued corporate guarantees to ICICI Bank in respect of Zydus Netherlands BV (Guarantee amount:

> US $ 30 million; Period: 365 days) and to Bank of Baroda in respect of Zydus Inc USA (Guarantee amount: US $ 30 million; Period: 365 days). So far as these two guarantees were concerned, the assessee did not charge any guarantee fees at all. The assessee's explanation for not charging any guarantee commission from these AEs was that "these companies have availed loans from banks to make strategic acquisitions in furtherance of Cadila's inorganic expansion strategy". It was stated in the assessee's transfer pricing report that "issuance of guarantees to these AEs has benefitted Cadila itself rather than the AEs, and hence, keeping with the arm's length principle, no guarantee commission has been charged". These contentions of the assessee did not find favour with the TPO. He was of the view that "the current OECD guidelines as well as cases decided by the US and Canadian tax courts have also held that provision of guarantee by the guarantor is a service rendered and the guarantor is justified in charging a suitable fees for this service". The TPO was further of the view that the credit rating variation between Cadila and its AEs is between an AA

rated company (Cadila) and BB rated company (its AE) on the basis of Fitch rating. The interest rate difference between these rating of the companies, IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 according to the TPO, works out to 2.706%, and taking into account the currency risk, this amount can be enhanced to 3%. When assessee was put to notice in respect of this opinion of the TPO, it was explained by the assessee that in the preceding years, in assessee's own case, the guarantee commission @ 1%, as charged by the assessee, has been accepted by the TPO. It was then explained that the guarantees allowed to the AE for buy back of shares of Zydus Inc was to leverage upon the experience gained in US markets which in turn helped the group as a whole, rather than the company, as the funds raised on that basis were used for inorganic growth of the assessee. As regards guarantee given for Zydus Netherlands BV, it was for raising funds from ICICI Bank which were used to acquire Laboratorie Combix, Spain, enabling the assessee to enter Spanish market. It was also stated that even when we proceed on the basis that guarantee is covered by the definition of 'international transaction', it does not preclude determination of guarantee fees at nil value. In any event, interest differential between two categories of credit rating, even if that be so, cannot be attributed to the guarantee charges. The assessee further explained that the AEs have not been allowed clean loans as the borrowings were against stocks and debtors as also other collaterals, the guarantee fees of 1% is quite reasonable. None of these submissions impressed the TPO. He proceeded to reject all these submissions and proceed to adopt 3% as ALP for all the guarantees issued by the assessee. While doing so, he observed as follows:

6.5 The submission made by the assessee is considered. Following points are noted on the various issues raised by the assessee.

i. The plea of rule of consistency raised by the assessee is not found acceptable. It is seen that the issue of guarantee has not been examined by the TPO in the earlier year. Further, a TP study is an evolving art and depends on the tools available with the person conducting the study. Since the earlier TPO did not have access to data now available, he may have not gone into the issue at benchmarking of guarantee. However, that does not preclude the TPO to examine the benchmarking of guarantees in light of fresh comparable data now accessible. The concept of res judicata would not apply in a scenario of database analysis on a year to year basis.

ii. It is an acknowledged fact that there is significant benefit passed on to the AEs by giving guarantees while a significant risk is assumed on behalf of the AE. Hence, considerable service has been rendered by the assessee while giving guarantees. The acquisition is being done by the AE and not by the assessee although it may benefit as a part of the group as a whole. However, when the matter is being considered at an arm's length, such benefit has to be attributed to the AE acquiring the shares. To this extent, there is no benefit to the assessee company. Substantive funds have been raised by AEs on account of the guarantees given by the assessee company and all these guarantees mean additional risk on the assessee and a charge on the balance sheet. The liability of the guarantee will result in higher risk margin being applied in case of the loans to the assessee because of its exposure.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 iii. The assessee is correct to the extent that in specific circumstances, the value of guarantee can be taken as nil. Such a case would arise if the guarantee is given but funds are not withdrawn on the strength of this guarantee. This would mean that the services of the assessee have not been availed by the other party. But in all other cases, the guarantee would be benchmarked at reasonable amount. The assessee has elaborately discussed the benefits being given by the AEs to the assessee company. However, for this, these companies are being remunerated at arm's length rate. Providing free guarantee support cannot be a reward for providing market access. For that, a separate reward system exists. As far as guarantee is concerned, it needs to be benchmarked at suitable rate.

iv) A transaction, for the purpose of benchmarking, needs to be treated in the same way as it has been characterized in the books of the assessee. A loan is a loan and it cannot be taken as equity. Similarly, a guarantee is liable to be treated as guarantee. It cannot be treated as a share holder's investment. Similar view has been held by Hon'ble ITAT in the case of Perot Systems TSI vs. DCIT (ITAT Delhi).

v) The submission made by the assessee relating to spread of the risk over various assets is not found acceptable as no supporting data has been provided by the assessee except merely stating that some shares of ZIPL and some inventory and some receivables have also been pledged. In absence of any such data supporting the averment, no decision can be taken on this issue.

6.6 For the purpose of benchmarking, the US bond data has been taken as a representative reflection of variation in spreads with change in the rating of the bonds because these bonds are highly liquid and are freely traded and hence they reflect the most reasonable spreads and most reliable valuation. Further, they are insulated from the Indian market influence. One way of benchmarking the service rendered by the assessee company would be to find out the difference in risk spread between highly rated and medium rated corporate bonds being traded in the US markets. Since the rating agencies generally capture the expected default frequency of corporations and give ratings, a highly rated company would have a lesser chance of default and so on. By offering guarantee, the assessee company has taken over the risk of default of the guaranteed company on itself. The risk spread between the two differently rated bonds (A and BB) as mentioned above would represent the level of risk being adopted by the assessee company on behalf of its AE.

6.7 An attempt has been made to analyze the bond data in US market to arrive at various levels of yields for differently rated bonds in a global scenario since the US bond market is a mature one and is freely traded globally. The coupon rate represents yield on various bonds and the rate is directly proportional to the rating given to the bond. Higher the risk of default by the issuing company on this bond, higher the coupon rate. Details of these bonds are available on the web. The details of such corporate bonds available on IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 www.finanace.vahoo.com (publicly available) was gathered. On analysis of over 1100 bond data, from where the bonds issued during the FY 2008-09 were segregated, it is seen that the difference in coupon rate (yield or interest rate) in respect of AA rated bonds and BB rated bonds comes to 2.706%age points. By taking guarantee for payments on behalf of its AE, the assessee has incurred significant currency risk as evident by general depreciation of rupee against dollar. In order to factor this currency risk, the above spread is increased 25 basis points and hence a spread of 2.956% is found to be reasonable spread which the assessee should have charged as benefit granted to the AE.

6.8 Based on this benchmark, the service rendered by the assessee by offering guarantees to the financial institutions on behalf of its AE is liable to be benchmarked at 2.956% of the amount of guarantee given. The contention of the assessee that the guarantees given on behalf of ZIPL and Zydus Inc., USA relate to acquisition of shares of other company and to that extent, they reflect shareholder activity is not found acceptable. As already discussed above, a benefit passed to an AE as a service falls within the provisions of section 92B and hence it needs to be benchmarked. The total guarantee fee is computed as below:

Sl.	Name of the AE to whom guarantee provided	Bank	Amount guaranteed in millions of US$	No. of days	Outstanding amount in Rs. millions (On avg. dollar rate)	Arm's length guarante fee
1	Zydus Healthcare Brazil Ltd, Brazil	BNP	1	365	45.94	
2	Quimica E Pharmaceutica Brazil	BNP	2.6	365	119.444	
3	Simayala Pharmaceuticals (Pty), South Africa	SCB	1	237	45.94	
			1.5	160	68.91	
4	Zydus Pharma Inc US	Citi	4	365	183.76	

IT (TP) Nos.519 and 89
and 694 and 747
Assessment years: 2009-10 an

5	Zydus Netherlands BV (ZIPL)	ICICI	30	240	1378.2	
6	Zydus Inc. USA	BOB	30	117	1378.2	

Total Guarantee fee	51.94

On the basis of above computation, upward adjustment of Rs.5,19,40,000/- is required to be made to the income of the assessee company on account of guarantee fee to be charged from the associate enterprises. The assessee has already charged guarantee fee of Rs.1.001 million. Hence an upward adjustment of Rs.5,09,40,000/- is required to be made to the income of the assessee.

19. The quantification of the adjustment so proposed was subsequently modified, vide rectification order dated 26th March 2013, to Rs 4,19,22,177. Aggrieved by the adjustment so proposed, assessee did raise a grievance before the DRP but without complete success. While DRP did hold that the ALP of the guarantee fees should be taken @1%, the DRP did not agree that the guarantees given, as shareholder service and for arranging finance for investments in step down subsidiaries, could indeed be given without charging any fees. The relevant observations of the DRP are as follows:

> Considering the facts of the case, we direct the TPO to accept guarantee fees @1% as in earlier years. However, we are not impressed by the assessee's argument that some of the guarantees were given as shareholder's service and hence no charge will be justified. The AO has detailed the reasons as to why providing guarantee is a service that requires arm's length payment. We uphold charge of guarantee commission in respect of all the guarantees provided albeit @ 1%.

20. The Assessing Officer thus proceeded to make an ALP adjustment of Rs.4,19,22,177 in respect of guarantee commission. The assessee is aggrieved and is in appeal before us.

21. Learned representatives fairly agree that so far as this issue is concerned, it is covered, in favour of the assessee, by a coordinate bench decision in the case of Micro Ink Ltd Vs ACIT [(2016) 157 ITD 0132 (Ahd)], even as learned Departmental Representative vehemently relied upon the stand of the authorities below.

22. In the case of Micro Ink (supra), dealing with the above issue, a coordinate bench of this Tribunal has, inter alia, observed as follows:

> IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11
>
> 21. It is only elementary that the determination of arm's length price, under the scheme of the international transfer pricing set out in the Income-tax Act, 1961, can only be done in respect of an 'international transaction'. Section 92(1) provides that, "(a)ny income arising from an international transaction shall be computed having regard to the arm's length price". In order to attract the arm's length price adjustment, therefore, a transaction has to be an 'international transaction' first. The

expression 'international transaction' is a defined expression. Section 92B defines the expression 'international transaction' as follows:

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

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

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

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

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

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

(c) capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

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

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

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

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

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

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

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

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

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

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

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

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

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

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

(l) any other similar item that derives its value from its intellectual content rather than its physical attributes.' IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years:

2009-10 and 2010-11

22. As analyzed by a coordinate bench, in the case of Bharti Airtel Ltd. (supra) and speaking through one us, the legal position with respect to the above definition is as follows:

> '25. An analysis of this definition of 'international transaction' under Section 92B, as it stood at the relevant point of time, and its break-up in plain words, shows the following:
>
> An international transaction can be between two or more AEs, at least one of which should be a non-resident.
>
> An international transaction can be a transaction of the following types:
>
> in the nature of purchase, sale or lease of tangible or intangible property, in the nature of provision of services, in the nature of lending or borrowing money, or in the nature of any other transaction having a bearing on the profits, income, losses or assets of such enterprises An international transaction shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to anyone or more of such enterprises.
>
> Section 92B (2), covering a deeming fiction, provides that even a transaction with non-AE in a situation in which such a transaction is de facto controlled by prior agreement with AE or by the terms agreed with the AE.
>
> 26. Let us now deal with the Explanation, inserted with retrospective effect from 1st April 2002 i.e. right from the time of the inception of transfer pricing legislation in India, which was brought on the statute vide Finance Act, 2012.
>
> 27. This Explanation states that it is merely clarificatory in nature inasmuch as it is 'for the removal of doubts', and, therefore, one has to proceed on the basis that it does not alter the basic character of definition of 'international transaction' under Section 92B. Clearly, therefore, this Explanation is to be read in conjunction with the main provisions, and in harmony with the scheme of the provisions, under Section 92B. Under this Explanation, five categories of transactions have been clarified to have been included in the definition of 'international transactions'.
>
> 28. The first two categories of transactions, which are stated to be included in the scope of expression 'international transactions' by the virtue of clause (a) and (b) of Explanation to Section 92B, are transactions with regard to purchase, sale, transfer, lease or use of tangible and intangible properties.

These transactions were anyway covered by 2 (a) above which covered transactions 'in the nature of purchase, sale or lease of tangible or intangible property'. The only additional expression in the clarification is 'use' as also illustrative and inclusive descriptions of tangible and intangible assets.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 Similarly, clause (d) deals with the " provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service" which are anyway covered by 2(b) and 3 above in "provision for services" and "mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to anyone or more of such enterprises". That leaves us with two clauses in the Explanation to Section 92B which are not covered by any of the three categories discussed above or by other specific segments covered by Section 92B, namely borrowing or lending money.

29. The remaining two items in the Explanation to Section 92B are set out in clauses (c) and (e) thereto, dealing with (a) capital financing and (b) business restructuring or reorganization. These items can only be covered in the residual clause of definition in international transactions, as in Section 92B(1), which covers "any other transaction having a bearing on profits, incomes, losses, or assets of such enterprises".

30. It is, therefore, essential that in order to be covered by clauses (c) and (e) of Explanation to Section 92B, the transactions should be such as to have bearing on profits, incomes, losses or assets of such enterprise. In other words, in a situation in which a transaction has no bearing on profits, incomes, losses or assets of such enterprise, the transaction will be outside the ambit of expression 'international transaction'. This aspect of the matter is further highlighted in clause (e) of the Explanation dealing with restructuring and reorganization, wherein it is acknowledged that such an impact could be immediate or in future as evident from the words "irrespective of the fact that it (i.e. restructuring or reorganization) has bearing on the profit, income, losses or assets of such enterprise at the time of transaction or on a future date". What is implicit in this statutory provision is that while impact on " profit, income, losses or assets" is sine qua non, the mere fact that impact is not immediate, but on a future date, would not take the transaction outside the ambit of 'international transaction'. It is also important to bear in mind that, as it appears on a plain reading of the provision, this exclusion clause is not for "contingent" impact on profit, income, losses or assets but on "future" impact on profit, income, losses or assets of the enterprise. The important distinction between these two categories is that while latter is a certainty, and only its crystallization may take place on a future date, there is no such certainty in the former case. In the case before us, it is an undisputed position that corporate guarantees issued by the assessee to the Deutsche Bank did not even have any such implication because no borrowings were resorted to by the subsidiary from this bank.

31. In this light now, let us revert to the provisions of clause (c) of Explanation to Section 92B which provides that the expression 'international transaction' shall include "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". In view of the discussions above, the scope of these transactions, as could be covered under Explanation to Section 92B read with Section 92B(1), is restricted to such IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 capital financing transactions, including inter alia any guarantee, deferred payment or receivable or any other debt during the course of business, as will have "a bearing on the profits, income, losses or assets or such enterprise". This precondition about impact on profits, income, losses or assets of such enterprises is a precondition embedded in Section 92B(1) and the only relaxation from this condition precedent is set out in clause (e) of the Explanation which provides that the bearing on profits, income, losses or assets could be immediate or on a future date. The contents of the Explanation fortifies, rather than mitigates, the significance of expression 'having a bearing on profits, income, losses or assets' appearing in Section 92B(1).

32. There can be number of situations in which an item may fall within the description set out in clause (c) of Explanation to Section 92B, and yet it may not constitute an international transaction as the condition precedent with regard to the 'bearing on profit, income, losses or assets' set out in Section 92B(1) may not be fulfilled. For example, an enterprise may extend guarantees for performance of financial obligations by its associated enterprises. These guarantees do not cost anything to the enterprise issuing the guarantees and yet they provide certain comfort levels to the parties doing dealings with the associated enterprise. These guarantees thus do not have any impact on income, profits, losses or assets of the assessee. There can be a hypothetical situation in which a guarantee default takes place and, therefore, the enterprise may have to pay the guarantee amounts but such a situation, even if that be so, is only a hypothetical situation, which are, as discussed above, excluded. One may also have a situation in which there is a receivable or any other debt during the course of business and yet these receivables may not have any bearing on its profits, income, losses or assets, for example, when these receivables are out of cost free funds and these debit balances do not cost anything to the person allowing such use of funds. The situations can be endless, but the common thread is that when an assessee extends an assistance to the associated enterprise, which does not cost anything to the assessee and particularly for which the assessee could not have realized money by giving it to someone else during the course of its normal business, such an assistance or accommodation does not have any bearing on its profits, income, losses or assets, and, therefore, it is outside the ambit of international transaction under section 92B (1) of the Act.

33. In any event, the onus is on the revenue authorities to demonstrate that the transaction is of such a nature as to have "bearing on profits, income, losses or assets" of the enterprise, and there was not even an effort to discharge this onus. Such an impact on profits, income, losses or assets has to be on real basis, even if in present or in future, and not on contingent or hypothetical basis, and there has to be some material on record to indicate, even if not to establish it to hilt, that an intra AE international transaction has some impact on profits, income, losses or assets. Clearly, these conditions are not satisfied on the facts of this case.'

23. Learned Departmental Representative submits that this decision is no longer good law in the light of Everest Kanto Cylinders Ltd. decision (supra) and Vodafone India Services (P.) Ltd. decision (supra) by Hon'ble Bombay High Court.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

24. As for Hon'ble High Court's judgment in the case of Everest Kanto Cylinders Ltd. (supra), it is necessary to appreciate the fact the assessee was charging a .5% commission on issuance of corporate guarantees, on behalf of the AEs, and it could not, therefore, be said that the transaction will have no impact on "profits, incomes, losses or assets of such enterprise". This aspect of the matter is clear from an observations in the related Tribunal order, which is reported as Everest Kanto Cylinders Ltd (supra), to the effect that "However, in this case, the assessee has itself charged 0.5% guarantee commission from its AE and, therefore, it is not a case of not charging any kind of commission from its AE". The Tribunal did note, in the immediately following sentence in paragraph 23 itself, that "the only point to be seen in this case is whether the same is at ALP or not". The very fact of charging this guarantee commission brings the issuance of corporate guarantees to the net of transfer pricing. Nevertheless, the ALP adjustment made by the TPO was deleted by the Tribunal. Aggrieved by the relief so given by the Tribunal, the matter was carried in further appeal, by the Commissioner, before the Hon'ble Bombay High Court which eventually upheld the relief granted by the Tribunal. The appeal before the Hon'ble High Court was by the Commissioner, and not by the assessee, and, therefore, the grievance against the issuance of corporate guarantee being held to be an international transaction could not have come up for consideration. Of course, the assessee had no occasion to challenge the stand of the Tribunal on this aspect since the addition, on merits, was deleted anyway making revenue's success in this respect hollow and of no damage to the interests of the assessee. It was in this backdrop that the action of the Tribunal was upheld in granting relief to the assessee on merits. It is difficult to understand as to how this decision is taken as supporting the proposition that the issuance of corporate guarantee, even in a case in which neither any guarantee commission is charged nor any costs are incurred, is an international transaction. In any case, there is nothing in the operative portion which even remotely suggests that Their Lordships had any occasion to address themselves to the question as to whether the issuance of corporate guarantee amounts to international transaction. The operative portion of the judgment is reproduced below for ready reference:

> "............In the matter of guarantee commission, the adjustment made by the TPO were based on instances restricted to the commercial banks providing guarantees and did not contemplate the issue of a Corporate Guarantee. No doubt these are contracts of guarantee, however, when they are Commercial banks that issue bank guarantees which are treated as the blood of commerce being easily encashable in the event of default, and if the bank guarantee had to be obtained from Commercial Banks, the higher commission could have been justified. In the present case, it is assessee company that is issuing Corporate Guarantee to the effect that if the subsidiary AE does not repay loan availed of it from ICICI, then in such event, the assessee would make good the amount and repay the loan. The considerations which applied for

> issuance of a Corporate guarantee are distinct and separate from that of bank guarantee and accordingly we are of the view that commission charged cannot be called in question, in the manner TPO has done. In our view the comparison is not as between like transactions but the comparisons are between guarantees issued by the commercial banks as against a Corporate Guarantee issued by holding company for the benefit of its AE, a subsidiary company. In view of the above discussion we are of the view that the appeal does not raise any substantial question of law and it is dismissed."

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

25. We are unable to see, in the judgment of Hon'ble Bombay High Court, any support to the proposition that issuance of corporate guarantees is inherently within the ambit of definition of 'international transaction' under section 92B irrespective of whether or not such transactions have any "bearing on profits, incomes, losses, or assets of such enterprises". Revenue, therefore, does not derive any help from the said decision.

26. Coming to Hon'ble Bombay High Court in the case of Vodafone India Services (P.) Ltd. (supra), which has been relied upon by the learned Departmental Representative, we find that the operative portion of this judgment, so far as relevant to this discussion, is as follows:

> '213. The amendment to section 2(47) raises several important questions of fact and of law. Whether or not it affects the proceedings which were the subject matter before the Supreme Court is not relevant for the purpose of this Writ Petition. But, whether it is relevant or not for the purpose of the assessment proceedings in respect of the petitioner which are the subject matter of this Writ Petition, is relevant. The effect of the amendment would have to be considered. It cannot be brushed aside.
>
> 214. Section 2(47), as amended, even on a cursory glance raises various issues. It is necessary to note four preliminary aspects of Explanation 2 to section 2(47). Firstly, as the opening words, For the removal of doubts it is hereby clarified that ......", indicate it is a clarificatory amendment. Secondly, it is an inclusive definition as is evident from the words "transfer" includes ".

