* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Reserved on: 03.10.2016
Pronounced on: 25.10.2016

\+ **ITA 350/2014**

MAGNETI MARELLI POWERTRAIN INDIA PVT. LTD.

……Appellant

Through: Sh. Ajay Vohra, Sr. Advocate with Sh. Neeraj Jain and Sh. Aditya Vohra, Advocates.

Versus

DEPUTY COMMISSIONER OF INCOME TAX ……..Respondent

Through: Sh. P. Roychaudhri, Sr. Standing Counsel with Ms. Vibhooti Malhotra, Jr. Standing Counsel.

CORAM:
HON'BLE MR. JUSTICE S. RAVINDRA BHAT
HON'BLE MS. JUSTICE DEEPA SHARMA

MR. JUSTICE S. RAVINDRA BHAT

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1. The assessee appeals, under Section 260-A of the Income Tax Act ("the Act" hereafter) against the decision of the Income Tax Appellate Tribunal (ITAT) for AY 2008-09 in respect of transfer pricing adjustments; more specifically, the remand by ITAT to the Transfer Pricing Officer (TPO) to segregate the payment of technical assessment fee and subject it to independent examination is under challenge. The following questions of law were framed:

> *1. Whether the Income Tax Appellate Tribunal was right in holding that royalty and technical assistance fee did not form part of a composite transaction and have to be treated as two separate transactions for the purpose of benchmarking and computing arms length price?*

2. Whether the Income Tax Appellate Tribunal was right in holding that Transactional Net Margin Method should not be applied for benchmarking/computing arm's length price in respect of transaction relating to "technical assistance fee"?

2. The assessee is a Joint Venture Company (JV) of M/s. Magneti Marelli Powertrain SPA, Italy, Maruti Suzuki India Ltd. and Suzuki Motor Corporation, Japan. It was incorporated in India to manufacture and sell Engine Control Units (ECUs). It reported six international transactions including "Payment of technical assistance fee" to the extent of ₹38,58,80,000/- This transaction alone is the subject matter of dispute; the TPO did not question the other five international transactions. The relevant facts for this transaction are that the assessee entered into agreement with its foreign Associated Enterprise (A.E.) for acquiring technology required for the purpose of manufacturing ECUs in respect of the following : -

"(1) Euro IV/75 HP 1.3 SDE/Suzuki Swift car application (2) Bharat III/75 HP 1.3 SDE/MS Swift application (3) Bharat III/75 HP 1.3 SDE/Tata Indica car application (4) Bharat III/75 HP 1.3 SDE/Fiat India Palio-Linea car application."

3. The assessee applied the Transactional Net Margin Method (TNMM) to benchmark its international transactions of import of raw materials, sub-assemblies and components, payment of technical assistance fees, payment of royalty, payment of software and purchase of fixed assets. All these were categorized under one broad head, viz. "Manufacturing of automotive components". The ratio of the assessee's `projected' operating profit margin to the operating revenue at 18.78% was compared with the mean operating profit margin at 6.65% of comparables taken on the basis of past three years'

data of Magneti Marelli Powertrain India Pvt. Ltd. The assessee, on the basis of its analysis claimed that its international transactions under the broad head (which included `Payment of technical assistance fee') were the Arm's Length Price (ALP). This was rejected by the TPO who held that the Transactional Net Margin Method ("TNMM") had to be applied separately for each international transaction and not collectively as done by the assessee. He, therefore, held all international transactions could not be ALP merely because the overall operating profit was more than the comparables. The TPO consequently rejected the assessee's `entity level approach' applied by it to benchmark its international transactions which included `Technical assistance fees' of ₹ 38.58 crores. According to the TPO, the Comparable Uncontrolled Price (CUP) method was more apt and had to be applied. The assessee's TNMM was consequently rejected and the CUP method was adopted. Accordingly, ALP of this transaction was determined. The assessee was unsuccessful before the Dispute Resolution Panel (DRP). In the final order passed under Section 144C(13), the A.O added the amounts towards income. The assessee was aggrieved against such addition and appealed to ITAT.

4. The ITAT firstly held that merely because the assessee capitalized the amount (₹ 38.58 crores) in the year and claimed depreciation on it, did not take the transaction outside the ambit of `international transaction'. That the assessee incurred liability for the said amount and did acquire technical assistance in the financial year relevant to the assessment year under consideration in respect of ECUs to be manufactured distinctly for the four different car makes and their application was not disputed. Therefore, the character of international transaction was- according to ITAT, left intact. The

assessee did not dispute this aspect. The ITAT, therefore, held that:

> *"6. It is seen that the assessee clubbed transactions of import of raw material, sub-assembles and components, payment of technical assistance fees, payment of royalty, payment of software and purchase of fixed assets under one segment of 'Manufacturing of the automotive components' and analyzed all such transactions on a combined basis. This type of combined benchmarking of all the international transactions is not in accordance with law. The mere fact that the overall profit earned by the assessee is more, would not ipso facto lead to the interference then all the international transactions are at ALP. The Special Bench of the Tribunal in the case of LG Electronics India Pvt. Ltd. Vs ACIT 2013 140 ITD 41 (Delhi) (SB) has held to this extent. Thus, the approach so adopted by the assessee in combining so many international transaction for determining ALP on a consolidated basis, is incorrect.*
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> *7. The next major flaw in the assessee's calculation is that it took into consideration the 'Projected operating profit margin' to show that its international transaction for the current year was at ALP. The requirement under the relevant provisions of the Act along with the rules is to consider the `actual' figures and not any `projected' figures. It is beyond our comprehension as to how the projected figures can be substituted for the actuals when the requirement is to benchmark actual international transactions at ALP. We, therefore, do not approve the methodology adopted by the assessee in this regard.*
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> *8. It is further seen that the assessee showed mean operating margin of certain comparables at 6.65% on the basis of past three years data. We do not approve this kind of approach adopted by the assessee for the obvious reason that Rule 10B(4) provides that the data to be used in analyzing the comparability of an uncontrolled transaction with an international transaction shall be the data relating to the financial year in which the international transaction has been entered into. Proviso of this rule for use of multiple year data is only an exception and not a rule, which can be invoked if the data for the current year does*