Thirdly, the amendment is with retrospective effect from 1st April, 1962. Fourthly, the Finance Act 2012 which introduced, inter alia, the amendment to section 2(47) and section 92CA(2B) is a validating act in view of section 119 thereof.

215. Explanation 2 to section 247 broadly has four elements. Disposal or parting with or creating any interest in an asset. The asset or any interest in the asset.

The disposing of or parting with the asset or creating any interest therein may be:

```
(a)          Direct or indirect.
```

```
(b)           Absolute or conditional.
(c)           Voluntary or involuntary.
(d)           By amendment or otherwise.
```

(iv) A non-obstante provision regarding the nature of a transfer. If an act, arrangement, transaction etc. constitutes a transfer as defined in the section it would be so notwithstanding the transfer of rights having been categorised as being effected or dependent upon or flowing from the transfer of a share or shares of a company registered or incorporated outside India.

216. Two aspects of a transfer are clarified - the asset itself and the manner in which it is dealt with. The asset is no longer restricted to the asset per se or a right therein, but also extends to "any interest therein". Prior to the amendment, the words "any interest therein" were absent. Further, the nature of the disposal is also expanded. It now includes the creation of any interest in any asset. Moreover, the disposal of or creation of any interest in the asset IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 may be direct or indirect, absolute or conditional, voluntary or involuntary. It may be by way of an agreement or otherwise. Further, the concluding words constitute a non-obstante provision. It provides that the transfer contemplated therein would be notwithstanding that it has been characterised as being effected or dependent upon or flowing from the transfer of a share or shares of a company registered or incorporated outside India.

It would be evident, therefore, that a lot more must now be seen and considered than before while arriving at a conclusion whether the terms and conditions of the Framework agreement constituted a transfer or assignment of the call options by one party to another.

217. At the cost of repetition, we are not concerned here with whether the amendment is valid or not. One of the issues, however, that does arise is whether the amendment, albeit clarificatory, would make a difference in the construction of the provisions of the Framework agreements themselves, to wit as regards the construction of the clauses thereof without the aid of any other material for interpreting them. Vodafone's case obviously considered the ambit of the term "transfer" prior to the amendment. In the present assessment proceedings, it is the amended definition which would have to be considered.

218. We do not find it either necessary or proper to indicate the application of section 2(47) as amended to the present proceedings. The application would depend upon the facts on record or those may be permitted to be brought on record.

219. There is another aspect. The petitioner may well contend that the amended definition makes no difference it being clarificatory in nature. The provisions thereof must, therefore, be deemed always to have been in existence. We will presume that it would be open to the petitioner to contend, therefore, that the judgment of the Supreme Court would remain entirely unaffected for the Supreme Court must be deemed to have considered the term as per its true ambit, as always intended by the Parliament. On the other hand, it may be equally open to the Revenue to contend that certain ingredients of a transfer were not considered by the Revenue itself in the proceedings

relating to Vodafone's case on account of the Revenue itself not having appreciated or realized the actual ambit of the term "transfer" which are now clarified by the amendment. Even assuming that the Revenue cannot re-open the Vodafone case, it cannot be barred from relying upon the true ambit of the term "transfer" in future cases, including the proceedings in respect of the petitioner. Thus, even assuming that the judgment of the Supreme Court remains unaffected by the clarificatory amendment, the Revenue would be entitled hereafter in other cases, at least, to appreciate, analyze and construe the transactions relating to call options, including the Framework agreements in a proper perspective which it may not have done earlier.

220. These are important issues. There is no justification for withdrawing the proceedings from the channel provided by the Income-tax Act, bypassing the Tribunal and considering all these questions in exercise of the High Court's extraordinary jurisdiction under Article 226.' (Emphasis supplied) IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

27. Revenue's emphasis is on the last two sentences in paragraph No 213 which state that "The effect of the amendment would have to be considered. It cannot be brushed aside" but in doing so what it overlooks is the subsequent observations highlighted above which recognize the fact that merely because a subsequent Explanation is introduced by the legislature, it is not an open and shut case against the assessee or the revenue, and that all these observations are in the context that "there is no justification for withdrawing the proceedings from the channel provided by the Income-tax Act, bypassing the Tribunal and considering all these questions in exercise of the High Court's extraordinary jurisdiction under Article 226". When Their Lordships have made it clear that they would not like to bypass the channels under the Income-tax Act and proceed to decide these issues in writ jurisdiction under article 226, there cannot obviously be any question of Their Lordships deciding the matter one way or the other. Any observations made by Their Lordships, while declining to decide the matter in writ jurisdiction, cannot be treated as decisive of the issue on merits. While it is true that Hon'ble Bombay High Court has observed that the effect of amendment will have to be considered, Hon'ble Bombay High Court has also observed that even after taking into account the amendments, the legal implications of this amendment is still an open issue which will have to be adjudicated in the light of pleadings of the parties. Even in these observations, which do not anyway decide anything on merits, effect of a retrospective amendment was not in the context of the precise issue before us, or on the scope of the international transaction, but in respect of connotations of 'transfer'. As learned counsel rightly contends, in the light of Hon'ble Bombay High Court's judgment in the case of Sudhir Jayantilal Mulji (supra) "ratio of a decision alone is binding, because a case is only an authority for what it actually decides and not what may come to follow from some observations which find place therein". In view of these discussions, the reliance placed on Vodafone India Services (P.) Ltd. (supra) is also equally misplaced and devoid of legally sustainable merits. In any case, as is noted by Hon'ble Supreme Court in the case of CIT v. Sun Engg. Works (P.) Ltd. [1992] 198 ITR 297/64 Taxman 442 (SC), "It is neither desirable nor permissible to pick out a word or a sentence from the judgment of this Court, divorced from the context of the question under consideration and treat it to be the complete "law" declared by this Court. The judgment must be read as a whole and the observations from the judgment have to be considered in the light of the questions which were before this Court" Their Lordships further noted

that "A decision of this Court takes its colour from the questions involved in the case in which it is rendered and, while applying the decision to a later case, the Courts must carefully try to ascertain the true principle laid down by the decision of this Court and not to pick out words or sentences from the judgment, divorced from the context of the questions under consideration by this Court, to support their reasoning" It was also recalled that in Madhav Rao Jivaji Rao Scindia Bahadur v. Union of India AIR 1971 SC 530, Hon'ble Supreme Court had cautioned that "It is not proper to regard a word, clause or a sentence occurring in a judgment of the Supreme Court, divorced from its context, as containing a full exposition of the law on a question when the question did not even fall to be answered in that judgment." That precisely, however, has been the approach of the revenue authorities in placing reliance on Vodafone India Services (P.) Ltd. (supra) decision. We reject this approach.

28. For the reasons set out above, learned Departmental Representative's reliance on Hon'ble Bombay High Court's judgments in the cases of Everest Kanto (supra) and Vodafone India Services (supra) is wholly misplaced and devoid of any merits. As for coordinate bench decision in the case of Hindalco Industries (supra), all it does is to follow the Everest Kanto decision by Hon'ble Bombay High Court, but then, as IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 we have seen earlier, that was a case in which Their Lordships were in seisin of a situation in which guarantee commission was actually charged by the assessee. That is not the case before us. The coordinate bench decisions dealing with the situations in which the guarantee commission was actually charged, and as such there was indeed a bearing on the profits of the assessee, clearly do not apply on this case. We, therefore, reject the reliance on these decisions as devoid of legally sustainable merits.

29. Let us now deal with the reliance placed by the revenue authorities on GE Capital's case by the Tax Court of Canada. In the DRP's order, a reference is made to well known Canadian decision in the case of GE Capital Canada (supra). The said case, to quote the words of the DRP, "also shows that the group company issuing the guarantee (i.e. guarantor) would, in principle, at least need to cover the cost that it incurs with respect to providing the guarantee" and that "these costs may include administrative expenses as well as the costs of maintaining an appropriate level of cash equivalents, capital, subsidiary credit lines or more expensive external funding conditions on other debt finance". The DRP had also noted that "in addition, the guarantor would want to receive appropriate compensation for the risk it incurs" and concluded that "following the above discussions, an arm's length guarantee fees is typically required to be determined by establishing a range of fees that the guarantor would, at least, want to receive and the fees that the guaranteed group company would be willing to pay depending on the prevailing conditions within financial markets in practice".

30. However, while dealing with this aspect of the matter, it is necessary to bear in mind the fact that this judicial precedent, whatever be its worth in the hierarchy of binding judicial precedents in India, does not even deal with the fundamental question as to whether issuance of a corporate guarantee is an international transaction at all- which is what we are concerned with at present. This TCC decision dealt with a situation in which the assessee was denied, in computation of its business income, tax deduction for payment of guarantee fees on the ground that there was no effective

benefit to the assessee, in obtaining the said guarantee. Aggrieved by denial of deduction, assessee carried the matter in appeal before the Canadian Tax Court, and the plea of the assessee was eventually upheld. It is also interesting to note that as a sequel to this Tax Court of Canada decision, the transfer pricing legislation was amended, to bring greater clarity on the issue and as a measure of abundant caution, and section 247 (7.1), granting specific exemption to guarantee fees, was introduced. This amendment is as follows:

> (7.1) Sub-section (2) does not apply to adjust an amount of consideration paid, payable or accruing to a corporation resident in Canada (in this sub- section referred to as the "parent") in a taxation year of the parent for the provision of a guarantee to a person or partnership (in this sub-section referred to as the "lender") for the repayment, in whole or in part, of a particular amount owing to the lender by a non-resident person, if (a) the non- resident person is a controlled foreign affiliate of the parent for the purposes of section 17 throughout the period in the year during which the particular amount is owing; and (b) it is established that the particular amount would be an amount owing described in paragraph 17(8)(a) or (b) if it were owed to the parent.
>
> (http://www.fin.gc.ca/drleg-apl/ita-lrir-dec12-l-eng.pdf) IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

31. It is also important to bear in mind the fact that, under the Canadian law, the definition of 'international transaction', unlike an exhaustive definition under section 92B of the Indian Income-tax Act, 1961, is a very brief but inclusive and broad definition to the effect that "'transaction' includes a series of transactions, an arrangement or an event" [See Section 247(1) of the Canadian Income-tax Act, 1985; http://laws-lois.justice.gc.ca/eng/acts/I-3.3/page-419.html#h-156] coupled with the legal position that arm's length adjustment to the prices of such transaction come into play "Where a taxpayer or a partnership and a non-resident person with whom the taxpayer or the partnership, or a member of the partnership, does not deal at arm's length" [See Section 247(2) ibid]. When one takes into account these variations in the statutory provisions, it will become very obvious that the provisions of the Indian Income-tax Act, 1961 and the Canadian Income-tax Act, 1985 are so radically different that just because a particular transaction is to be examined on arm's length principle in Canada cannot be a reason enough to hold that it must meet the same in India as well. While the Canadian transfer pricing legislation, as indeed the transfer pricing legislation in many other jurisdictions, does not put any fetters on the nature of transactions between the AEs, so as to be covered by the arm's length price adjustment, and, therefore, covers all transactions between the related enterprises, Indian transfer pricing legislation covers only such transactions as are "in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises". Our transfer pricing provisions, perhaps being in the quest of comprehensive coverage, have ended up in a limited scope of the transactions being covered by the arm's length price adjustments for transfer pricing. In any event, as emphasized earlier as well, the decision was in the context of the deduction, and, post this decision, a specific amendment was introduced in the

Canadian transfer pricing law to clarify the position that all corporate guarantees issued by the assessee, in support of its subsidiaries, are not necessarily international transactions. Revenue, therefore, does not derive any advantage from the Tax Court of Canada's decision in the case of GE Capital Canada. There are many more aspects which make this decision wholly irrelevant in the present context but suffice to say that relevant legal provisions and context being radically different, the reliance of this decision must be rejected for this short reason alone.

32. As we take note of the above legal position in Canada, it is appropriate to take note of the concept of 'shareholder activities' in the context of corporate guarantees which provides conceptual justification for exclusion of corporate guarantees, under certain conditions, from the scope of transfer pricing adjustments. Taking note of these proposed amendments, 'Transfer Pricing and Intra Group Financing - by Bakker & Levvy, IBFD publication (ISBN- 978-90-8722-153-9)' observes that "Proposed sub-section 247(7.1) of the ITA provides that the transfer pricing rules will not apply to guarantees provided by Canadian parent corporations in respect of certain financial commitments of their Canadian controlled foreign affiliates to support the active business operations of those affiliates". As to what could be conceptual support for such an exclusion, we find interesting references in a discussion paper issued by the Australian Tax Officer in June 2008 and titled as "Intra-group finance guarantees and loans"

> (http://www.transferpricing.com/pdf/Australia_Thin%20Capitalisation.pdf). The fact that this discussion paper did not travel beyond the stage of the discussion paper is not really relevant for the present purposes because all that we are concerned with right now is understanding the conceptual basis on which, contrary to popular but apparently erroneous belief, the issuance of corporate guarantees can indeed be IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 kept outside the ambit of services. The relevant extracts from this document are as follows:
>
> "102. An independent company that is unable to borrow the funds it needs on a stand-alone basis is unlikely to be in a position to obtain a guarantee from an independent party to support the borrowings it needs. Where such a guarantee is given it compensates for the inadequacies in the financial position of the borrower; specifically, the fact that the subsidiary does not have enough shareholders' funds. .....
>
> 103. It would not be expected that a company pay for the acquisition of the equity it needs for its formation and continued viability. Equity is generally supplied by the shareholders at their own cost and risk.
>
> 104. Accordingly to the extent that a guarantee substitutes for the investment of the equity needed to allow a subsidiary to be self-sufficient and raise the debt funding it needs, the costs of the guarantee (and the associated risk) should remain with the parent company providing the guarantee."

33. On a conceptual note, thus, there is a valid school of thought that the corporate guarantees can indeed be a mode of ownership contribution, particularly when, as is often the case, "where such a guarantee is given it compensates for the inadequacies in the financial position of the borrower; specifically, the fact that the subsidiary does not have enough shareholders' funds". There can be number of reasons, including regulatory issues and market conditions in the related jurisdictions, in which such a contribution, by way of a guarantee, would justify to be a more appropriate and preferred mode of contribution vis-a-vis equity contribution. It is significant, in this context, that the case of the assessee has all along been, as noted in the assessment order itself, that "said guarantees were in the form of corporate guarantees/ quasi-capital and not in the nature of any services". In other words, these guarantees were specifically stated to be in the nature of shareholder activities. The assessee's claim of the guarantees being in the nature of quasi- capital, and thus being in the nature of a shareholder's activity, is not rejected either. The concept of issuance of corporate guarantees as a shareholder activity is not alien to the transfer pricing literature in general. On the contrary, it is recognized in international transfer pricing literature as also in the official documentation and legislation of several transfer pricing jurisdictions. The 'OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations' itself recognizes the distinction between a shareholder activity and a provision for services, when, contrasting the shareholder activity with broader term "stewardship activity" and thus highlighting narrow scope of shareholder activity, it states that "Stewardship activities covered a range of activities by a shareholder that may include provision for services to other group members, for example services that would be provided by a coordinating centre". It proceeded to add, in the immediately following sentence at page 207 of 2010 Guidelines, that "These latter type of non-shareholder activities could include detailed planning services for particular operations, management or technical advice (trouble shooting) or in some cases assistance in day-to-day management". The shareholder activities are thus seen as conceptually distinct from the provision of services. The issuance of corporate guarantee, as long as it is in the nature of shareholder activity, cannot, therefore, amount to a "provision for services".

34. Undoubtedly, pioneering work done by the OECD, in the field of international taxation, has been judicially recognized worldwide by various judicial forums, IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 including, most notably by Hon'ble Andhra Pradesh High Court in the case of CIT v. Visakhapatnam Port Trust [1983] 144 ITR 146/15 Taxman 72 (AP). Their Lordships also referred to Lord Radcliffe's observations in Ostime v. Australian Mutual Provident Society [1960] 39 ITR 210 (HL), which has described the language employed in the models developed by the OECD as the "international tax language". The work done by OECD in the field of transfer pricing is no less significant. No matter which part of the world we live in, and irrespective of whether or not that tax jurisdiction is an OECD member jurisdiction, the immense contribution of the OECD, in the field of the transfer pricing as well, is admired and respected. However, the relevance of this work, so far as interpretation to transfer pricing legislation is concerned, must remain confined to the areas which have remained intact from legislative or judicial guidance. There is no scope for parallel or conflicting guidance by such forums. Legislation is an exclusive domain of the sovereign, and, therefore, as long as an area is adequately covered by the work of legislation, things like guidance of the OECD, or for that purpose any other multilateral forum, are not decisive. While we are alive to the school of thought that when the domestic transfer pricing regulations do not provide any guidelines, it may have to be decided having regard to

international best practices, we do not quite agree with it inasmuch as, in our considered view, Revenue cannot seek to widen the net of transfer pricing legislation by taking refuge of the best practices recognized by the OECD work.

35. While dealing with "special consideration for intra-group services", the 'OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations' has noted that there are two fundamental issues with respect to the intra-group services- first, whether intra-group services have indeed been provided, and, second- if the answer to the first question is in positive, that charge to these services should be at an arm's length price. Dealing with the first question, which is relevant for the present purposes, these Guidelines (2010 version) state as follows:

> '7.6 Under the arm's length principle, the question whether an intra-group service has been rendered when an activity is performed for one or more group members by another group member should depend on whether the activity provides a respective group member with economic or commercial value to enhance its commercial position. This can be determined by considering whether an independent enterprise in comparable circumstances would have been willing to pay for the activity if performed for it by an independent enterprise or would have performed the activity in-house for itself. If the activity is not one for which the independent enterprise would have been willing to pay or perform for itself, the activity ordinarily should not be considered as an intra-group service under the arm's length principle.
>
> 7.7 The analysis described above quite clearly depends on the actual facts and circumstances, and it is not possible in the abstract to set forth categorically the activities that do or do not constitute the rendering of intra-

group services. However, some guidance may be given to elucidate how the analysis would be applied for some common types of activities undertaken in MNE groups.

7.8 Some intra-group services are performed by one member of an MNE group to meet an identified need of one or more specific members of the group. In such a case, it is relatively straightforward to determine whether a service has been provided. Ordinarily an independent enterprise in comparable circumstances would have satisfied the identified need either by IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 performing the activity in-house or by having the activity performed by a third party. Thus, in such a case, an intra-group service ordinarily would be found to exist. For example, an intra-group service would normally be found where an associated enterprise repairs equipment used in manufacturing by another member of the MNE group.

7.9 A more complex analysis is necessary where an associated enterprise undertakes activities that relate to more than one member of the group or to the group as a whole. In a narrow range of such cases, an intra-group activity may be performed relating to group members even though those group members do not need the activity (and would not be willing to pay for it were they independent enterprises). Such an activity would be one that a group member (usually the parent company or a regional holding company) performs solely because of its ownership interest in one or more other group members, i.e. in its capacity as shareholder. This type of activity would not justify a charge to the recipient companies. It may be referred to as a "shareholder activity", distinguishable from the broader term "stewardship activity" used in the 1979 Report. Stewardship activities covered a range of activities by a shareholder that may include the provision of services to other group members, for example services that would be provided by a coordinating centre. These latter types of non-shareholder activities could include detailed planning services for particular operations, emergency management or technical advice (trouble shooting), or in some cases assistance in day-to-day management.

7.10 The following examples (which were described in the 1984 Report) will constitute shareholder activities, under the standard set forth in paragraph 7.6:

> (a) Costs of activities relating to the juridical structure of the parent company itself, such as meetings of shareholders of the parent, issuing of shares in the parent company and costs of the supervisory board;
>
> (b) Costs relating to reporting requirements of the parent company including the consolidation of reports;
>
> (c) Costs of raising funds for the acquisition of its participations.

In contrast, if for example a parent company raises funds on behalf of another group member which uses them to acquire a new company, the parent company would generally be regarded as providing a service to the group member. The 1984 Report also mentioned "costs of managerial and control (monitoring) activities related to the management and protection of the investment as such in participations". Whether these activities fall within the definition of shareholder activities as defined in these Guidelines would be determined according to whether under comparable facts and circumstances the activity is one that an independent enterprise would have been willing to pay for or to perform for itself.' (Emphasis supplied)

36. We have noticed that the 'OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations' specifically recognizes that an activity in the nature of shareholder activity, which is solely because of ownership interest in one or IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 more of the group members, i.e. in the capacity as shareholder "would not justify a charge to the recipient companies". It is thus clear that a shareholder activity, in issuance of corporate guarantees, is taken out of ambit of the group services. Clearly, therefore, as long as a guarantee is on account of, what can be termed as 'shareholder's activities', even on the first principles, it is outside the ambit of transfer pricing adjustment in respect of arm's length price. It is essential to appreciate, at this stage, the distinction in a service and a benefit. One may be benefited even when no services are rendered, and, therefore, in many a situation it's a 'benefit test' which is crucial for transfer pricing legislation, such as in US Regulations 1.482-9(1)(3)(i) which defines 'benefit', form a US Transfer Pricing perspective, as "an activity is considered to be provided a benefit to the recipient if the activity directly results in a reasonably

identifiable increment of economic or commercial value that enhances the recipient's commercial position, or that may be reasonably anticipated to do so". The expression "activity", in turn is defined, as "including the performance of functions; the assumption of risks; the use by a rendered of tangible or intangible property or other resources capabilities or knowledge (including knowledge of and ability to take advantage of a particularly advantageous situation or circumstances); and making available to the recipient any property or other resources of the rendered"

> [Regulation 1.482-9(1)(2)]. The issuance of guarantees is not within the ambit of transfer pricing in United States because it is a service but because it is covered by the specific definition discussed above. As a matter of fact, David S Miller, in a paper titled 'Federal Income Tax Consequences of Guarantees; A Comprehensive Framework for Analysis' published in the 'The American Lawyer Vol. 48, No. 1 (Fall 1994), pp. 103-165 (http://www.jstor.org/stable/20771688), has stated that a guarantee is not a service. The following observations, at pages 114, are important:
>
> The position that guarantees are services has been discredited by the courts with good reason38. Guarantee fees do not represent payments for services any more than payments with respect to other financial instruments constitute payment for services39. A guarantor does not arrange financing for the debtor, but merely executes a financial instrument in its favour.
>
> 38See. e.g., Centel Communications Co. v. Commissioner, 92 T.C. 612, 632 (1989), aff d, 920 F2d 1335 (7th Cir. 1990); Bank of Am. v. United States, 680 F.2d 142, 150 (Cl. Ct. 1982). The Service's current position on the characterization of guarantee fees as payment for services under section 482 is inconsistent with its treatment of guarantee fees under other provisions.

See P.L.R. 9410008 (Dec. 13, 1993).

39But cf Federal Nat'l Mortgage Ass'n v. Commissioner, 100 T.C. 541, 579 (1993) (Fannie Mae provided services by buying mortgages).

37. We are in agreement with these views. There can thus be activities which benefit the group entities but these activities need not necessarily be 'provision for services'. The fact that the OECD considers such activities in the services segment does not alter the character of the activities. While the group entity is thus indeed benefited by the shareholder activities, these activities do not necessarily constitute services. There is no such express reference to the benefit test, or to the concept of benefit attached to the activity, in relevant definition clause of 'international transaction' under the domestic transfer pricing legislation. As we take note of these things, it is also essential to take note of the legal position, in India, in this regard. No matter how desirable is it to read such a test in the definition of the international transaction' under our domestic transfer pricing legislation, as is the settled legal position, it is not open to us to infer the same. Hon'ble Supreme Court, in the case of Smt. Tarulata IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 Shyam v. CIT [1977] 108 ITR 345 (SC) , took note of the situation before

Their Lordships in these words: "We have given anxious thoughts to the persuasive arguments of Mr Sharma. His arguments, if accepted, will certainly soften the rigour of this extremely drastic provision and bring it more in conformity with logic and equity". However, Their Lordships declined to do so on the ground that "There is no scope for importing into the statute the words which are not there. Such importation would be not to construe but to amend the statute". Their Lordships noted that "Even if there be casus omissus, the defect can be remedied only by legislation and not by judicial interpretation". The benefit test, which is set out in the OECD Guidance and which finds its place in the international best practices, does not find its place in the main definition of international transaction, even though there is a reference to the expression 'benefit' in the context of cost or expense sharing arrangements but that is a different aspect of the matter altogether. In the absence of benefit test being mentioned in the definition for the present purposes, we cannot infer the same.

38. One more thing which is clearly discernable from the above discussions is that the tests recognized by these guidelines are interwoven twin tests of benefit and arm's length. Benefit test implies the recipient group member should get "economic or commercial value to enhance its commercial position". The benefit test is interlinked with the an arm's length test in the sense that it seeks an answer to the question whether under a similar situation an independent enterprise would have been willing to pay for the activity concerned, or would have performed the activity in- house for itself. So far as the benefit test is concerned, as we have noted earlier, it is alien to the definition of international transaction' under the Indian transfer pricing legislation. So far as arm's length test is concerned, it presupposes that such a transaction is possible in arm's length situation. However, in a situation in which the subsidiary does not have adequate financial standing of its own and is inadequately capitalized, none will guarantee financial obligations of such a subsidiary.

39. The issuance of financial guarantee in favour of an entity, which does not have adequate strength of its own to meet such obligations, will rarely be done. The very comparison, between the consideration for which banks issue financial guarantees on behalf of its clients with the consideration for which the corporates issue guarantees for their subsidiaries, is ill-conceived because while banks seek to be compensated, even for the secured guarantees, for the financial risk of liquidating the underlying securities and meeting the financial commitments under the guarantee, the guarantees issued by the corporates for their subsidiaries are rarely, if at all, backed by any underlying security and the risk is entirely entrepreneurial in the sense that it seeks to maximize profitability through and by the subsidiaries. It is inherently impossible to decide arm's length price of a transaction which cannot take place in arm's length situation. The motivation or trigger for issuance of such guarantees is not the kind for consideration for which a banker, for example, issue the guarantees, but it is maximization of gains for the recipient entity and thus the MNE group as a whole. In general, thus, the consideration for issuance of corporate guarantees are of a different character altogether.

40. At this stage, it would appropriate to analyze the business model of bank guarantees, with which corporate guarantees are sometimes compared, in the context of benchmarking the arm's length price of corporate guarantees. A bank guarantee is a surety that that the bank, or the financial institution issuing the guarantee, will pay off the debts and liabilities incurred by an individual or a

business entity in case they are unable to do so. By providing a guarantee, a bank offers to honour related payment to the creditors upon receiving a request. This requires that bank has to be very sure of the business or individual to whom the bank guarantee is IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 being issued. So, banks run risk assessments to ensure that the guaranteed sum can be retrieved back from the business. This may require the business to furnish a security in the shape of cash or capital assets. Any entity that can pass the risk assessment and provide security may obtain a bank guarantee. The consideration for the issuance of bank guarantee, so far as a banker is concerned, is this. When the client is not able to honour the financial commitments and when client is not able to meet his financial commitments and the bank is called upon to make the payments, the bank will seek a compensation for the action of issuing the bank guarantee, and for the risk it runs inherent in the process of making the payment first and realizing it from the underlying security and the client. Even when such guarantees are backed by one hundred per cent deposits, the bank charges a guarantee fees. In a situation in which there is no underlying assets which can be realized by the bank or there are no deposits with the bank which can be appropriated for payment of guarantee obligations, the banks will rarely, if at all, issue the guarantees. Of course, when a client is so well placed in his credit rating that banks can issue him clean and unsecured guarantees, he gets no further economic value by a corporate guarantee either. Let us now compare this kind of a guarantee with a corporate guarantee. The guarantees are issued without any security or underlying assets. When these guarantees are invoked, there is no occasion for the guarantor to seek recourse to any assets of the guaranteed entity for recovering payment of defaulted guarantees. The guarantees are not based on the credit assessment of the entity, in respect of which the guarantees are issued, but are based on the business needs of the entity in question. Even in a situation in which the group entity is sure that the beneficiary of guarantee has no financial means to reimburse it for the defaulted guarantee amounts, when invoked, the group entity will issue the guarantee nevertheless because these are compulsions of his group synergy rather than the assurance that his future obligations will be met. We see no meeting ground in these two types of guarantees, so far their economic triggers and business considerations are concerned, and just because these instruments share a common surname, i.e. 'guarantee', these instruments cannot be said to be belong to the same economic genus. Of course, there can be situations in which there may be economic similarities, in this respect, may be present, but these are more of an exception than the rule. In general, therefore, bank guarantees are not comparable with corporate guarantees.

41. As evident from the OECD observation to the effect "In contrast, if for example a parent company raises funds on behalf of another group member which uses them to acquire a new company, the parent company would generally be regarded as providing a service to the group member", it is also to be clear that when the corporate guarantees are issued for the purpose of subsidiaries raising funds for acquisitions by such subsidiaries, these guarantees will be deemed to be services to the subsidiaries, and, as a corollary thereto, when corporate guarantees are issued for the subsidiaries to raise funds for their own needs, the corporate guarantees are to be treated as shareholder activity. The use of borrowed funds for own use is a reasonable presumption as it is a matter of course rather than exception. There has to be something on record to indicate or suggest that the funds raised by the subsidiary, with the help of the guarantee given by the assessee, are not for its own business purposes. As a plain look at the details of corporate guarantees would show,

these guarantees were issued to various banks in respect of the credit facilities availed by the subsidiaries from these banks. The guarantees were prima facie in the nature of shareholder activity as it was to provide, or compensate for lack of, core strength for raising the finances from banks. No material, indicating to the contrary, is brought on record in this case. Going by the OECD Guidance also, it is not really IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 possible to hold that the corporate guarantees issued by the assessee were in the nature of 'provision for service' and not a shareholder activity which are mutually exclusive in nature. In the light of these discussions, we are of the considered view, and are fully supported by the OECD Guidance in this, that the issuance of corporate guarantees, in the nature of quasi-capital or shareholder activity- as is the uncontroverted position on the facts of this case, does not amount to a service in which respect of which arm's length adjustment can be done.

42. As observed by Hon'ble Delhi High Court in the case of CIT v. EKL Appliances Ltd. [2012] 345 ITR 241/209 Taxman 200/24 taxmann.com 199 (Delhi), a re- characterization of a transaction is indeed permissible, inter alia, in a situation "(i) where the economic substance of a transaction differs from its form and (ii) where the form and substance of the transaction are the same but arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner". The case of a corporate guarantee clearly falls in the second category as no independent enterprise would issue a guarantee without an underlying security as has been done by the assessee. We may, in this regard, refer to the observations made by Hon'ble High Court, speaking through Hon'ble Justice Easwar (as he then was), as follows:

> '16. The Organization for Economic Co-operation and Development ('OECD', for short) has laid down "transfer pricing guidelines" for Multi-National Enterprises and Tax Administrations. These guidelines give an introduction to the arm's length price principle and explains article 9 of the OECD Model Tax Convention. This article provides that when conditions are made or imposed between two associated enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises then any profit which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, if not so accrued, may be included in the profits of that enterprise and taxed accordingly. By seeking to adjust the profits in the above manner, the arm's length principle of pricing follows the approach of treating the members of a multi-national enterprise group as operating as separate entities rather than as inseparable parts of a single unified business. After referring to article 9 of the model convention and stating the arm's length principle, the guidelines provide for "recognition of the actual transactions undertaken" in paragraphs 1.36 to 1.41. Paragraphs 1.36 to 1.38 are important and are relevant to our purpose. These paragraphs are reproduced below:--
>
> "1.36 A tax administration's examination of a controlled transaction ordinarily should be based on the transaction actually undertaken by the associated enterprises as it has been structured by them, using the methods applied by the taxpayer insofar as

these are consistent with the methods described in Chapters II and III. In other than exceptional cases, the tax administration should not disregard the actual transactions or substitute other transactions for them. Restructuring of legitimate business transactions would be a wholly arbitrary exercise the inequity of which could be compounded by double taxation created where the other tax administration does not share the same views as to how the transaction should be structured.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 1.37 However, there are two particular circumstances in which it may, exceptionally, be both appropriate and legitimate for a tax administration to consider disregarding the structure adopted by a taxpayer in entering into a controlled transaction. The first circumstance arises where the economic substance of a transaction differs from its form. In such a case the tax administration may disregard the parties' characterization of the transaction and re- characterise it in accordance with its substance. An example of this circumstance would be an investment in an associated enterprise in the form of interest-bearing debt when, at arm's length, having regard to the economic circumstances of the borrowing company, the investment would not be expected to be structured in this way. In this case it might be appropriate for a tax administration to characterize the investment in accordance with its economic substance with the result that the loan may be treated as a subscription of capital. The second circumstance arises where, while the form and substance of the transaction are the same, the arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner and the actual structure practically impedes the tax administration from determining an appropriate transfer price. An example of this circumstance would be a sale under a long-term contract, for a lump sum payment, of unlimited entitlement to the intellectual property rights arising as a result of future research for the term of the contract (as previously indicated in paragraph 1.10). While in this case it may be proper to respect the transaction as a transfer of commercial property, it would nevertheless be appropriate for a tax administration to conform the terms of that transfer in their entirety (and not simply by reference to pricing) to those that might reasonably have been expected had the transfer of property been the subject of a transaction involving independent enterprises. Thus, in the case described above it might be appropriate for the tax administration, for example, to adjust the conditions of the agreement in a commercially rational manner as a continuing research agreement.

1.38 In both sets of circumstances described above, the character of the transaction may derive from the relationship between the parties rather than be determined by normal commercial conditions as may have been structured by the taxpayer to avoid or minimize tax. In such cases, the totality of its terms would be the result of a condition that would not have been made if the parties had been engaged in arm's length dealings. Article 9 would thus allow an adjustment of conditions to reflect those which the parties would have attained had the transaction been structured in accordance with the economic and commercial reality of parties dealing at arm's length."

17. The significance of the aforesaid guidelines lies in the fact that they recognise that barring exceptional cases, the tax administration should not disregard the actual transaction or substitute other transactions for them and the examination of a controlled transaction should ordinarily be based on the transaction as it has been actually undertaken and structured by the associated enterprises. It is of further significance that the guidelines IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 discourage re-structuring of legitimate business transactions. The reason for characterisation of such re-structuring as an arbitrary exercise, as given in the guidelines, is that it has the potential to create double taxation if the other tax administration does not share the same view as to how the transaction should be structured.

18. Two exceptions have been allowed to the aforesaid principle and they are

(i) where the economic substance of a transaction differs from its form and (ii) where the form and substance of the transaction are the same but arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner.'

43. It is thus clear that even if we accept the contention of the learned Departmental Representative that issuance of a corporate guarantee amounts to a 'provision for service', such a service needs to be re-characterized to bring it in tune with commercial reality as "arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner". No bank would be willing to issue a clean guarantee, i.e. without underlying asset, to assessee's subsidiaries when the banks are not willing to extend those subsidiaries loans on the same terms as without a guarantee. Such a guarantee transaction can only be, and is, motivated by the shareholder, or ownership considerations. No doubt, under the OECD Guidance on the issue, an explicit support, such as corporate guarantee, is to be benchmarked and, for that purpose, it is in the service category but that occasion comes only when it is covered by the scope of 'international transaction' under the transfer pricing legislation of respective jurisdiction. The expression 'provision for services' in its normal or legal connotations, as we have seen earlier, does not cover issuance of corporate guarantees, even though once a corporate guarantee is covered by the definition of international transaction', it is benchmarked in the service segment. In view of the above discussions, OECD Guidelines, as a matter of fact, strengthen the claim of the assessee that the corporate guarantees issued by the assessee were in the nature of quasi-capital or shareholder activity and, for this reason alone, the issuance of these guarantees should be excluded from the scope of services and thus from the scope of 'international transactions' under section 92B. Of course, once a transaction is held to be covered by the definition of international transaction, whether in the nature of the shareholder activity or quasi-capital or not, ALP determination must depend on what an independent enterprise would have charged for such a transaction. In this light of these discussions, we hold that the

issuance of corporate guarantees in question was not in the nature of 'provision for services' and these corporate guarantees were required to be treated as shareholder participation in the subsidiaries.

44. As for the words 'provision for services" appearing in Section 92B, and connotations thereof, our humble understanding is that this expression, in its natural connotations, is restricted to services rendered and it does not extend to the benefits of activities per se. Whether we look at the examples given in the OECD material or even in Explanation to Section 92B, the thrust is on the services like market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, and scientific research, legal or accounting service or coordination services. As a matter of fact, even in the Explanation to Section 92B- which we will deal with a little later, guarantees have been grouped in item 'c' dealing with capital financing, rather than in item 'd' which IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 specifically deals with 'provision for services'. When the legislature itself does not group 'guarantees' in the 'provision for services' and includes it in the 'capital financing', it is reasonable to proceed on the basis that issuance of guarantees is not to be treated as within the scope of normal connotations of expression 'provision for services'. Of course, the global best practices seem to be that guarantees are sometimes included in 'services' but that is because of the extended definition of 'international transaction' in most of the tax jurisdictions. Such a wide definition of services, which can be subject to arm's length price adjustment, apart, "Transfer Pricing and Intra-Group Financing - by Bakker & Levvy" (ibid) notes that "the IRS has issued a non-binding Field Service Advice (FSA 1995 WL 1918236, 1 May 1995) stating that, in certain circumstances (emphasis supplied), a guarantee may be treated as a service". If the natural connotations of a 'service' were to cover issuance of guarantee in general, there could not have been an occasion to give such hedged advice. This will be stretching the things too far to suggest that just because when guarantees are included in the international transactions, these guarantees are included in service segment in contradistinction with other heads under which international transactions are grouped, the guarantees should be treated as services, and, for that reason, included in the definition of international transactions. That is, in our considered view, purely fallacious logic. In our considered view, under Section 92B, corporate guarantees can be covered only under the residuary head i.e. "any other transaction having a bearing on the profits, income, losses or assets of such enterprise". It is for this reason that Section 92B, in a way, expands the scope of international transaction in the sense that even when guarantees are issued as a shareholder activity but costs are incurred for the same or, as a measure of abundant caution, recoveries are made for this non-chargeable activity, these guarantees will fall in the residuary clause of definition of international transactions under section 92B. As for the learned Departmental Representative's argument that "whether the service has caused any extra cost to the assessee should not be the deciding factor to determine whether it is an international and then gives an example of brand royalty to make his point. What, in the process, he overlooks is that Section 92B(1) specifically covers sale or lease of tangible or intangible property". The expression "bearing on the profits, income, losses or assets of such enterprises" is relevant only for residuary clause i.e. any other services not specifically covered by Section 92B. It was also contended that, while rendering Bharti Airtel decision, the Delhi Tribunal did go overboard in deciding something which was not even raised before us. In the written submission, it was stated that "Hon'ble Delhi ITAT was not

requested by the contesting parties to decide the issue as to whether the provision of guarantee was a service or not". That's not factually correct. We are unable to see any merits in learned Departmental Representative's contention, particularly as decision categorically noted that not only before the Tribunal, but this issue was also raised before the DRP- as evident from the text of DRP decision. We now take up the issue with respect to specific mention of the words in Explanation to Section 92B which states that "For the removal of doubts, it is hereby clarified that (i) the expression "international transaction" shall include........ (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." There is no dispute that this Explanation states that it is merely clarificatory in nature inasmuch as it is 'for the removal of doubts', and, therefore, one has to proceed on the basis that it does not alter the basic character of definition of 'international transaction' under Section 92B. Accordingly, this Explanation is to be read in conjunction with the main provisions, and in harmony with the scheme of the provisions, under Section 92B. Under this Explanation, five categories of transactions have been clarified to IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 have been included in the definition of 'international transactions'. The first two categories of transactions, which are stated to be included in the scope of expression 'international transactions' by virtue of clause (a) and (b) of Explanation to Section 92B, are transactions with regard to purchase, sale, transfer, lease or use of tangible and intangible properties. These transactions were anyway covered by transactions 'in the nature of purchase, sale or lease of tangible or intangible property'. The only additional expression in the clarification is 'use' as also illustrative and inclusive descriptions of tangible and intangible assets. Similarly, clause (d) deals with the "

> provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service" which are anyway covered in "provision for services" and "mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to anyone or more of such enterprises ". That leaves us with two clauses in the Explanation to Sect ion 92B which are not covered by any of the three categories discussed above or by other specific segments covered by Section 92B, namely borrowing or lending money. The remaining two items in the Explanation to Section 92B are set out in clause (c) and
>
> (e) thereto, dealing with (a) capital financing and (b) business restructuring or reorganization. These items can only be covered in the residual clause of definition in international transactions, as in Section 92B (1), which covers "any other transaction having a bearing on profits, incomes, losses, or assets of such enterprises". It is, therefore, essential that in order to be covered by clause (c) and (e) of Explanation to Section 92B, the transactions should be such as to have bearing on profits, incomes, losses or assets of such enterprise. In other words, in a situation in which a transaction has no bearing on profits, incomes, losses or assets of such enterprise, the

> transaction will be outside the ambit of expression 'international transaction'. This aspect of the matter is further highlighted in clause (e) of the Explanation dealing with restructuring and reorganization, wherein it is acknowledged that such an impact could be immediate or in future as evident from the words "irrespective of the fact that it (i.e. restructuring or reorganization) has bearing on the profit, income, losses or assets of such enterprise at the time of transaction or on a future date". What is implicit in this statutory provision is that while impact on " profit, income, losses or assets" is sine qua non, the mere fact that impact is not immediate, but on a future date, would not take the transaction outside the ambit of 'international transaction'. It is also important to bear in mind that, as it appears on a plain reading of the provision, this exclusion clause is not for "contingent" impact on profit, income, losses or assets but on "future" impact on profit, income, losses or assets of the enterprise.

The important distinction between these two categories is that while latter is a certainty, and only its crystallization may take place on a future date, there is no such certainty in the former case. In the case before us, it is an undisputed position that corporate guarantees issued by the assessee to the various banks and crystallization of liability under these guarantees, though a possibility, is not a certainty. In view of the discussions above, the scope of the capital financing transactions, as could be covered under Explanation to Section 92B read with Section 92B(1), is restricted to such capital financing transactions, including inter alia any guarantee, deferred payment or receivable or any other debt during the course of business, as will have "a bearing on the profits, income, losses or assets or such enterprise". This precondition about impact on profits, income, losses or assets of such enterprises is a precondition embedded in Section 92B(1) and the only relaxation from this condition precedent is set out in clause (e) of the Explanation which provides that the bearing on profits, income, losses or assets could be immediate or on a future date.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 These guarantees do not have any impact on income, profits, losses or assets of the assessee. There can be a hypothetical situation in which a guarantee default takes place and, therefore, the enterprise may have to pay the guarantee amounts but such a situation, even if that be so, is only a hypothetical situation, which are, as discussed above, excluded. When an assessee extends an assistance to the associated enterprise, which does not cost anything to the assessee and particularly for which the assessee could not have realized money by giving it to someone else during the course of its normal business, such an assistance or accommodation does not have any bearing on its profits, income, losses or assets, and, therefore, it is outside the ambit of international transaction under section 92B (1) of the Act.

45. Before we part with this issue, there are a couple of things that we would like to briefly deal with.

46. The first issue is this. We find that in the case of Four Soft Ltd v. Dy. CIT [(2011) 142 TTJ 358 (Hyd)], a co-ordinate bench had, vide order dated 9th September 2011, observed as follows:

> "We find that the TP legislation provides for computation of income from international transaction as per Section 92B of the Act. The corporate guarantee provided by the assessee company does not fall within the definition of international transaction. The TP legislation does not stipulate any guidelines in respect to guarantee transactions. In the absence of any charging provision, the lower authorities are not correct in bringing aforesaid transaction in the TP study. In our considered view, the corporate guarantee is very much incidental to the business of the assessee and hence, the same cannot be compared to a bank guarantee transaction of the Bank or financial institution."

47. However, within less than four months of this decision having been rendered, the Finance Act 2012 came up with an Explanation to Section 92B stating that "for the removal of doubts", as we have noted earlier in this decision, "clarified" that international transactions include, inter alia, capital financing by way of guarantee. This legislative clarification did indeed go well beyond what a coordinate bench of this Tribunal held to be the legal position and we are bound by the esteemed views of the coordinate bench. We are, therefore, of the opinion that the Explanation to Section 92B did indeed enlarge the scope of definition of 'international transaction' under section 92B, and it did so with retrospective effect. If, for argument sake, it is assumed that the insertion of Explanation to Section 92B did not enlarge the scope of definition, there cannot obviously be any occasion to deviate from the decision that the coordinate bench took in Four Soft Ltd. case (supra), but if the scope of the provision was indeed enlarged, as is our opinion, the question that really needs to be addressed whether, given the peculiar nature and purpose of transfer pricing provision, is it at all a workable idea to enlarge the scope of transfer pricing provisions with retrospective effect There can be little doubt about the legislative competence to amend tax laws with retrospective effect, and, in any case, we are not inclined to be drawn into that controversy either. On the issue of implementing the amendment in transfer pricing law with retrospective effect, in the case of Bharti Airtel Ltd. (supra), a coordinate bench had observed as follows:

> "34. There is one more aspect of the matter. The Explanation to Section 92B has been brought on the statute by the Finance Act 2012. If one is to proceed on the basis that the provisions of Explanation to Section 92B enlarges the IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 scope of Section 92B itself, even as it is modestly described as 'clarificatory' in nature, it is an issue to be examined whether an enhancement of scope of this anti avoidance provision can be implemented with retrospective effect. Undoubtedly, the scope of a charging provision can be enlarged with retrospective effect, but an anti-avoidance measure, that the transfer pricing legislation inherently is, is not primarily a source of revenue as it mainly seeks compliant behaviour from the assessee vis-à-vis certain norms, and these norms cannot be given effect from a date earlier than the date norms are being introduced. However, as we have decided the issue in favour of the assessee on merits and even after taking into account the amendments brought about by Finance Act 2012, we need not deal with this aspect of the matter in greater detail."

48. In the present case, we have held that the issuance of corporate guarantees were in the nature of shareholder activities- as was the uncontroverted claim of the assessee, and, as such, could not be included in the 'provision for services' under the definition of 'international transaction' under section 92B of the Act. We have also held, taking note of the insertion of Explanation to Section 92B of the Act, that the issuance of corporate guarantees is covered by the residuary clause of the definition under section 92B of the Act but since such issuance of corporate guarantees, on the facts of the present case, did not have "bearing on profits, income, losses or assets", it did not constitute an international transaction, under section 92B, in respect of which an arm's length price adjustment can be made. In this view of the matter, and for both these independent reasons, we have to delete the impugned ALP adjustment. The question, which was raised in Bharti Airtel's case (supra) but left unanswered as the assessee had succeeded on merits, remains unanswered here as well. However, we may add that in the case of Krishnaswamy SPD v. Union of India [2006] 281 ITR 305/151 Taxman 286 (SC), wherein Their Lordships had, inter alia, observed that "the law does not compel a man to do what he cannot possibly perform. The law itself and its administration is understood to disclaim as it does in its general aphorisms, all intention of compelling impossibilities, and the administration of law must adopt that general exception in the consideration of particular cases. It was for this reason that a coordinate bench of this Tribunal, in the case of Channel Guide India Ltd. v. Asstt. CIT [2012] 139 ITB 49/25 taxmann.com 25 (Mum.), held that even though the assessee had not deducted the applicable tax at source under section 195, the disallowance could not be made under section 40(a)(i) since the taxability was under the provisions which were amended, post the payment having been made by the assessee, with retrospective effect. All this only shows that even when law is specifically stated to have effect from a particular date, its being implemented in a fair and reasonable manner, within the framework of judge made law, may require that date to be tinkered with. When a proviso is introduced with effect from a particular date specified by the legislature, the judicial forums, including this Tribunal, at times read it as being effect from a date much earlier than that too. One such case, for example, is CIT v. Ansal Landmark Township (P.) Ltd. [2015] 377 ITR 635/234 Taxman 825/61 taxmann.com 45 (Delhi), wherein Hon'ble Delhi High Court confirmed the action of the Tribunal in holding that the provision, though stated to be effective from 1st April 2013 must be held to be effective from 1st April 2005. Whether such an exercise can be done in the present case is, of course, something to be examined and our observations should not be construed as an expression on merits of that aspect of matter. Given the fact that the assessee has succeeded on merits in this case, it would not really be necessary to deal with that aspect of the matter.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

49. The second issue is this. We must deal with the question whether in this case the matter should have been referred to a larger bench. The parties before us were opposed to the matter being sent for consideration by the special bench, and at least one of the reasons for which the grievance of the assessee is upheld, i.e. guarantees being in the nature of shareholder activity and excludible from the scope of services for that reason alone, is an area which had come up for consideration for the first time. In effect, therefore, there was no conflict on this issue of and the other issues, given decision on the said issue, were wholly academic. It cannot be open to refer the academic questions to the

special bench. No doubt, some decisions of the coordinate benches which have reached the different conclusions. There is, however, no conflict in the reasoning. Four Soft Ltd. decision (supra) had decided the issue in favour of the assessee but that was with respect to the law prior to insertion to Explanation to Section 92B. As for the post-amendment law and the impact of amendment in the definition of 'international transaction', the matter was again decided in favour of the assessee by Bharti Airtel Ltd. decision (supra) on the peculiar facts of that case. The decisions like Everest Kento Cylinders Ltd. (supra) and Aditya Birla Minacs Worldwide (supra) were decisions in which the assessee had charged the fees and, for that reason, such cases are completely distinguishable as discussed above. In Prolific' Corp Ltd. case (supra), as indeed in any other case so far, it was not the case of the assessee that corporate guarantees are quasi-capital, or shareholder activity, in nature, and, for that reason, excludible from chargeable services, even if these are held to be services in nature. That plea has been specifically accepted in the present case. Therefore, the question whether issuance of corporate guarantee per se in general constitutes a 'international transaction' under section 92B would have been somewhat academic question on the facts of this case. In any event, in Prolific' Corp Ltd. case (supra), an earlier considered decision on the same issue by coordinate bench of equal strength was simply disregarded and that fact takes this decision out of the ambit of binding judicial precedents. We have also noted that in view of the decision a coordinate bench, in the case of JKT Fabrics v. Dy. CIT [2005] 4 SOT 84 (Mum.) and following the Full bench decision of Hon'ble AP High Court in the case of CIT v. BR Constructions [1993] 202 ITR 222/[1994] 73 Taxman 473 (AP), a decision disregarding an earlier binding precedent on the issue is per incurium. Such decisions cannot be basis for sending the matters to special bench since occasion for reference to special bench arises when binding and conflicting judicial precedents from coordinate benches come up for consideration. That was not the case here. All these factors taken together, in our considered view, it was not possible in this case to refer the matter for constitution of a special bench. In any case, whatever we decide is, and shall always remain, subject to the judicial scrutiny by Hon'ble Courts above and our endeavour is to facilitate and expedite, within our inherent limitations, that process of such a judicial scrutiny, if and when occasion comes, by analyzing the issues in a comprehensive and holistic manner.

50. In the light of the detailed discussions above, and for the detailed reasons set out above, we uphold the grievance raised by the assessee. The impugned ALP adjustment of Rs 2,23,62,603, thus stands deleted. As we do so, however, we must add that, in our considered view, the way forward, to avoid such issues being litigated and to ensure satisfactorily resolution of these disputes, must include a clear and unambiguous legislative guidance on the transfer pricing implications of the corporate guarantees as also on the methodology of determining its ALP, if necessary. Of course, no matter how good is the legislative framework, the importance of a very comprehensive analysis, in the transfer pricing study, of the nature of corporate guarantees issued by the assessees, can never be overemphasized. The sweeping IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 generalizations, vague statements and evasive approach in the transfer pricing study reports, which are quite common in most of the transfer pricing reports, cannot do good to a reasonable cause. When judicial calls on the complex transfer pricing issues are to be taken, utmost clarity in the legislative framework and a comprehensive analysis of relevant facts, in the transfer pricing documentation, are basic inputs. Unfortunately, both of these things leave a lot to be desired. We can only hope, and we do hope, that things will change for better.

23. We are in considered agreement with the views so expressed by the coordinate bench. It is not really necessary to deal into finer details, beyond stating that the matter in the case of Micro Ink (supra) is already pending for adjudication before Hon'ble jurisdictional High Court, and it is, therefore, no longer the right forum to sit in judgment whether or not in view of the arguments of the revenue, this decision of Micro Ink (supra), needs to be revisited. It is for the Hon'ble Courts above to take that call now. Respectfully following the views taken by the coordinate bench, therefore, we uphold the grievance of the assessee, and direct the Assessing Officer to delete the ALP adjustment of Rs 4,19,22,177.

(iii) Liaison services: Rs 34,86, 285

24. The assessee is engaged in the manufacturing formulations and APIs (Active Pharmaceutical Ingredients), and the products so manufactured by the assessee are required to be registered with the competent authorities, under the local regulatory framework, in each jurisdiction. The assessee has obtained these registrations through its local affiliates in such jurisdictions. During the relevant previous year, the assessee has paid product registration charges amounting to Rs 2,48,48,862, at a mark up @ 10% over actual expenses incurred, to Zydus Healthcare (USA)LLC (Zydus LLC, in short) , and Rs 4,44,95,968, at a mark up @ 6%, to Zydus Pharma Inc, Japan (Zydus Japan, in short). The stand of the assessee was that the services rendered by these entities was for preparing all the relevant information and data, filing applications, before the regulatory authorities in respective jurisdictions. This work was one under the guidance of technical and qualified persons. The work was done under the local regulatory framework and in accordance with the local laws. The AEs were also to follow up with the regulatory authorities, deal with deficiency letters, if any, in respect of such registration applications and provide necessary legal and technical inputs to the assessee. As the AEs were the least complex entities, between the assessee and the AEs, the AEs were chosen as the tested parties. Accordingly, as noted by the TPO himself, the benchmarking was done as follows:

> 5.2 As per assessee, after carrying out FAR analysis, assessee has chosen Zydus LLC and Zydus Japan as tested parties as Cadila was considered more complex entity. Also the AEs appear to be less complex entitles as their functions are limited to providing product registration and marketing support services to Cadila. Net Cost Plus Mark Up (NCP) was considered appropriate PLI. The focus of selection of comparable company was to identify companies carrying out similar functions and operating in similar market as that of Zydus LLC and IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 Zydus Japan. Companies chosen as per the Assessee were those companies that provided marketing or related services. The Assessee has chosen companies carrying out the following services in respect of Zydus LLC:

```
A)    Advertising services
B)    Direct Mail advertising services
C)    Business services
D)    General Management services
E)    Management consulting services
F)    Public Relation Services
```

5.2.1 After carrying out qualitative and quantitative filtration, following companies were selected by the assessee as comparable independent companies in respect of Zydus LLC:

```
a)    COSSETTE COMMUNICATIONS GRP
b)    HARTE HANKS INC
c)    INTERPUBLIC GROUP OF COS.
d)    MDC PARTNERS INC
e)    VALASSIS COMMUNOCAT1ONS INC
```

5.2.2 The weighted average NCP of the aforesaid companies ranged from 2.80 to 18.40 per cent with an arithmetical mean of 10.20%. Thus, it was concluded that Zydus LLC has earned NCP of 10 per cent on the transactions and hence payment by assessee to Zydus LLC for availing registration and marketing services was stated to be at arm's length from Indian transfer pricing perspective.

5.3 Similarly, the assessee has chosen the following companies that provided the marketing and related services in respect of transactions with Zydus Japan:

```
A)    Advertising Agencies
B)    Outdoor advertisement services
C)    Advertising, not elsewhere classified
D)    Business Services
E)    Management services
F)    Management Consulting Services
G)    Public Relations services
H)    Facilities support management services
I)    Business Consulting Services, Not Elsewhere Classified
```

5.3.1 In all the assessee has taken a list of total 338 independent companies for comparables, which after qualitative and quantitative screening, the assessee has finally identified the following 9 comparable independent companies:

1 AOCORP AUSTRIA LIMITED IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 2 COG CO LTD 3 COMMUNICATION DESIGN INTERNATIONAL LTD.

4 FAR EAST DDB PUBLIC COMPANY LIMITED 5 LEGS COMPANY LIMITED 6 MPCLTD 7 OR1COM INC 8 PHOTON GROUP LIMITED 9 SALMAT LIMITED 5.3.2 The weighted average NCP of the aforesaid 13 companies comes to between 2.6% to 13.52% with an arithmetical mean of 6.03 per cent.

Thus, the NCP of Zydus Japan was taken at 6 percent.

25. The Transfer Pricing Officer was, however, not satisfied with the approach so adopted by the assessee. He rejected the same by observing as follows 5.4 The business description of above companies which the Assessee wants to compare for its product registration services are perused. The companies selected are primarily in the business of direct mail media, marketing, advertising, public relation services, management services, business consulting services, outdoor advertising services, etc. None of these companies have functions which are similar to the activities of Zydus LLC and Zydus Japan i.e. product registration services. In view of above, the assessee should have rejected all these companies for comparison purpose. Detailed business description of these companies was submitted by the Assessee himself as Appendix-B & D to its transfer pricing report. It is further seen that these companies are taking all business risks as like an independent entrepreneur; whereas the assessee himself submitted that there was no business risk involved in respect of this product registration services, namely, market risk, contract risk, regulatory risk with regard to its transaction with Cadila.

5.4.1 In fact, transaction carries zero risk and if it was to be compared with independent entrepreneur, adjustment to the results of above mentioned companies was to be carried out which would have resulted into profit of almost zero percent as these were purely administrative support services provided by one person to another and where all cost incurred on behalf of others has been paid to the last penny. In view of above, comparables selected are rejected as there is -

a) No similar functions involved

b) No similar risk involved

c) No adjustment for above carried out as per rule 10B (e) (iii) as provided in Income tax rule 1962.

5.4.2 The work carried out by Zydus LLC and Zydus Japan are zero risk administrative operations i.e. non business operations which does not IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 have any profit motive or element with it and these are similar to the "other similar services" as provided under US regulations for services cost method (SCM) and cannot be considered as core activities of Zydus LLC and Zydus Japan. There are a number of cases relating to pharmaceutical industries where this office has received transfer pricing reference and where similar issue is involved i.e. product registration services carried out by Associated Enterprise in the United States for their Indian parent company. None of these companies have charged any mark up and parent companies have just reimbursed all the expenses incurred by the Associated Enterprise on its behalf in this regard.

26. The TPO then observed that in the assessment year 2006-07, this Tribunal had held 2% mark up as reasonable mark up, and, accordingly, ALP is to be computed on the same basis. In effect thus, the transaction that the assessee had with its own AE was adopted as a comparable to that extent. The consideration paid in excess of the amount so computed was disallowed as in excess of arm's length price. As regards the assessee's stand that even if the arm's length price is computed on the basis of assessee's stand in 2006-07, which has met approval of the Tribunal, the benefit of +_5% should be allowed, the TPO rejected the same and observed that such an adjustment comes into play

only when there are more than one comparable prices available and the ALP is computed on the basis of arithmetic mean of such prices. What the TPO disregarded, however, was the fact that the Tribunal had also directed the benefit of +_5% in the order. In effect thus, the amount paid by the assessee in excess of 2% mark up was declined, and 2% mark up was accepted as an arm's length price. On this basis, an ALP adjustment of Rs.34,86,285 was justified. Aggrieved by the addition so proposed, assessee carried the matter in appeal before the DRP, but without any success. Aggrieved by the resultant ALP adjustment of Rs 34,86,285, the assessee is in appeal before us.

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

28. We have noticed that what has been held to be arm's length price in this case is the price at which transaction has taken place between the assessee and its AE, to the extent it has been accepted to be at an arm's length price in the assessment year 2006-07. In effect, thus the basis of determining ALP of this transaction is another intra AE transaction at an earlier point of time. That is not acceptable. The approach adopted by the TPO is devoid of legally sustainable merits. A comparable, by definition, has to be in respect of an uncontrolled transaction. That is what the law states so unambiguously. If authority is needed for this proposition also, the same is contained in the decisions of the coordinate bench in the case of Skoda India Ltd Vs ACIT [(2009) 30 SOT 319 (Pune)] and a Third Member decision in the case of ACIT Vs Technimont ICB India Pvt Ltd [(2012) 138 ITD (TM) 23 (Mum)]. The approach adopted by the authorities below, therefore, cannot meet our judicial approval. If at all such an approach can be rationalized, it can be so rationalized by treating the decision for AY 2007-08 as a binding judicial precedent and follow it in entirety rather than in part. That, however, has not been done by the TPO.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

29. Even if we assume, as is contended by the TPO, that comparables adopted by the assessee are not proper comparables in view of the FAR analysis, the solution lies in finding the right comparables, and not in discarding the method altogether and adopting another intra AE transaction as sole and valid comparable. Clearly, the TPO has not brought into consideration any valid comparables to dislodge the comparables adopted by the assessee, and the only comparable brought by him is of an intra AE transaction and, therefore, not a valid comparable. Unless the TPO conducts this exercise of finding valid and suitable comparables by meeting the shortcomings pointed out by him, it cannot be open to the TPO to disregard the comparables selected by the assessee. As a matter of fact once the assessee has adopted an approach to determination of ALP, it cannot be open to the TPO to reject the same unless he can come up with some other more appropriate an approach to determination of arm's length price. The benchmarking done by the assessee can be rejected only when an alternate benchmarking, which has less shortcomings than the one pointed out in the benchmarking by the assessee, is demonstrated. If these comparables are not appropriate, let there be other comparables which are appropriate. If comparables are not available for a application of a particular method of the ALP, the possibilities of other methods are to be examined. As for his observation to the effect that "in fact, transaction carries zero risk and if it

was to be compared with independent entrepreneur, adjustment to the results of above mentioned companies was to be carried out which would have resulted into profit of almost zero percent as these were purely administrative support services provided by one person to another and where all cost incurred on behalf of others has been paid to the last penny", this observation is very much divorced from the ground reality inasmuch as it cannot be suggested that when an enterprise carries on any work for an independent enterprise or rank outsider, which does not have any risk at all, the enterprise should do it without any mark up or profit to itself and he should not even recover any part of the overheads costs relatable to such a work. When a business enterprise does anything for an independent enterprise, as is the inherent nature of an arm's length transaction, it does not do so driven by the desire to serve the mankind but with a view to make reasonable profit out of it, and, therefore, arm's length mark up of any service rendered by any AE cannot be zero. What decides the ALP of a transaction is answer to the question that if that the tested party was to be enter into the same transaction with an independent enterprises, i.e. rank outsider, what would have been consideration for the same. Profit is not a reward for risk alone, it is also a reward for the functions performed as also the assets employed in rendition of service. The TPO has examined only the risk factor, in FAR analysis, and ignored the functions and assets. That approach cannot be approved. However, as the matter regarding appropriate comparables has not been discussed in reasonable detail and as the discussions in the orders of the authorities below have been somewhat at superficial level, we deem it fit and proper to remit the matter to the stage of the DRP for fresh adjudication on this issue, in accordance with the law, in the light of our observations above after giving a reasonable opportunity of hearing to the assessee, and by way of a speaking order. We direct so.

30. So far impugned ALP adjustments are concerned, to sum up our conclusions,

(i) the ALP adjustment of Rs 5,00,35,270 in respect of interest on loans is deleted;

(ii) the ALP adjustment of Rs 4,19,22,177 in respect of corporate guarantee IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 commission is deleted; and (iii) the ALP adjustment of Rs 34,86,285 is remitted to the assessment stage for fresh adjudication.

31. Ground no. 1 is thus partly allowed.

32. In the second ground of appeal, the assessee has raised the following grievance:

> That the learned Assessing Officer erred in law and on facts in making an addition of Rs.18,18,96,302/- u/s. 40(a)(i) on the ground that no TDS was made by the Appellant u/s. 195 of the I.T. Act. Without prejudice to the merits of the Appellant's case, the said action of the learned Assessing Officer being in clear violation of the direction of the Hon'ble DRP, is prima facie unjustified and unsustainable.

33. So far as this grievance of the assessee is concerned, the relevant material facts are as follows. During the relevant previous year, the assessee has made a number of payments to non residents

without any tax deduction at source. On this fact, the Assessing Officer required the assessee to show cause as to why all these payments aggregating to Rs 101.44 crores, without deduction of tax at source, not be disallowed under section 40(a)(i). It was pointed out by the assesse that, vide his earlier submissions, complete details of payments made to non-residents have already been placed on record. It was also pointed out at the time of making these payments, the taxability of payments in the hands of the non-residents is duly examined and only when it does not have any income taxable in India, the payments are made without deduction of tax at source. It was also submitted that the supporting evidences are duly furnished to the tax authorities and no infirmities therein have been pointed out. It was then submitted that, as is the settled legal position in the light of Hon'ble Supreme Court's judgment in the case of G E India Technology Centre Pvt Ltd Vs CIT [(2010) 327 ITR 456 (SC)], tax withholding obligations under section 195(1), from payments made to non residents, come into play only when income embedded therein are taxable in India. That is not, according to the assessee, case here. It was also submitting that, as held by the Tribunal in the case of ACIT Vs Anchor Health and Beauty Care Pvt Ltd [13 taxmann.com 148 (Mum),unless Assessing Officer demonstrates that the recipient has a tax liability in respect of income embedded in the payment, he cannot invoke disallowance under section 40(a)(i) on the short ground that the assessee did not deduct tax at source while making payments to the non residents. The Assessing Officer the proceeded to deal with these submissions by stating as follows:

> 3.6 Brief description of the nature of the above payments is as under :
>
> Clinical Trial Studies Company made payments to above non residents towards clinical trials of certain pharmaceutical molecules. Clinical Trials involves scientific knowledge and experience of the conducting person/firm or company with regard to administration of medicines to animals/human beings and keeping them under observation of IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 Doctors/Scientists for reaction of medicines, and efficacy of said medicine in mitigating the disease/disorder for which it is intended to be used. It involves study of side effects/contra indications. All these observations are noted down systematically/chronologically and the effects of medicine are analyzed and submitted to the assessee company in the form of information consisting of observations, graphs, tables and suggestions by the said foreign research entity. Therefore payments for clinical trials are fees for technical services as these services not only involve services of technical person, but also these services are ancillary and subsidiary to the application or enjoyment of information for which the payments are made.
>
> Analytical studies for Bio Analysis:
>
> Bio Analysis studies involve highly technical Analytical study of distribution of medicine molecules the body of the animal/human being after administration of the same. This may involve study with time taken for distribution of medicine to the particulars organ of the body and amount/concentration of medicine reaching the organ and reaction of cell of the organ etc. This is also a highly technical study and

covered by FTS. After the Analytical study the Research Institute submits a report giving the data and analysis of studies. All these data and analysis of studies submitted to the assessee company in the form of information consisting of observations, graphs, tables and suggestions by the said foreign research entity. Therefore payments for clinical trials are fees for technical services as these services not only involve services of technical person, but also these services are ancillary and subsidiary to the application or enjoyment of information for which the payments are made.

Assessee submitted that with regard to the Bio-Analysis and Clinical Trials the language of the DTAA with USA, UK, Canada and Singapore, is clear with regard to 'fees for Technical Services' which exclude such payments when no technology is made available by the non-resident party, to whom such payment for Bio-Analysis is made.

3.7 Contention of the assessee is considered carefully. The arguments of the assessee are that the 'DTAA with regard to FTS excludes such payments where no technology is made available by the non-resident. Article 12 reads as under :

ARTICLE 12-Royalties and fees for included services-1. Royalties and fees for included services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such royalties and fees for included services may also be taxed in the Contracting State in which they arise and according to the laws of that State; but if the beneficial owner of the royalties or fees for included services is a resident of the other Contracting State, the tax so charged shall not exceed :

(a) in the case of royalties referred to in sub-paragraph (a) of paragraph 3 and fees for included services as defined in this Article [other than services described in sub-paragraph (b) of this paragraph]:

```
             (i)        during the first five taxable years for which this
       Convention      has effect,
                                               IT (TP) Nos.519 and 898/Ahd/201
                                                      and 694 and 747/Ahd/2015
                                          Assessment years: 2009-10 and 2010-11




               (a)     15 per cent of the gross amount of the royalties
```

> or fees for included services as defined in this Article, where the payer of the royalties or fees is the Government of that Contracting State, a political sub-

division or a public sector company; and

(b) 20 per cent of the gross amount of the royalties or fees for included services in all other cases; and

(ii) during the subsequent years, 15 per cent of the gross amount of royalties or fees for included services; and

(b) in the case of royalties referred to in sub-paragraph (b) of paragraph 3 and fees for included services as defined in this Article that are ancillary and subsidiary to the enjoyment of the property for which payment is received under paragraph 3(b) of this Article, 10 per cent of the gross amount of the royalties or fees for included services.

3. The term "royalties" as used in this Article means :

> (a) payments of any kind received as a consideration for the use of, or the right to use, any copyright of a literary, artistic, or scientific work, including cinematograph films or work on film, tape or other means of reproduction for use in connection with radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience, including gains derived from the alienation of any such right or property which are contingent on the productivity, use, or disposition thereof; and
>
> (b) payments of any kind received as consideration for the use of, or the right to use, any industrial, commercial, or scientific equipment, other than payments derived by an enterprise described in paragraph 1 of Article 8 (Shipping and Air Transport) from activities described in paragraph 2(c) or 3 of Article 8.

4. For purposes of this Article, "fees for included services" means payments of any kind to any person in consideration for the rendering of any technical or consultancy services (including through the provision of services of technical or other personnel) if such services :

> (a) are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment described in paragraph 3 (a) of this article is received; or
>
> b) make available technical knowledge, experience, skill, know-

how, or processes, or consist of the development and transfer of a technical plan or technical design.

UK Article 12 IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

4. For the purposes of paragraph 2 of this Article, and subject to paragraph 5, of this Article, the term "fees for technical services" means payments of any kind of any person in consideration for the rendering of any technical or consultancy services (including the provision of services of a technical or other personnel) which:

> (a) are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment described in paragraph 3(a) of this article is received ; or
>
> (b) are ancillary and subsidiary to the enjoyment of the property for which a payment described in paragraph 3(b) of this Article is received; or
>
> (c) make available technical knowledge, experience, skill know-

how or processes, or consist of the development and transfer of a technical plan or technical design.

CANADA Article 12

4. For the purposes of this Article, 'fees for Included services' means payments of any kind to any person in consideration for the rendering of any technical or consultancy services (including through the provision of services of technical or other personnel) if such services :

> (a) are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment described in paragraph 3 is received; or
>
> (b) make available technical knowledge, experience, skill, know-

how, or processes or consist of the development and transfer of a technical plan or technical design.

SINGAPORE Article 12

4. The term "fees for technical services" as used in this Article means payments of any kind to any person in consideration for services of a managerial, technical or consultancy nature (including the provision of such services through technical or other personnel) if such services:

> (a) are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment described in paragraph 3 is received; or
>
> (b) make available technical knowledge, experience, skill, know-

how, or processes, which enables the person acquiring the services to apply the ethnology contained therein; or

(c) consist of the development and transfer of a technical plan or technical design, but excludes any service that does not enable the person acquiring the service to apply the technology contained therein.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 For the purpose of (b) and (c) above, the person acquiring the service shall be deemed to include an agent, nominee, or transferee of such person.

3.8 It may be seen from the clause 4 of the article, that definition of Fees for included services mean payment for rendering any technical consultancy service if such service are ancillary to the application of information. Therefore the payments for Clinical Trials and Bio Analysis studies clearly falls in Fees for included services and the assessee was liable to deduct tax from such payments. Between the sub clauses (a) and (b) of clause 4 of Article the word used is "or", therefore the payments in question fall under sub clause (a) and not under sub clause (b) as sought to be argued by the assessee. Certificate of a CA in form 15CA/CB is not the final authority on the taxability of an amount in India. It is a facility given to the assessee for convenience in remittance.

Payments for consultancy (legal. patent application or other consultant) 3.9 There are 69 entries of consultancy, 160 entries of consultancy for patent fees and one entry for legal fees in the data supplied to the assessee. These were payments towards services given by the foreign law firms either individuals, firm of individuals or companies with regards to IPRs and Trademark Registration/Patent Registration. Assessee has contended that the payment falls in the 'Independent Personal Services' under DTAA and falls in Article 14 or 15 of the DTAA. For example, Article 15 of DTAA between India-USA reads as under

> ARTICLE 15 - Independent personal services - 1. Income derived by a person who is an individual or firm of individuals (other than a company) who is a resident of a Contracting State from the performance in the other Contracting State of professional services or other independent activities of a similar character shall be taxable only in the first-mentioned State except in the following circumstances when such income may also be taxed in the other Contracting State :
>
> (a) if such person has a fixed base regularly available to him in the other Contracting State for the purpose of performing his activities; in that case, only so much of the income as is attributable to that fixed base may be taxed in that other State; or
>
> (b) if the person's stay in the other Contracting State is for a period or periods amounting to or exceeding in the aggregate 90 days in the relevant taxable year.

2. The term "professional services" includes independent scientific, literary, artistic educational or teaching activities as well as the independent activities of physicians, surgeons, lawyers, engineers,

architects, dentists and accountants.

3.10 Assessee is correct in stating that such payment made to individuals and firm of individuals is not taxable in India. However verification of the list of payment reveals that there are some payments to companies of those countries. There is no dispute after reading of DTAA and the Income tax Act, that these payments of consultancy paid to companies are taxable in India. List of companies to whom consultancy and legal charges which are in the nature of Independent Personal Services are as under :

> IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 Consultancy Fees Sl. No. Name of the Company Amount paid 1 Biopharma Technology Ltd. 1,39,058 2 Gorodissky & Partners Ltd 42,30,696 3 Pride City General Trading (L.L.C) 38,94,300 4 RIC Chemicals Plc 4,36,386 Consultancy for Patent application Sl. No. Name of the Company Amount paid 1 Anapharm INC 50,27,760 2 Computer Patents Annuities Ltd. 4,28,880 3 DM Kisch Inc. Patent, Trade mark and Copyright 8,87,265 Attorneys 4 Danubia Patent & Law Office LLC 42,711 5 Iphorgan Limited 98,179 6 Nixon & Vanderhye P.C. 5,45,887 7 Nixon & Vanderhye P.C. Attorney at Law 9,84,266 8 Sanford T. Colb & Co. Intellectual Property Law 55,883 Firm Legal Fees Sl. No. Name of the Company Amount paid 1 SL Balnes Anapharm INC 15,15,286 3.11 The assessee was liable to deduct tax from these payments which are in the nature of Independent Personal services, but failed to deduct u/s 195 of the Act.

Certificate of a CA in form 15CA/CB is not the final authority on the taxability of an amount in India. It is a facility given to the assessee for convenience in remittance. Therefore after examination of the nature of 'Independent Personal Services' it is held that the amounts paid to companies are taxable in India and the assessee failed to deduct tax.

3.12 Details of payments made to non-residents without deduction of tax is as under :

Nature of Expenditure	Amount	Nature of payment u/s. DTAA
1 Bio Analysis	13,33,43,342	Fees included Services
2 Clinical Trials	73,03,725	(Article 12)
3 Consultancy Fees	87,00,440	Independent Personal
4 Consultancy Fees for Patent Application	73,96,136	Services (Article 15)
5 Legal Fees-SL. Balnes	15,15,286	
6 Professional Fees (Linklatees S.L., Spain Company)	29,80,712	

IT (TP) Nos.519 and 898/
and 694 and 747/A
Assessment years: 2009-10 and

7 Various Remittances	2,06,56,661	Consultancy etc., (Article 15)
Total	18,18,96,302	Independent Personal Service (Articles 12 & 15)

3.13 Therefore following payments made by the assessee company to non

residents without deducting the tax as required u/s 195 is liable to be added u/s 40(a)(i) of the Act.

34. He thus proposed to make a disallowance of Rs 18,18,96,302 under section 40(a)(i) of the Act. Aggrieved by the disallowance so proposed by the Assessing Officer, assessee raised a grievance before the Dispute Resolution Panel, but without much success. The DRP directed the Assessing Officer to refer the matter to the International Taxation wing of the department, and based on what has been held by the officers in the international tax wing, make the disallowance under section 40(a)(i). The observations of the DRP are reproduced below for ready reference:

> The contentions of the petitioner have been considered. The detailed chart showing 1193 remittances along with Form No.15CA/CB and reason for non-deduction of TDS and letter dated 11th February, 2010 issued by the ITO (International Taxation)-II, Ahmedabad submitted by the petitioner have been perused and considered. The Assessing Officer has not mentioned about any order by the ITO (International Taxation) - II, Ahmedabad who is the Competent Authority to decide whether foreign remittances were liable to be taxed in India and the Assessee was liable to deduct tax on such remittances. In view of these facts, the Assessing Officer is directed to obtain the order passed by the ITO (international Taxation)-II, Ahmedabad, on taxability and liability to deduct tax on foreign remittances on all the transactions under consideration and will disallow the expenditure for foreign remittances only to the extent of the foreign remittances liable to taxed in India on which the Assessee was liable to deduct tax u/s 195 of the I T Act. For the remaining expenditure disallowed u/s. 40(a)(i), the AO is directed to delete and objection to that extent will be treated as sustained.

35. Based on the stand taken by the Income Tax Officer (International Taxation- II), the Assessing Officer proceeded with the above disallowance of Rs.18,18,96,302. The assessee is aggrieved and is in appeal before us.

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

37. We must, at the outset, express our anguish at the evasive approach adopted by the DRP. They have simply declined to examine the matter on merits and preferred to let the Income Tax Officer in international tax wing decide what the DRP ought to have decided on its own. Simply because an ITO in the international tax wing decides that tax ought to have been deducted at source from certain payments IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment

years: 2009-10 and 2010-11 to non-residents, it does not mean that the DRP must mechanically uphold the related disallowance under section 40(a)(i). What was before the DRP was the question as to disallowance under section 40(a)(i) has been correctly made or not, and essentially, therefore, the DRP was required to decide as to whether income embedded in these payments was taxable in India or not. This process of judicial scrutiny cannot be delegated to a lower functionary, but when DRP holds that, to the extent such a disallowance is supported by the stand that the ITO (International Taxation) takes, the disallowance is upheld, the DRP, in effect, decides the matter on the basis of scrutiny by a lower functionary. Upholding the disallowance only because the disallowance is in consonance with the stand taken by another lower functionary amounts to preferring to the guided by the wisdom of a lower authority without application of own mind. Such an approach is wholly unsustainable in law. It also results in a situation that the view taken at the assessment stage travels in appeal directly to us, without independent scrutiny of the same by the CIT(A) or the DRP. That is much less than an ideal situation, and it does not meet our approval.

38. We have noted that, so far as the stand taken by the ITO (International Taxation) in the proceedings under section 201(1) is concerned, many of these issues have come up before coordinate benches of this Tribunal, in assessee's own cases, and the stand taken by the ITO has not been approved by several coordinate benches in judicial scrutiny. One such order is passed by this very coram in ITA No. 486/Ahd/2016 for the assessment year 2010-11. So far as these issues are concerned, the very foundation of impugned disallowance ceases to hold good in law. We may also add that, as is contended by the assesse, the order passed by the Assessing Officer is in violations of the directions given to the Assessing Officer. However, as these directions have been held to be inappropriate, nothing really turns on this grievance.

39. We may place on record the fact that the assessee has made elaborate arguments, on merits, in respect of these payments. The total payments made by the assessee were as many as 1,193 payments, out of which a large number of payments have been disallowed under section 40(a)(ia). Much as learned counsel urges us to examine these payments individually, and decide the disallowance under section 40(a)(i) on merits, we donot think that will be appropriate on the facts of this case. As we have noted earlier in this order, the DRP has not examined the matter on merits at all. The discussions by the Assessing Officer in respect of these payments have also been inadequate, superficial and without sufficient application of mind, and a reasonable case has not been made out for invoking the disallowance under section 40(a)(i) by meeting the arguments of the assessee and demonstrating that the income embedded in these payments is indeed taxable in India. As learned counsel for the assessee rightly contends, and as held by a coordinate bench in the case of Anchor Health and Beauty Care (supra), unless Assessing Officer demonstrates that the recipient has a tax liability in respect of income embedded in the payment, he cannot invoke disallowance under section 40(a)(i). It is equally true that the Assessing Officer cannot decide taxability of income embedded in these payments on the basis of sweeping generalizations either. Essentially, therefore, the DRP also must decide the matter on the same parameters and in the same manner. While doing so, the DRP may also call for, and take into account, specific case by case comments of the Assessing Officer on each of, or each set of- as may be IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 appropriate, the payment. The DRP may also take into account decisions of the coordinate benches, on the taxability of income embedded in

such payments, in assessee's own case as indeed in other similarly situated cases, as also other binding judicial precedents.

40. In view of the above discussions, as also bearing in mind entirety of the case, we deem it fit and proper to remit the matter to the file of the DRP for adjudication de novo on merits, after taking into account the decisions of the coordinate benches in assessee's own case as indeed other binding judicial precedents, in accordance with the law and by way of a speaking order. The DRP will give a due and fair opportunity of hearing to the assessee.

41. Ground no. 2 is thus allowed for statistical purposes.

42. In ground no. 3, the assessee has raised the following grievance:

> That the learned Assessing Officer erred in law and on facts in making a disallowance of Rs.16,06,73,002/- u/s 14A, instead of Rs.10,47,16,917/- being the correct disallowance as per Rule 8D r.w.s, 14A of the I.T. Act.

43. To adjudicate on this grievance, only a few material facts need to be taken note of. During the course of assessment proceedings, the Assessing Officer noticed that the assessee has disclosed a tax exempt income of Rs 117,52,65,961 on account of dividend income, interest income and share in partnership firm. It was also noticed that the assessee, on his own, had offered a disallowance under section 14A read with rule 8 D, in respect of expenses incurred for earning such tax exempt income, amounting to Rs 3,89,21,994. However, the Assessing Officer recomputed the said disallowance and, according to his calculation, the disallowance was quantified at Rs 16,06,73,002. It was in this backdrop that the Assessing Officer raised the disallowance on the basis of his computations, and proposed a further disallowance of Rs 12,17,51,000. Aggrieved, assessee raised a grievance before the DRP but without any success. The Assessing Officer thus made a further disallowance of Rs 12,17,51,000 which is impugned in appeal before us.

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

45. Learned counsel's short submission is that the impugned disallowance is incorrect for two reasons- first, that the computation of average investments takes into account investments abroad which do not yield tax exempt income; and - second, that the total interest paid is taken at Rs 66.40 crores whereas the actual interest paid is only Rs 64.37 crores. It is also pointed out that rectification petition under section 154 is pending in respect of these adjustments, and that he will be content by our direction to the Assessing Officer to look into these two issues. We see merits in the plea. It is beyond controversy that dividends from companies abroad do not enjoy the tax exempt status, and, as a corollary thereto, the related investments must therefore be kept out of investments yielding tax exempt income for the purpose of rule 8D. As for the correct figure of interest paid, it is purely a IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 factual issue and the Assessing Officer is, therefore, directed to look into the contention of the assessee by way of a speaking order after giving an opportunity of hearing to the assessee. To the

extent, disallowance under section 14A r.w.r. 8D stands reduced as a result of the above, the assessee will get relief. The balance addition stands confirmed as no grievance is raised in respect of that portion of disallowance. With these directions, the matter stands restored to the file of the Assessing Officer.

46. Ground no. 3 is thus allowed for statistical purposes.

47. Ground no. 4 is not pressed and is dismissed as such.

48. In ground no. 5, the assessee has raised the following grievance:

> That the learned Assessing Officer erred in law and on facts in not acknowledging in the Assessment Order, the availability of the amount of Carried Forward MAT Credit u/s. 115JAA of Rs.20,08,52,398/-, to which the Appellant is lawfully entitled to in view of it being covered under the provisions of MAT u/s. 115JB.

49. So far as this grievance of the assessee is concerned, short grievance of the assessee is that the Assessing Officer has not specifically mentioned that the assessee is entitled to carry forward the MAT credit of Rs 20,08,52,398. However, we are unable to see much merits in this plea because, as is the settled legal position in the view of Hon'ble Supreme Court's judgment in the case of CIT Vs Manmohan Das [(1966) 59 ITR 699 (SC)], in the year of carry forward only quantification of a set off claim is to be seen. The question as to its entitlement for being set off is to be examined in the year in which set off is claimed. Grievance of the assessee is premature and is dismissed as such.

50. Ground no. 5 is thus dismissed.

51. No other grievances raised by the assessee, as learned counsel for the assessee fairly states at the bar, are required to be adjudicated on merits, as these consequential in nature. In the result, the appeal filed by the assessee for the assessment year 2009-10 is thus partly allowed in the terms indicated above.

52. We now take up the appeal filed by the Assessing Officer for the assessment year 2009-10.

53. In the first three grounds of appeal, which we will take up together, the Assessing Officer has raised the following grievance:

> 1. Whether the DRP has erred in holding that the assessee is eligible for deduction u/s 80IC on the entire profit of 84.65% which includes the profit of 76.74% which the company was already earning from marketing IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 the same products. The actual increase in profit was only 7.91% after manufacturing the same products at Baddi unit.

> 2. Whether the DRP has substantially erred in holding that the AO should not determine the fair market value of goods when there is no intercorporate transfer, despite the provisions of sect/on 80IA(8) which applies to intra-corporate transfer of goods from eligible business unit to non-eligible business unit of the assessee. In the case of the assessee only Baddi unit is eligible unit.
>
> 3. Whether the DRP has substantially erred by not approving the AO's action for determination of market value of goods on internal transfer from eligible unit to non-eligible unit as per the provisions of section 80IA(8).

54. So far as these grievances of the Assessing Officer are concerned, learned representatives fairly agree that the issue is covered, in favour of the assesse, by a coordinate bench in assessee's own case for the assessment year 2008-09, which in turn has followed the assessment years 2006-07 and 2007-08 which have attained finality as revenue's appeals against these orders stand dismissed. As a matter of fact, all that the DRP has done is to follow the said order of the coordinate bench.

55. We see no infirmity in the relief so granted by the DRP and no arguments have been advanced before us to even contend that we should take any other view of the matter than the view so taken by the coordinate bench. In this view of the matter, and respectfully following the coordinate bench decision, we confirm the relief granted by the CIT(A) and decline to interfere in the matter.

56. Ground nos. 1 to 3 are thus dismissed.

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

58. As regards this grievances of the Assessing Officer as well, learned representatives fairly agree that the issue is covered, in favour of the assesse, by a coordinate bench in assessee's own case for the assessment year 2008-09, which in turn has followed the assessment years 2006-07 and 2007-08 which have attained finality as revenue's appeals against these orders stand dismissed. As a matter of fact, all that the DRP has done is to follow the said order of the coordinate bench.

59. We see no infirmity in the relief so granted by the DRP and no arguments have been advanced before us to even contend that we should take any other view of the matter than the view so taken by the coordinate bench. In this view of the matter, and respectfully following the coordinate bench decision, we confirm the relief granted by the CIT(A) and decline to interfere in the matter.

60. Ground no. 4 is thus dismissed.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

61. In ground no. 5, the Assessing Officer has raised the following grievance:

> Whether the DRP is right in allowing deduction of share of profit from firm (Zydus Healthcare Sikkim) of Rs.76.75 Crores u/s. 10(2A) overlooking the fact that the same was not included in the total income of the firm. Hence there was no question of double taxation.

62. So far as this grievance of the Assessing Officer is concerned, the relevant material facts are as follows. During the course of the assessment proceedings, the Assessing Officer noticed that the assessee has claimed that its income of Rs.76,75,02,966 is exempt under section10(2A) of the Act as 96% share in partnership firm by the name of Zydus Healthcare Sikkim. When the Assessing Officer probed the matter further, he noticed that the total income of the said partnership firm, as per statement of income, was only Rs 4,97,200. When this, what was termed by the Assessing Officer as 'discrepancy' was brought to the notice of the assessee, it was explained by the assessee that statement of income of the partnership firm shows the taxable income component of its income, whereas what has been claimed as exempt in the hands of the assessee is entire share of profit, authorised by the partnership deed, received by the assessee. In other words, even when the assessee receives a partnership firm's share of income, which is exempt from tax in the hands of the partnership firm, it will be exempt in the hands of the assessee under section 10(2A) anyway. This interpretation was not accepted by the Assessing Officer. He was of the view that exemption under section 10(2A), in respect of assessee's share of income in partnership firm, is confined to the amount which is included in total income of the firm, and thus is taxable in nature. He was also of the view that exemption under section 10(2A) is to avoid double taxation of an income, in the hands of the partnership firm as also in the hands of the partners, but when an income is not taxable in the first place, section 10(2A) cannot come into play at all. It was in this backdrop that the Assessing Officer proposed an addition of Rs.76,75,02,966. Aggrieved, assessee raised a grievance before the Dispute Resolution Panel. The DRP was of the view that, as explained by the CBDT circular No. 636 dated 31st August 1992, the legal position is that "the share of partner in the income of the firm will not be included in computing his total income". This circular was issued in the context of explaining the scope of Section 10(2A) and it binds the field authorities. It was held by the DRP that "on holistic consideration of entire facts, interpretation given by the Assessing Officer is resulting into absurd situation defeating the very purpose of introduction of the new scheme of taxation of firms and partners with effect from 1st April 1993 and is against the binding circular issued by the CBDT, and, hence, it is held that addition made by the Assessing Officer cannot be sustained". The DRP sustained the aforesaid objection of the assesse, and direct the Assessing Officer not to make any addition on this account. The Assessing Officer is aggrieved and is in appeal before us.

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

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

64. We find that Section 10states that in computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included, and clause 2(A) thereof states that "in the case of a person being a partner of a firm which is separately assessed as

such, his share in the total income of the firm" and Explanation appended thereto provides that "For the purposes of this clause, the share of a partner in the total income of a firm separately assessed as such shall, notwithstanding anything contained in any other law, be an amount which bears to the total income of the firm the same proportion as the amount of his share in the profits of the firm in accordance with the partnership deed bears to such profits". A plain reading of this provision does indicate that what is to be treated as exempt from tax under section is partner's share in "total income" of the firm. The expression "total income" is a defined expression under section 2(45) and it refers to "the total amount of income referred to in section 5, computed in the manner laid down in this Act". It is this approach which underlies the argument, as indeed adopted by the Assessing Officer, that an income which is not includible in total income cannot ordinarily be a part of total income of the firm.

65. However, the above approach, as DRP has rightly concluded, would be erroneous. We must bear in mind the fundamental legal position that, definition of the expression 'total income' under section 2(45), as indeed all definitions under section 2, are subject to the rider that these definitions are in consonance with the context in which the meanings are to be found out, as obvious from the words "unless the context otherwise requires". The context in which we have to find meaning to the expression 'total income' in the scheme of Section 10(2A) is the scheme of taxation of partnership firms. In the method of taxation of firms that we now follow in India, while the partnership firm is treated as an opaque entity and taxed as such on the profits arising in its hands, the share of profits in the firm in the hands of its partners are excluded from their taxable income. The point of taxation is, as such, the profits being earned by the partnership firm. Once the tax liability in respect of these profits is discharged, that is end of the matter. Any subsequent division of profits does not result in taxation once again in the hands of the partners. Viewed thus, total income of the partnership firm cannot mean taxable income of the partnership firm because the connotations of total income must essentially extend to a literal and common sense meaning of 'total income' which refers to the 'income of the firm in its entirety'. It is so for the reason that in case an income of the firm is held to be not taxable in nature, by the virtue of an incentive provision or whatever other reason, it cannot be brought to tax in the hands of the partner only because it has not been taxed in the partnership firm; that would be destructive of the purpose for which incentive deduction is granted to the partnership firm. If a literal interpretation is to be adopted, as indeed has been adopted by the Assessing Officer, all that an incentive deduction will result in is shifting the point of taxation from the partnership firm to the partners. That will be quite inappropriate to the context in which the expression 'total income' is used in section 10(2A).

66. We have noted that the DRP has gone by the CBDT circular on the basis that this circular requires entire share from the partnership firm, whether included in total income or not, to be treated as exempt under section 10(2A). The relevant extracts from this circular for ready reference, are reproduced below:

> IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 Taxation of firm's income

48. Before changes made by the Finance Act, the system of levy of tax on firms involved double taxation. The firm as such was taxed in respect of its total income at rates varying from 5% to 18% (the maximum rate being applicable at Rs 1 lakh and above). After deducting the tax payable by the firm, the balance of income was distributed amongst the partners and they were again taxed at the appropriate rates. Further, the tax liability of a firm and its partners depended upon the question whether the firm was granted registration under the Income-tax Act or not. In the case of a registered firm, the firm paid tax on its total income according to the rates prescribed in the Schedule for registered firms. An unregistered firm was taxed at the rates applicable to individuals, with the share income included in the hands of the partners for rate purposes only. There has been a consistent demand for removal of the double taxation. A new scheme of assessment of firms has been introduced from assessment year 1993-94. The scheme is modelled after the scheme introduced by the Direct Taxes Laws (Amendment) Act, 1987, with suitable modifications to take care of the difficulties pointed out in the context of the 1987 scheme. The scheme contained in Direct Taxes Laws (Amendment) Act, 1987 sought to tax firms at the maximum marginal rate after allowing interest and remuneration to partners. Further there was a rigorous definition of "whole-time working partners" to whom alone remuneration was payable. The deduction for remuneration and interest allowable to partners and allowing remuneration to any partner or partners at the discretion of the firm, have been suitably restructured.

48.1 A firm will now onwards be taxed as a separate entity (Sections 184 &

185). There will be no distinction between registered and unregistered firms, and clauses (39) and (48) of section 2 containing the definition of "registered firm" and "unregistered firm" have been omitted. After allowing remuneration and interest to the partners, the balance income of the firms will be subject to maximum marginal rate of tax of income-tax, which will be 40% for assessment year 1993-94. The surcharge on income-tax will be at the rate of 12%, of the total tax, if the income exceeds Rs 1,00,000. The earlier distinction between rates of income-tax for professional and non-professional firms has been removed. Partners are not liable to tax in respect of the share of income from the firm. However, remuneration and interest allowed to partners will be charged to income-tax in their respective hands. The only distinction between professional and non-professional firms will be in respect of slabs for allowing deduction to firms in respect of remuneration.

48.2 The share of the partner in the income of the firm will not be included in computing his total income [section 10(2A)]. However, interest, salary, bonus, commission or any other remuneration allowed by the firm to a partner will be liable to be taxed as business income in the partner's hand [section 2(24)(ve) and section 28(v)]. An Explanation has been added to the newly inserted clause (2A) of section 10 to make it clear that the remuneration or interest which is disallowed in the hands of the firm will not suffer taxation in the hands of the partner. In case, any remuneration paid to a partner is disallowed in the hands of the firm or the amount is varied in subsequent proceedings, the partner's assessment can be rectified [section155(1A)].

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 48.3 The gross total income of the firm is to be determined in the normal way under different heads as in the case of any taxable entity. The gross total income so computed is reduced by salary, bonus, commission, or any remuneration payable or paid to a partner [section 40(b)]. Remuneration due to or received by a partner is not to be assessed as income under the head "Salaries" [Explanation 2 to section 15]. Any salary, interest, bonus, commission or remuneration due to or received by a partner in view of clause

(v) to section 28 shall be chargeable to income-tax under the head "Profit and gains of business or profession."

48.4 The payment of remuneration only to working partner is allowable [defined in Explanation 4 to section 40(b)]. Only individuals are capable of being working partners.

48.5 The payments should be duly authorised by and in accordance with the terms of the partnership deed. These payments will be allowed as deduction only for a period beginning with the date of the partnership deed and not for any earlier period. Thus, if a partner is allowed a higher remuneration by varying the terms of the deed on a particular date, such higher remuneration cannot be allowed to him for any period prior to the said date. However, as the financial year 1992-93 had already commenced, by the time the Bill received the Presidential assent, it would not have been possible for assessees to change the partnership deed with effect from 1st April, 1992. Therefore, the Finance Act has provided that for the previous year, 1992-93 interest or remuneration would be allowed if the partnership deed provides for such payment anytime during the accounting period. Thus, for the previous year 1992-93, relevant to assessment year 1993-94, the terms of the partnership deed may be amended to have retrospective operation. There is no restriction as to the number of times the terms of a partnership deed may be changed during a previous year in so far as payment of salary, bonus, commission or other remuneration to a working partner is concerned. It is also possible that a partner who is not a 'working partner' may become a 'working partner' at any point of time during a year (or vice versa). In such a situation also, the said terms of the deed may be suitably amended.

48.6 Of the aggregate payment to all partners by way of salary, bonus, commission or other remuneration upto Rs.50,000 is fully allowable in the hands of the firm. In case the aggregate payment exceeds the limit of Rs.50,000, certain monetary limits have been prescribed under section 40(b)(v)) in the form of a percentage of "book profit" [defined in Explanation 3 to section 40(b)]. Upto a "book- profit" of Rs.1,00,000 or a loss, in the case of a professional firm and Rs.75,000, in the case of a non-professional firm, the limit is 90% of the "book-profit" or Rs.50,000 whichever is higher. For "book- profit" exceeding Rs.1,00,000 in the case of a professional firm and Rs.75,000 in the case of a non professional firm, the limit is 60% of the "book-profit" in this slab. For the balance of the "book-profit" after these two slabs, the limit is 40%.

48.7 Under the provisions of section 40A(2) an Assessing Officer can disallow any expenditure, if it is excessive having regard to the legitimate needs of the business. There have been several representations on this issue. A demand has been raised that this provision should not be used in the case of remuneration paid by a firm to its partners, since a ceiling is already separately IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 provided. The Finance Minister, in his speech dated 30th April, 1992 in Parliament during the budget discussion stated as follows:

> "There seems to be some apprehension that the provisions of section 40A(2) of the Income-tax Act may be indiscriminately resorted to by the Assessing Officer to make disallowance out of salary paid to the partners as being excessive. The Central Board of Direct Taxes will be asked to issue instructions to the Assessing Officers so as to ensure that this power is not used in the case of small firms and even otherwise, it should be used sparingly."

Assessing Officers who invoke the provisions of section 40A(2), in any case, must keep in mind the assurance given by the Finance Minister to the Parliament.

48.8 Interest paid to a partner would be allowed as a deduction in the hands of the firm. The payment of interest should be in pursuance of the partnership deed. The maximum rate of interest allowed would be 18% simple interest per annum [section 40(b)(iv)].

48.9 Changes have been made in the scheme of set-off and carry forward of losses. The existing provisions relating to firms and their partners in sections 76 and 77 have been omitted. Under the new scheme, the firms are treated as a separate entity and the losses suffered by them would be allowed to be carried forward in their hands only. There would be cases where brought forward losses apportioned to a partner have not been set-off in the hands of the partner prior to assessment year 1992-93. A provision has been made for dealing with brought forward losses pertaining to assessment years prior to assessment year 1993-94. In such cases the carried forward losses of a partner will be allowed as a set-off in the assessment income of the firm subject to the condition that the partner continued to remain a partner in the said firm (section 75).

48.10 Although the distinction between a registered and unregistered firm has been removed, a firm will be assessed as a firm only if--

(i) the partnership is evidenced by an instrument ; and

(ii) the individual shares of the partners are specified in that instrument.

A copy of the partnership instrument duly certified has to accompany the return of income for the relevant year for which assessment as a firm is first sought. Thereafter, assessment as a firm will continue to be made so long as the constitution of the firm remains unchanged. Whenever there is a change in the constitution of a firm, a copy of the new partnership instrument has to be similarly filed. Where a firm does not comply with the provisions of section 184 for any assessment year, the firm shall be assessed as for the assessment year in the same manner as an association of persons and all the provisions of this Act shall accordingly be applicable (section 185).

[Underlined portion has been relied upon by the assessee and the DRP]

67. The scheme of taxation of firm, as evident from the above circular, supports our preceding analysis about true connotations of the expression 'total income' appearing in section 10(2A). As is quite clear from the CBDT circular above, the IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 point of taxation in the case of partnership firm is assessment of income of the firm, and once that exercise is carried out, that is the end of the matter so far as taxation of income of the firm is concerned. It cannot once again be brought to tax in the hands of the partners. As a corollary to this undisputed position, when an income is found to be not taxable in the hands of the partnership firm, it cannot be brought to tax in the hands of the partners on the ground that it was not actually taxed in the hands of the partnership firm. If it is found to be not taxable in the hands of the partnership firm, it is not taxable at all, because so far as income of the partnership firm is concerned, that is the only point when such an income, if at all and to whatever extent, can be taxed. We have also noted that in the subsequent assessment year the Assessing Officer himself has not made such additions in the course of assessment proceedings, and the above interpretation, as such, stands accepted by the field authorities. Yet, ironically, when DRP grants this relief on the same point, the Assessing Officer is in appeal before us. This fact shows how frivolous is this appeal. In view of the above discussions, in our considered view, the DRP was quite justified in granting the impugned relief. We approve the same and decline to interfere in the matter.

68. Ground no. 5 is thus dismissed.

69. In ground no. 6, the Assessing Officer has raised the following grievance:

> Whether the DRP has erred in considering Product Registration expenses of Rs.7.22 Crores as revenue expenditure when the same entitles the assessee to export the registered drugs to various countries for many years.

70. Learned representatives fairly agree that this issue is settled in favour of the assessee by decisions of the coordinate benches in assessee's own case, and Hon'ble High Court has declined to admit appeal against such decision, as in the esteemed views of Their Lordships, no question of law arises from these decisions. The relief granted to the assessee on this point in past has thus achieved finality. In this view of the matter, we approve the relief granted by the DRP on this point and decline to interfere in the matter.

71. Ground no. 6 is thus dismissed.

72. In ground no. 7, the Assessing Officer has raised the following grievance:

> Whether the DRP has substantially erred in holding that Trademark Registration and Patent fee of Rs.4.64 Crores are revenue expenses when the same are classified as intangible assets u/s.32(1)(ii) of the Act.

73. Learned representatives fairly agree that this issue is settled in favour of the assessee by decisions of the coordinate benches in assessee's own case, and Hon'ble High Court has declined to admit appeal against such decision, as in the esteemed views of Their Lordships, no question of law arises from these decisions. The relief granted to the assessee on this point in past has thus achieved finality. In IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 this view of the matter, we approve the relief granted by the DRP on this point and decline to interfere in the matter.

74. Ground no. 7 is thus dismissed.

75. In ground no. 8, the Assessing Officer has raised the following grievance:

> Whether the DRP has substantially erred in holding that the expenses incurred outside the approved R&D facility is also eligible for weighted deduction in contravention of section 35(2AB) whereby only expenditure on in-house research and development facility qualifies for weighted deduction.

76. Learned representatives fairly agree that this issue is also settled in favour of the assessee by decisions of the coordinate benches in assessee's own case, and Hon'ble High Court has declined to admit appeal against such decision, as in the esteemed views of Their Lordships, no question of law arises from these decisions. The relief granted to the assessee on this point in past has thus achieved finality. In this view of the matter, we approve the relief granted by the DRP on this point and decline to interfere in the matter.

77. Ground no. 8 is thus dismissed.

78. In ground no. 9, the Assessing Officer has raised the following grievance:

> Whether the DRP is right in allowing depreciation of Rs.9.38 lacs on Hummer car despite the fact that the same was in the name of the Director and there was no evidence to show that the same was used wholly and exclusively for the purpose of business. The provisions of section 32 were therefore not satisfied.

79. As far as this grievance of the Assessing Officer is concerned, there is no dispute that the car was not legally owned by the assessee company but by the director, even though the payment for acquisition of this car was made by the assessee company and the car is used by the company. The beneficial ownership thus rests with the assessee company. The depreciation was proposed to be declined by the Assessing Officer mainly on the ground that the assessee did not own the vehicle in question. However, the assessee succeeded in the DRP in his objection to this proposal. We have noted that the DRP has given a categorical finding to the effect that the car was used for the purpose

of business and the Assessing Officer has himself allowed the running and maintenance expenses of this car. It has also been noted that the registration of car in the name of driver was a matter of convenience as it gave advantage to the assessee in terms of road tax. On these facts, as held by the DRP, the mere fact that the car was not legally owned by the assessee company- particularly when beneficial ownership of this vehicle is not even in dispute, the depreciation on car cannot be declined. Aggrieved, assessee is in appeal before us.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

80. Having heard the rival contentions and having perused the material on record, we are not inclined to disturb very well reasoned findings of the DRP and the conclusions arrived at by the DRP. Once it is not in dispute that the vehicle was owned, in substance, by the assessee and the vehicle was used for the purposes of its business, there cannot be any legally sustainable reasons for declining the depreciation. Learned Departmental Representative could not bring on record any material to dislodge the findings of the DRP. We approve the action of the DRP and decline to interfere in the matter.

81. Ground no. 9 is thus dismissed.

82. In ground no. 10, the Assessing Officer has raised the following grievance:

> Whether the DRP was right in allowing foreign exchange derivative loss of Rs.30.40 Crores despite the finding that the same was a notional loss in the nature of contingent liability not pertaining to the relevant year.

83. As regards this grievance of the Assessing Officer, the relevant material facts are as follows. During the course of assessment proceedings, the Assessing Officer noticed that the assessee has claimed a deduction of Rs 5,686.40 lakhs in respect of exchange rate arising on long term foreign currency loans, even though only Rs.2,645.90 lakhs, relating to loss actually incurred in this year, was amortized and debited to the profit and loss account. On these facts, the Assessing Officer required the assessee to show cause as to why the balance amount of Rs 3,040.50 lakhs not be treated as notional loss and disallowed. In reply, the assessee placed reliance on the decision of Hon'ble Supreme Court in the case of CIT Vs Woodward Governor India Pvt Ltd [(2009) 32 ITR 254 (SC)] and on Special Bench decision of this Tribunal in the case of Oil and Natural Gas Corp Ltd Vs DCIT [(2004) 83 ITD SB 51(Del)]. The Assessing Officer, however, rejected the submissions so made by the assessee and proposed to disallow the loss of Rs 3,040.50 lakhs. He also noted that claiming the entire loss in this year will be contrary to the matching concept, and placed reliance on, in this regard, on judicial precedents in the cases of Madras Industrial Corp Ltd Vs CIT [(1997) 91 Taxmann 340 (SC) and Taparia Tools Ltd Vs JCIT [(2003) 126 Taxmann 544 (Bom)]. Aggrieved by this proposal, the assesse raised a grievance before the DRP and he was successful in that. Disapproving the stand of the Assessing Officer, the DRP held that "the issue of allowability of foreign exchange loss arising on the balance sheet date is an item of expenditure under section 37(1) of the Act, and this view is upheld by Hon'ble Supreme Court in the case of CIT Vs Woodward

Governor India Pvt Ltd [(2009) 312 ITR 254 (SC)]. Considering the same, addition proposed in the draft assessment order is deleted and objection of the petitioner is upheld". The Assessing Officer is aggrieved and is in appeal before us.

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

85. We have noted that there is no dispute about the fact that the loss on foreign exchange conversion is allowed as a deduction, and the dispute is confined to the IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 fact whether entire amount is to be allowed as deduction or only so much of the loss as pertains to the payments actually made during the relevant year. Once the deduction has been allowed by the Assessing Officer himself, though in respect of loss in respect of payments made during the year, clearly there is no dispute about its being on revenue account. The question then remains whether the deduction should be of the entire loss evident as at the year end or it should remain confined to the loss which has fructified in the sense the payments are actually made. As we deal with this question, it is important to bear in mind the fact that it is one of the most fundamental principles of accounting that while all anticipated losses are taken into account in computing the profits and losses of business, even though such losses may not have crystallized, as long as these losses can be reasonably quantified. This approach can be contrasted with the anticipated profits being ignored, in the computation of profits and losses of an enterprise, unless the profits are actually realized. To that extent, there is a dichotomy in accounting approach but then this is what is the sound accounting policy and it has the sanction of law. As a matter of fact, it is this principle, as recognized by Hon'ble Supreme Court in the case of Chainrup Sampatram Vs CIT [(1953) 24 ITR 481 (SC)], which explains the valuation of closing stock on market price or cost price whichever is less. The loss actually incurring to the assessee may finally be more or less than the loss computed on the balance sheet date but that does not affect the claim for deduction of a loss which can be reasonably anticipated. There is thus, in principle, no difficulty is seeking a deduction in respect of a reasonably anticipated loss, even though it may not have actually fructified, in computation of profits and gains of business. While on this issue, we may also refer to the following observations made by Hon'ble Supreme Court in the case of Woodward Governor (supra):

> As stated above, one of the main arguments advanced by the learned Addl. Solicitor General on behalf of the Department before us was that the word "expenditure" in s. 37(1) connotes "what is paid out" and that which has gone irretrievably. In this connection, heavy reliance was placed on the judgment of this Court in the case of Indian Molasses Company (supra). Relying on the said judgment, it was sought to be argued that the increase in liability at any point of time prior to the date of payment cannot be said to have gone irretrievably as it can always come back. According to the learned counsel, in the case of increase in liability due to foreign exchange fluctuations, if there is a revaluation of the rupee vis-a-vis foreign exchange at or prior to the point of payment, then there would be no question of money having gone irretrievably and consequently, the requirement of "expenditure" is not met. Consequently, the additional liability arising on account of fluctuation in the rate of

> foreign exchange was merely a contingent/notional liability which does not crystallize till payment. In that case, the Supreme Court was considering the meaning of the expression "expenditure incurred" while dealing with the question as to whether there was a distinction between the actual liability in praesenti and a liability de futuro. The word "expenditure" is not defined in the 1961 Act. The word "expenditure" is, therefore, required to be understood in the context in which it is used. Sec. 37 enjoins that any expenditure not being expenditure of the nature described in ss. 30 to 36 laid out or expended wholly and exclusively for the purposes of the business should be allowed in computing the income chargeable under the head "Profits and gains of business". In ss.
>
> IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 30 to 36, the expressions "expenses incurred" as well as "allowances and depreciation" has also been used. For example, depreciation and allowances are dealt with in s. 32. Therefore, Parliament has used the expression "any expenditure" in s. 37 to cover both. Therefore, the expression "expenditure"

as used in s. 37 may, in the circumstances of a particular case, cover an amount which is really a "loss" even though the said amount has not gone out from the pocket of the assessee.

86. To this extent, the Assessing Officer was clearly in error in treating the loss on foreign exchange as a notional loss not deductible in computation of business income, as long as the related transaction is on revenue account- as aspect which is not in dispute. The relief granted by the DRP was thus justified. In any case, learned Departmental Representative has not pointed out any reasons or arguments for not confirming the action of the DRP. In view of these discussions, as also bearing in mind entirety of the case, we approve the conclusions arrived at on the facts of this case.

87. Ground no. 10 is thus dismissed.

88. In ground no. 11, the Assessing Officer has raised the following grievance:

> Whether the DRP is right in deleting the addition to Book Profit amounting to Rs.16.06 Crores being addition u/s 14A, despite the specific clause (f) to Exp.1 of section 115JB.

89. As regards this grievances of the Assessing Officer, learned representatives fairly agree that the issue is covered, in favour of the assesse, by a coordinate bench in assessee's own case for the assessment year 2008-09, which in turn has followed the assessment years 2006-07 and 2007-08. As a matter of fact, all that the DRP has done is to follow the said order of the coordinate bench.

90. We see no infirmity in the relief so granted by the DRP. No arguments have been advanced before us to persuade us to take any other view of the matter than the view so taken by the coordinate bench which have been followed by the DRP in the impugned order. In this view of the matter, and respectfully following the coordinate bench decision, we confirm the relief granted by

DRP and decline to interfere in the matter.

91. Ground no. 11 is thus dismissed.

92. In the result, the appeal of the Assessing Officer for the assessment year 2009-10 is thus partly allowed in the terms indicated above.

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

94. In the first ground of appeal, the assessee has raised the following grievance:

> IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 That the learned Assessing Officer erred in law and on facts in making an addition of Rs.6,55,25,762/- as upward adjustment on international transactions involving the provisions of Transfer Pricing.

95. In connected grievances, which we will take up together with the above grievance of the assessee, the Assessing Officer has raised the following grievance by way of its first and second grounds of appeal:

> 1. The DRP has erred in law and on facts in restricting the guarantee fee @ 1% without any basis as against 2.98% determined by the TPO on a scientific basis,
>
> 2. The DRP has substantially erred in law and on facts in directing the TPO to restrict benchmarking to new loans/advance taken during the year and not subject to old loans/advances to transfer pricing study.

96. So far as these grounds of appeal are concerned, only a few material facts need to be taken of at this stage. When a reference was made to the TPO for determination of arm's length price in respect of international transactions entered into by him, he proposed the following arm's length price adjustments:

> (i) Product Registration consideration paid to the AEs 39,36,230
>
> (ii) Corporate guarantee commission charges 8,62,37,606
>
> (iii) Interest on optionally convertible loans 3,76,36,873
>
> (iv) Interest on loan to Zydus France 13,44,042

97. The relevant facts of the case, so far as item nos. (i), (ii) and (iii) are concerned, are broadly the same as for the assessment year 2009-10 which we have discussed in detail earlier in this order. The variation is only in terms of the quantum of adjustments. For the sake of brevity, we need not, therefore, discuss these facts in much detail. As far as ALP adjustment on account on interest on

loan to Zydus France is concerned, the relevant facts are like this. During the course of proceedings before the TPO, it was noticed that the assessee has advanced a loan to Zydus France and the interest rate charged thereon is 6 months LIBOR plus 2.40%. The TPO, however, rejected this claim and, on the basis of information gathered from Dealscan database- except for inter alia secured loans or loans to A, AA and AAA rated companies, adopted the rate of 4.48% pa. Accordingly, an ALP adjustment of Rs 13,44,042 was proposed. Aggrieved by the adjustments so proposed by the TPO, except for the product registration consideration paid to the AEs, assessee raised the grievance before the DRP. So far as ALP in respect of guarantee commission charges are concerned, the DRP upheld the same in principle but restricted the rate of guarantee commission to 1%. The ALP adjustment was thus downscaled to Rs 2,40,91,100. As regards interest on convertible loans, the DRP upheld the action of the TPO though directed the AO to recalculate the ALP adjustment after taking care of calculation errors pointed out by the assessee. The ALP adjustment was at Rs 3,76,36,870. As regards loan to Zydus France, the DRP noted that as the TPO himself has accepted the ALP interest at LIBOR plus 2.5% in earlier years, he cannot deviate from the stand so taken and make ALP adjustments IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 now. For the fresh loans, however, he upheld the ALP adjustments made by the TPO. The ALP adjustment finally sustained thus was Rs 13,44,042. None of the parties is satisfied by the verdict so given by the DRP. The assessee is aggrieved of the ALP adjustments sustained by the DRP and the Assessing Officer is aggrieved of the relief granted by the DRP. Both the parties are in cross appeals before us.

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

99. We find that so far as corporate guarantee commission and interest on optionally convertible loans are concerned, these issues are covered by our decision earlier in this order for the assessment year 2009-10. We see no reasons to take any other view of the matter than the view so taken by us, and for the elaborate reasons set out earlier in this order, in assessee's own case. Respectfully following these views, we direct the Assessing Officer to delete these ALP adjustments. To that extent, grievance of the assessee is upheld and the grievance of the Assessing Officer is dismissed. As regards interest on loans to Zydus France, we find that the same loan, on the same terms, has been held to be at an arm's length in the earlier assessment years. As regards the action of the TPO in comparing this loan with not so safe loans to companies other than the companies rates AAA, AA or A, we find that, quite to the contrary, the judicial consensus should be in making comparison with relatively safer loans. While on this issue, we may usefully take note of the following observations made by a coordinate bench in the case of UFO Movues.

........it will be useful to take note of the fact that in the case of Bharti Airtel Limited Vs ACIT [(2014) 161 TTJ 283], and a coordinate bench had deleted a similar ALP adjustment on account of interest amounting to Rs 10,11,786 wherein the same approach of adopting 400 basis points above the LIBOR as ALP was adopted. While deleting this ALP adjustment, speaking through one of us, the Tribunal had, inter alia, observed as follows:

> 62. As far as the first adjustment is concerned, while the TPO has adopted the rate as 4% over LIBOR rate, he has not set out the specific basis of this rate. He has mentioned about some information gathered from websites of financial institutions which, according to him, states that, "for the foreign currency denominated term loans, the maximum rate of interest is 4% over 6 months LIBOR", and then proceeded to adopt this maximum interest rate as a fair basis for his computing the arm's length price. On the other hand, the assessee has taken two specific comparables of USD borrowings, i.e. L&T and Seri Infrastructure, on the interest rate of LIBOR + 150 bps and 1.4% to 1.7% band over LIBOR respectively. There is no material whatsoever, save and except for vague observations about weak financials of the subsidiaries - which are not supported by any specific facts and proceed on sweeping generalizations and assumptions, to reject the comparables taken by the assessee. When a Transfer Pricing Officer rejects comparables taken by the assessee, he has to set IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 out specific, cogent and legally sustainable reasons for doing so.

On this point, therefore, the stand of the Assessing Officer cannot be accepted.

....

....

65. That leaves us with third point of difference between the assessee and the TPO and that is with regard to adjustment of 177.60 points, as balancing figure, towards lack of security and lender not being in the business of borrowing and lending money. This adjustment is justified by the TPO on the following ground:

> 7.10 Adjustment between a banker and non-banker As the taxpayer is not in the business of lending and borrowing money, his risk is higher in advancing loan to a single customer than a bank, which spreads its risk among its various customers. Thus, the difference between banker and non-banker is to be kept in mind while arriving at the arm's length CUP rate based on bank rates.
>
> 7.11 Adjustment for security Usually, bankers extending loans in foreign currency also insist on sufficient security. In this case, no security is offered by the AE. Keeping in view the financial health of the subsidiary, it may not be in a position to offer security.

Thus an adjustment is required to be made for not offering a security. This may be computed as the difference between the interest rates prevailing for the bonds of equivalent credit rating of the AE and sovereign government bonds in the country in which the AE is located. This can also be considered as the guarantee cost payable to the taxpayer for giving guarantee for equivalent amount of loan given to the AE i.e. the rate differential for the difference in interest spread between the credit rating of the taxpayer and the AE. Thus after the above analysis, the equivalent interest rate is the interest rate including the transaction cost for a foreign currency loan, if given to the AE for its credit standing / rating.

66. We see no substance in this adjustment either. The TPO has taken the lender as the tested party, and yet made adjustments for higher risks on account of assumed lack of security and increased risk of single party dealing. This approach overlooks the fact that the assessee has advanced monies to its subsidiaries which are under its management and control- a factor which substantially reduces the risk rather than increasing IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 it. On these facts, it is difficult to understand, much less approve, any rationale for adjustment on account of higher risks. On this point also, we see no merits in the stand of the TPO.

(Emphasis, by underlining, supplied by us now)

8. When the matter was carried in further appeal, this time by the Commissioner, before Hon'ble Delhi High Court, Their Lordships were, vide judgment dated 25th February 2015- a copy of which was placed before us by the learned counsel, pleased to approve the reasoning adopted by the Tribunal. In doing so, Their Lordship observed as follows:

> 8. The ITAT has also taken note of the fact that two specific comparables of USD borrowings i.e. L&T and Seri Infrastructure, on the interest rate of Libor had been taken into consideration.

There is no material whatsoever, save and except for vague observations about weak financials of the subsidiaries - which are not supported by any specific facts and proceed on sweeping generalizations and assumptions, to reject the comparables taken by the assessee. When a Transfer Pricing Officer rejects comparables taken by the assessee, he has to set out specific, cogent and legally sustainable reasons for doing so. On this point, therefore, the stand of the Assessing Officer cannot be accepted.

9.................

10. The Tribunal further noticed that the assessee advanced monies to the subsidiaries which were under its management and control, which in fact substantially reduced the risk and in these circumstances there was no rationale of adjusting any amount of higher basis.

11. This Court is of the opinion that the reasoning of the ITAT on each of the heads which went into the adjustment of Rs 10,11786/- is reasonable and justified and does not call for any interference.

(Emphasis, by underlining, supplied by us)

9. That was also a case in which the lender parent company was taken as the tested party, the loan was advanced to a subsidiary company without much to the credit of its financial credentials and the loan was treated as a high risk loan resulting in adopting the maximum LIBOR rate on which dollar

loans were advanced. Yet, Hon'ble High Court specifically approved the Tribunals reasoning that the "assessee advanced monies to the subsidiaries which were under its management and control, which in fact substantially reduced the risk and in these circumstances there was no rationale of adjusting any amount of higher IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 basis". When such are the views of Their Lordships, it is futile to suggest that the loans advanced by the parents to subsidiary can indeed be taken as BB to D grade investments which refers to, as noted by the TPO himself at page 28 of the order, investments with serious risks of inadequate safety, investments of high risk, investments of substantial risk and investments of default

100. In view of the above discussions, as also bearing in mind entirety of the case, we approve the reasoning adopted by the DRP as also the conclusions arrived at by the DRP. The relief granted by the DRP regarding deletion of ALP adjustments in respect of loan to Zydus France is thus also confirmed.

101. In the result, while the first ground of appeal of the assessee is allowed, first and second grounds of appeal is the appeal of the Assessing Office is dismissed.

102. In second ground of appeal taken by the assessee, following grievance is raised:

> That the learned Assessing Officer erred in law and on facts in making a disallowance of Rs.11,23,95,002/- u/s 14A instead of Rs.6,46,64,270/- being the correct disallowance as per Rule 8D r.w.s. 14A of the I.T. Act, offered by the assessee in its Return of Income.

103. On this ground, the assessee has limited arguments pointing out some apparent mistakes in the conclusions arrived at by the Assessing Office, which have been approved by the DRP rather mechanically. An identical issue came up for our adjudication in the immediately preceding assessment year, and, by our directions earlier in the order, we have remitted the matter to the file of the Assessing Officer for fresh consideration to deal with the objections raised by the assessee. In the present year also, the assessee has pointed out somewhat similar objections by way of a rectification petition under section 154 which is stated to be pending even now. We deem it fit and proper to remit the matter to the file of the Assessing Officer for this assessment year also and direct the Assessing Officer to deal with the points made by the assessee in his rectification petition.

104. Ground no. 2 is thus allowed for statistical purposes.

105. In third ground of appeal taken by the assessee, the following grievance is raised:

> That the learned Assessing Officer erred in law and on facts in not allowing the credit for excess Dividend Distribution Tax of Rs.75.04.966/- paid u/s 115 'O' of the Act.

106. So far as this grievance of the assessee is concerned, as learned representatives fairly agree, the matter is required to be remitted to the file of the Assessing Officer with a direction to deal with the

matter by way of a speaking order and after giving a reasonable opportunity of hearing to the assessee, particularly in IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 view of the fact that this aspect of the matter has not been discussed at all at the assessment stage. We accept this plea. Accordingly, the matter stands restored to the file of the Assessing Officer with directions, as above.

107. Ground no. 3 is thus allowed for statistical purposes in the terms indicated above.

108. In ground no. 4, the assessee has raised the following grievance:

> That the learned Assessing Officer erred in law and on facts in not acknowledging in the Assessment Order, the availability of the amount of Carried Forward MAT Credit u/s 115JAA of Rs.27,19,89,591/-, to which the Appellant is lawfully entitled to in view of it being covered under the provisions of MAT u/s 115JB.

109. So far as this grievance of the assessee is concerned, short grievance of the assessee is that the Assessing Officer has not specifically mentioned that the assessee is entitled to carry forward the MAT credit of Rs 20,08,52,398. However, we are unable to see much merits in this plea because, as is the settled legal position in the view of Hon'ble Supreme Court's judgment in the case of CIT Vs Manmohan Das [(1966) 59 ITR 699 (SC)], in the year of carry forward only quantification of a set off claim is to be seen. The question as to its entitlement for being set off is to be examined in the year in which set off is claimed. Grievance of the assessee is premature and is dismissed as such.

110. Ground no. 4 is thus dismissed. No other grievances of the assessee, as learned representatives fairly agree, require any specific adjudication by us.

111. In the result the appeal of the assessee for the assessment year 2010-11 is party allowed in the terms indicated above.

112. We now take up the appeal filed by the Assessing Officer for the assessment year 2010-11.

113. In the process of dealing with assessee's cross appeal for the same assessment year, we have already dealt with and dismissed the first two grounds of appeal of the Assessing Officer.

114. Ground nos. 1 and 2 are thus dismissed.

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

> IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 The DRP has erred in deleting the addition of Rs.13,40,16,897/- made by the AO u/s. 40(a)(i) of the Act in respect of commission on export, legal and professional fees and clinical trial and analytical and testing charges.

116. The relevant material facts related to the above ground of appeal are as follows. During the course of scrutiny assessment proceedings, the Assessing Officer noted that the assessee has a made a number of payments without any deduction of tax at source. The matter was probed further and explanations of the assessee were called. Thereafter, the Assessing Officer proceeded to make the impugned disallowance by observing as follows:

> 3.3 A careful perusal of the assessee's submission revels that the assessee has considered only payments in the show cause notice dated 25/02/2014 which has been held by the ITO (Int. Taxation)-II, Ahmedabad as the payment covered u/s.195 of the Act. In fact, on verification of the submission of the assessee, it is found that the assessee company has made the following payments to non residents which attract Sec. 195 of the Act.

Sr.No.	Nature of payments	Am
1.	Commission	6,94,88
2.	Trade Mark	14,08,8
3.	Royalty	1,85,61
4.	Legal & Professional Fees	3,70,04
5.	Clinical Trials & Analytical & Testing Charges	4,68,04

> From the nature of payment as numerated above, it can be seen that such payments is clearly covered u/s. 195 of the Act. As such, during the course of the assessment proceedings, the assessee was categorically asked to explain why above mentioned payments should not be considered for disallowance u/s. 40(a)(i) of the Act. In response thereto, the assessee furnished its reply on 28/03/2014 along with information in respect of TDS made u/s.195 of the Act for above mentioned expenditure incurred in foreign currency and reasons for non-deductions of tax on other items on which the assessee did not make TDS, the same is asunder:-

ParticularsExpenditur Amount TDS Amount on Reason for Non-

	e Amount	on which tax deducted		which not deducted	deduct
	(Rs.)	(Rs.)	(Rs.)	(Rs.)	
Commission on Exports	69,488,308			69,488,308	Remittance of Com to Overseas Selli is not liable to in view of the fo - CBDT Circula dated 23/07/1969 Circular No.7 07/02/2000 - Decision of the Court in Toshoku ITR 525 (SC)

IT (TP) Nos.519 and 898/Ahd/2014

					- It is further pertinent to point out that the aforesaid CBDT Circulars were withdrawn only from 22/10/2009 by CBDT Circular No.7/2009 of even date.
Trade-mark	127,406,250			127,406,250	Remittances are towards outright Purchase of Trade-mark. Accordingly, no liability for TDS u/s 195 arises. Moreover, it has also been capitalised in the books of accounts. So, Disallowance u/s.40(a)(i) is not applicable.
Technical know how	13,482,000	13,482,000	1,348,200		Not Applicable since Tax Deducted
Royalty	18,561,602	18,561,602	2,390,102	-	Not Applicable since Tax Deducted
Legal & Professional Fees	37,004,592	19,280,817	1,937,270	17,723,775	RemittancesofRs.1,77,23,775/- are towards such Professional Consultancy Fees for Legal Services, paid to Non-Resident Individual or Firm, in the nature of Independent Personal Services, which are not liable to TDS u/s.195 in view of the clear language of the provisions of the applicable DTAA (Article 14 or 15, as the case may be) with the respective countries. In other cases, Tax has been deducted.
Clinical Trials & Analytical & Testing Charges	46,804,814			46,804,814	Remittances are mainly covered under the DTAA with USA, Canada, UK etc., where the clear language of 'Fees for Technical or Included Services' excludes such payments, where no Technology is made available by the non-resident party, to whom

such payment for Clinical Trials is made. Accordingly, no liability for TDS u/s.195 arises in such cases, as directly held by

IT (TP) Nos.519 and 898/Ahd
and 694 and 747/Ahd/
Assessment years: 2009-10 and 201

the AAR n its ruling case of Anapharm Inc. ITR 394 (AAR), as als direct decision of th Mumbai ITA in the cas Wockhardt Ltd taxmann.com 208 (Mum) on the issue of remit for Clinical Trials. rely on decision of C in our own case of AY 2008-09, where follow the aforesaid decision, our appeal been duly allowed.

Total 312,747,56 51,324,41 5,675,57 261,423,14

3.4 The submission of the assessee has been gone through carefully but the same is not acceptable for the following reasons:

(i) Commission on export:

As stated above, the assessee has made payment of commission of Rs.6,94,88,308/-without complying the provisions of Section 195 of the Act. Clause

(i) to Sub-Section (1) of Section 9 provides that all income accruing or arising whether directly or indirectly through from any business connection in India or through or from any property in India deemed to accrue in India. Explanation -1 to Section 9 further provides that in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operation carried out in India. The assessee company is manufacturer and trader of pharmaceuticals goods. All the manufacturing of the assessee company is carried out in India only and only certain part of the manufactured goods are exported outside India. As such, it cannot be said that all the business operation are not carried in India. As such, the submission of the assessee in this respect is rejected.

The Circular No.23 of 1969 and 786 of 2000 quoted by the assessee are not applicable to the facts of the assessee's case. Circular No.786 of 2000 quoted by the assessee it is stated that the relevant section namely section 5(2) and section 9 of the I.T. Act not having undergone any change in this regard, the clarification in Circular No.23 still prevails. Clause (a) of Explanation 1 to 9(1)(i) of the Act is modified w.e.f. 01/04/2004. Accordingly, the decision quoted by the in the case of CIT Vs. Toshoku Ltd. reported in 125 ITR 525 is also distinguishable to the facts of the assessee's case. Accordingly, the claim of commission expense of Rs.6,94,88,308/- is disallowed.

(ii) Legal & Professional fees The assessee has made payment of Rs.3,70,04,592/- being legal & professional fees paid to non-residents out of which the assessee has deducted tax on amount of Rs.1,92,80,817/-leaving an amount of Rs.1,77,23,775/- on which no IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 TDS has been made. The submission of the assessee for non-deduction of tax is that the payments have been made to non-resident individual or firm in the nature of independent personal services which are not liable to TDS u/s. 195 of the Act is not acceptable. Scope of income as provided in clause (b) oil Sub-section 2 of Section 5 of the Act states that the income accrues or arises or is deemed to accrue or arise to non-resident in India is taxable. Clause (b) of Sub-Section (2) of Section 5of the Act provides that the total income of any previous year of a person whey is non-resident includes all income whatever source derived which accrues or is deemed to accrue arise to him in India during the year. The assessee submission that Article-15 of DTAA with United States provides that payment for professional fees to non-resident is not chargeable in view of Article-15 of said DTAA is found to be devoid of any merit. For the purpose of income-tax, the professional services are defined as -

> "professional services" means services rendered by a person in the course of carrying on legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or advertising or such other profession as is notified" by the Board for the purposes of section 44AA or of this section. As such, the assessee's submission that the payment of professional charges paid to non-resident and TDS is not deductable is not accepted and the same is rejected, as the assessee is liable to deduct the tax u/s. 195 of the Act. It is also worthwhile to point out here that Article-25 of the DTAA provide that subject to the limitations of the law of the United States (as it may be amended from time to time without changing the general principle thereof), the United States shall allow to a resident or citizen of the United States as a credit against the United States tax on income, the income-tax paid to India by or on behalf of such citizen or resident. It is, therefore, very clear that whatever the tax deducted from the commission payment to the non-resident, they are getting the relief from US as per the DTAA. As such, such income not only arose in India but also same is earned by the non-resident in India. Clearly, therefore, the commission paid to the non-resident is accrued in India for the services rendered in India. In view of the above, the assessee ought to have complied the provisions of Section 195 of the Act while making the payment of legal & profession fees to non-resident. The assessee, thus, having failed to comply with the provisions of section 195 of the Act, the provisions of Section 40(a)(i) are applicable to such payments. Accordingly, the expenditure of Rs.1,77,23,775/- is not allowable to

the assessee, as such, the said expenditure is disallowed.

(iii) Clinical Trial & Analytical & Testing Charges of Rs.4,68,04,814/-.

(a) Clinical Trial Company made payments to above non residents towards. clinical trials of certain pharmaceutical molecules. Clinical Trials involves scientific knowledge and experience of the conducting person/firm or company with regard to administration of medicines to animals/human beings and keeping them under observation of Doctors/Scientists for reaction of medicines, and efficacy of said medicine in mitigating the disease/disorder for which it is intended to be used. It involves study of side effects/contra indications. All these observations are noted down systematically/chronologically and the effects of medicine are analyzed and submitted to the assessee company in the form of information consisting of observations, graphs, tables and suggestions by the said foreign research entity.

Therefore payments for clinical trials are fees for technical services as these services not only involve services of technical person, but also these services are ancillary and subsidiary to the application or enjoyment of information for which the payments are made.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

(b) Analytical studies for Bio Analysis:

Bio Analysis studies involve highly technical Analytical study of distribution of medicine the body of the animal/human being after administration of the same. This may involve study with time taken for distribution of medicine to the particulars organ of the body and amount/concentration of medicine reaching the organ and reaction of cell of the organ etc. This is also a highly technical study and covered by FTS. After the Analytical study the Research Institute submits a report giving the data and analysis of studies. All these data and analysis of studies submitted to the assessee company in the form of information consisting of observations, graphs, tables and suggestions by the said foreign research entity. Therefore payments for clinical trials are fees for technical services as these services not only involve services of technical person, but also these services are ancillary and subsidiary to the application or enjoyment of information for which the payments are made.

The assessee submitted that with regard to the "Bio-Analysis and Clinical Trials the language of the DTAA with USA, UK, Canada and Singapore, is clear with regard to 'fees for Technical Services' which exclude such payments when no technology is made available by the non-resident party, to whom such payment for Bio-Analysis is made.

Contention of the assessee is considered carefully. The arguments of the assessee are that the 'DTAA with regard to FTS excludes such payments' were no technology is made available by the non-resident. Article 12 reads as under :

ARTICLE 12-Royalties and fees for included services-1. Royalties and fees for included services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such royalties and fees for included services may also be taxed in the Contracting State in which they arise and according to the laws of that State; but if the beneficial owner of the royalties or fees for included services is a resident of the other Contracting State, the tax so charged shall not exceed :

(a) in the case of royalties referred to in sub-paragraph (a) of paragraph 3 and fees for included services as defined in this Article [other than services described in sub-paragraph (b) of this paragraph]:

```
        (i)        during the first five taxable years for which this
  Convention      has effect,

                       (a)     15 per cent of the gross amount of the royalties
```

or fees for included services as defined in this Article, where the payer of the royalties or fees is the Government of that Contracting State, a political sub-

division or a public sector company; and

(b) 20 per cent of the gross amount of the royalties or fees for included services in all other cases; and

(ii) during the subsequent years, 15 per cent of the gross amount of royalties or fees for included services; and IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

(b) - in the case of royalties referred to in sub-paragraph (b) of paragraph 3 and fees for included services as defined in this Article that are ancillary and subsidiary to the enjoyment of the property for which payment is received under paragraph 3(b) of this Article, 10 per cent of the gross amount of the royalties or fees for included services.

3. The term "royalties" as used in this Article means :

(a) payments of any kind received as a consideration for the use of, or the right to use, any copyright of a literary, artistic, or scientific work, including cinematograph films or work on film, tape or other means of reproduction for use in connection with radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience, including gains derived from the alienation of any such right or property which are contingent on the productivity, use, or disposition thereof; and

(b) payments of any kind received as consideration for the use of, or the right to use, any industrial, commercial, or scientific equipment, other than payments derived by an enterprise described in paragraph 1 of Article 8 (Shipping and Air Transport) from activities described in paragraph 2(c) or 3 of Article 8.

4. For purposes of this Article, "fees for included services" means payments of any kind to any person in consideration for the rendering of any technical or consultancy services (including through the provision of services of technical or other personnel) if such services :

(a) are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment described in paragraph 3 (a) of this article is received; or

b) make available technical knowledge, experience, skill, know-

how, or processes, or consist of the development and transfer of a technical plan or technical design.

UK Article 12

4. For the purposes of paragraph 2 of this Article, and subject to paragraph 5, of this Article, the term "fees for technical services" means payments of any kind of any person in consideration for the rendering of any technical or consultancy services (including the provision of services of a technical or other personnel) which:

(a) are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment described in paragraph 3(a) of this article is received ; or

(b) are ancillary and subsidiary to the enjoyment of the property for which a payment described in paragraph 3(b) of this Article is received; or IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

(c) make available technical knowledge, experience, skill know-

how or processes, or consist of the development and transfer of a technical plan or technical design.

CANADA Article 12

4. For the purposes of this Article, 'fees for Included services' means payments of any kind to any person in consideration for the rendering of any technical or consultancy services (including through the provision of services of technical or other personnel) if such services :

(a) are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment described in paragraph 3 is received; or

(b) make available technical knowledge, experience, skill, know-

how, or processes or consist of the development and transfer of a technical plan or technical design.

It may be seen from the clause 4 of the article, that definition of Fees for included services mean payment for rendering any technical consultancy service if such service are ancillary to the application of information. Therefore the payments for Clinical Trials and Bio Analysis studies clearly falls in Fees for included services and the assessee was liable to deduct tax from such payments. Therefore, the payments of Rs.4,68,04,814/- being clinical trials & analytical & testing charges made by the assessee company to non-residents without deducting the tax as required 195 is liable to be added u/s 40(a)(i) of the Act.

3.5 In view of the above, the commission expense of Rs.6,94,88,308/-, Legal & Professional charges of Rs.1,77,23,775/- and clinical trials & analytical & testing charges of Rs.4,68,04,814/- totalling Rs.13,40,16,897/- [69488308 + 17723775 + 46804814] are disallowed u/s. 40(a)(i) of the Act.

117. Aggrieved, assesse raised an objection before the DRP and the DRP, after an elaborate analysis of each of the point, deleted the said disallowance. The reasoning broadly taken by the DRP was this. It was held that in none of these cases, any income embedded in the payments was taxable in India. The DRP held that commission payments in the hands of non resident are not taxable in India to the extent, as is the admitted position in this case, all the related activities ae carried out outside India. So far as legal and professional fees was concerned, the DRP noted that the payments are made to law firms in UK, USA, Japan and France but none of these firms have fixed base in India and, as such, these independent personal services are not taxable in the respective treaty provisions. As regards, clinical trial, analytical and testing services are concerned, it was observed that the issue stands concluded, in favour of the assessee, by coordinate bench decision in the case of DCIT Vs Dr Reddy Laboratories Ltd [(2013) 35 taxmann.com 339 (Hyd)] and that there is nothing to even indicate that make available clause is satisfied so as to bring these services, rendered by non residents, to tax in India under the fees for technical services clause in the respective treaties. As there was no income in these IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 payments which could be brought tax in India, opined the DRP, there was no tax withholding requirement, and, as such, section 40(a)(ia) could not have been invoked. The Assessing Officer is aggrieved and is in appeal before us.

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

119. We find that so far as the taxability of commission payments made to non residents agents is concerned, the same stands concluded, in favour of the assessee, by a coordinate bench decision dated 3rd January 2017 in the case of DCIT Vs Welspun Corporation Ltd and vice versa. Respectfully following the said decision, we confirm findings of the CIT(A) on that point. As regards the payments to professional law firms and consultancy fees, there is no dispute that these professionals did not have any fixed base available to them in India, as is the condition precedent for taxing fees for independent personal services in India under the respective treaty provisions. As

regards the clinical and analytical testing charges, the issue stands covered in favour of the assessee in assessee's own case as also in the case of Reddy Laboratories (supra). Learned Departmental Representative has not pointed out any distinguishing features or disputed this position. In view of these discussions, as also bearing in mind entirety of the case, we approve the conclusions arrived at by the DRP and decline to interfere in the matter. As we do so we may also add that, for the sake of brevity, we are not adding reproductions from the orders relied upon by us and these orders will be deemed to be attached and forming part of this order.

120. Ground no. 3 is thus dismissed.

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

> The DRP has erred in considering Product Registration expenses of Rs.6,40,32,914/- as revenue expenditure when the same entitles the assessee to export the registered drugs to various countries for many years.

122. Learned representatives fairly agree that this issue is settled in favour of the assessee by decisions of the coordinate benches in assessee's own case, and Hon'ble High Court has declined to admit appeal against such decision, as in the esteemed views of Their Lordships, no question of law arises from these decisions. The relief granted to the assessee on this point in past has thus achieved finality. In this view of the matter, we approve the relief granted by the DRP on this point and decline to interfere in the matter.

123. Ground no. 4 is thus dismissed.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

124. In ground no.5, the Assessing Officer has raised the following grievance:

> The DRP has substantially erred in holding that Trademark Registration and Patent fee of Rs.5,58,47,781/- are revenue expenses when the same are classified as intangible assets u/s 32(1)(ii) of the Act.

125. Learned representatives fairly agree that this issue is also settled in favour of the assessee by decisions of the coordinate benches in assessee's own case, and Hon'ble High Court has declined to admit appeal against such decision, as in the esteemed views of Their Lordships, no question of law arises from these decisions. The relief granted to the assessee on this point in past has thus achieved finality. In this view of the matter, we approve the relief granted by the DRP on this point and decline to interfere in the matter.

126. Ground no. 5 is thus dismissed.

127. In ground no. 6, the Assessing Officer has raised the following grievance:

> The DRP has substantially erred in holding that the expenses amounting to Rs.21,03,15,537/- incurred outside the approved R&D facility is also eligible for weighted deduction in contravention of section 35(2AB) whereby only expenditure on in-house research and development facility qualifies for weighted deduction.

128. Learned representatives fairly agree that this issue is also settled in favour of the assessee by decisions of the coordinate benches in assessee's own case, and Hon'ble High Court has declined to admit appeal against such decision, as in the esteemed views of Their Lordships, no question of law arises from these decisions. The relief granted to the assessee on this point in past has thus achieved finality. In this view of the matter, we approve the relief granted by the DRP on this point and decline to interfere in the matter.

129. Ground no. 6 is thus dismissed.

130. In ground no. 7, the Assessing Officer has raised the following grievance:

> The DRP has erred in allowing depreciation of Rs.12,65,293/- on Hummer Car despite the fact that the same was in the name of the Director and there was no evidence to show that the same was used wholly and exclusively for the purpose of business. The provisions of section 32 were therefore not satisfied.

131. As far as this grievance of the Assessing Officer is concerned, there is no dispute that the car was not legally owned by the assessee company but by the director, even though the payment for acquisition of this car was made by the IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11 assessee company and the car is used by the company. The beneficial ownership thus rests with the assessee company. The depreciation was proposed to be declined by the Assessing Officer mainly on the ground that the assessee did not own the vehicle in question. However, the assessee succeeded in the DRP in his objection to this proposal. We have noted that the DRP has given a categorical finding to the effect that the car was used for the purpose of business and the Assessing Officer has himself allowed the running and maintenance expenses of this car. It has also been noted that the registration of car in the name of driver was a matter of convenience as it gave advantage to the assessee in terms of road tax. On these facts, as held by the DRP, the mere fact that the car was not legally owned by the assessee company- particularly when beneficial ownership of this vehicle is not even in dispute, the depreciation on car cannot be declined. Aggrieved, assessee is in appeal before us.

132. Having heard the rival contentions and having perused the material on record, we are not inclined to disturb very well reasoned findings of the DRP and the conclusions arrived at by the DRP. Once it is not in dispute that the vehicle was owned, in substance, by the assessee and the vehicle was used for the purposes of its business, there cannot be any legally sustainable reasons for declining the depreciation. Learned Departmental Representative could not bring on record any material to dislodge the findings of the DRP. We approve the action of the DRP and decline to interfere in the matter.

133. Ground no. 7 is thus dismissed.

134. In ground no. 8, the Assessing Officer has raised the following grievance:

> The DRP has erred in deleting the addition to Book Profit amounting to Rs.11,23,95,002/- being addition u/s. 14A despite the specific clause (f) to Explanation 1 of section 115JB.

135. As regards this grievances of the Assessing Officer, learned representatives fairly agree that the issue is covered, in favour of the assesse, by a coordinate bench in assessee's own case for the assessment year 2008-09, which in turn has followed the assessment years 2006-07 and 2007-08. As a matter of fact, all that the DRP has done is to follow the said order of the coordinate bench.

136. We see no infirmity in the relief so granted by the DRP. No arguments have been advanced before us to persuade us to take any other view of the matter than the view so taken by the coordinate bench which have been followed by the DRP in the impugned order. In this view of the matter, and respectfully following the coordinate bench decision, we confirm the relief granted by DRP and decline to interfere in the matter.

IT (TP) Nos.519 and 898/Ahd/2014 and 694 and 747/Ahd/2015 Assessment years: 2009-10 and 2010-11

137. Ground no. 8 is thus dismissed.

138. In the result, the appeal filed by the Assessing Officer for the assessment year 2010-11 is dismissed.

139. To sum up, while both the appeals of the assessee and the appeal of the Assessing Officer for the assessment year 2009-10 are partly allowed in the terms indicated above, the appeal of the Assessing Officer for the assessment year 2010- 11 is dismissed. Pronounced in the open court today on the 3rd day of March, 2017.

```
      Sd/-                                                                 Sd/-
S S Godara                                                           Pramod Kumar
(Judicial Member)                                               (Accountant Member)

Dated: 3rd day of March, 2017.

Copies to:   (1)    The appellant               (2)    The respondent
             (3)    Commissioner                (4)    CIT(A)
             (5)    Departmental Representative (6)    Guard File

                                                                                 By o

                                                                Assistant Registrar
                                                       Income Tax Appellate Tribunal
```

Ahmedabad benches, Ahmedabad