not result into the determination of correct prices. Nothing of the sort has been shown as to why the data of the comparables for the current year was not appropriate. We, therefore, reject this point of view canvassed by the assessee in making comparability.

9. We further observe that the approach adopted by the TPO is also not correct. He rejected TNMM as applied by the assessee by holding that CUP method was applicable. However, he computed the ALP of such transaction under CUP as Nil. There is no dispute on the fact that the assessee did receive technical information in respect of ECUs to be manufactured by it for four different models of cars pertaining to Maruti, Fiat and Tata. When technical information was admittedly obtained, it could not be said that the assessee ought not to have paid any consideration for that to its A.E. The TPO seems to have gone wrong by considering that the foreign A.E contributed capital to the tune of Rs. 20 crores and odd and took away a sum of Rs. 38 crores and odd in the shape of fees for technical services. This type of comparison made by the TPO for determining that the ALP of the international transaction of payment of technical fee at Nil, has no legal legs to stand on. When he resorted to the application of CUP method, it was incumbent upon him to ask the assessee for the submission of details of some comparable uncontrolled transactions. There is no reference to the asking or supplying of any such information by the assessee in the first instance, or the TPO thereafter venturing to find out such comparables at his own. What is required under the CUP method is to compare the price paid with certain uncontrolled comparable transaction to analyze if the price paid in an international transaction is at ALP. Nothing of the sort has been done by the TPO to make comparison of any comparable case with that of the assessee. He simply proceeded to adopt nil value of as ALP of the international transaction of payment of technical fee and proposed addition for the full amount. In our considered opinion, when the assessee did receive technical information and earned income by using the same, it cannot be said that it has ALP at nil. Some sort of comparison is inevitable under this method, unless it is shown that the assessee did not get

any advantage at all by making payment to its AE.

10. Thus it is seen that neither the assessee followed correct methodology for determination of ALP of this international transaction, nor the TPO/DRP applied the CUP method for determination of ALP in correct perspective. In such a situation, the order passed by the A.O making addition proposed by the TPO, cannot be upheld. In our considered opinion, the ends of justice would meet adequately if the impugned order on this issue is set aside and the matter is restored to the file of AO/TPO for a fresh determination of ALP of this international transaction. We order accordingly. The ld. AR has agreed to assist the TPO in providing data of certain comparable cases which could assist in the determination of ALP. In such fresh proceedings, the TPO will ascertain as to which method can be correctly applied and then decide the question before him. Needless to say, a reasonable opportunity of being heard will be given to the assessee."

5. Mr. Ajay Vohra, learned senior counsel urges that under Section 92C(1) and (3), Parliament intended that in such matters the method most appropriate *"having regard to the nature of transaction or class of transactions or class of associated persons or functions"* is to be viewed. Therefore, it is not open to the TPO/AO to segregate a set of transactions from a series or class of transactions, while carrying out the benchmarking exercise to arrive at the Profit Loss Indicator (PLI). It is urged in this regard that the ITAT's decision, rejecting the assessee's contention that under TNMM, various components of payments and expenses could be aggregated together is in error of law.

6. Learned senior counsel relies on *Sony Ericsson Mobile Communications India (P) Ltd v Commissioner of Income Tax* (2015) 374 ITR 118 (Del), a decision of a Bench of this Court, which reviewed the

methodology that TPOs are to adopt while determining ALP. The said judgment held, *inter alia*, that:

> *"The use of the expression "class of transaction", "functions performed by the parties" in section 92C(1) illustrates to the contrary, that the word "transaction" can never include and would exclude bundle or group of connected transactions. More important would be reference to the meaning of the term "transaction" in section 92F, clause (v), which as per the said definition includes an arrangement or understanding or action in concert whether or not the same is formal or in writing, whether or not it is intended to be enforceable by legal proceedings. Rule 10A in clause (d) states that "for the purpose of this rule and rules 10AB and 10E", the term "transaction" would "include a number of closely linked transactions". This rule in positive terms declares that the legislative intent is not to deviate from the generic rule that singular includes plural. The meaning or definition of the expression "transaction" in clause (d) of rule 10A read with sub-section (1) of section 92C, therefore, does not bar or prohibit clubbing of closely connected or intertwined or continuous transactions. This is discernible also from sub-rule (2) of rule 10B quoted above. The sub-rule refers to "services provided", "functions performed", "contractual terms (whether or not such terms are formal or in writing) of the transactions" which lay down explicitly or impliedly the responsibilities, risks and benefits to be divided between the respective parties to the transactions. The use of plurality by way of necessity and legislative mandate is evident in the said rule.*
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> *81. Similarly, sub-rule (3) of rule 10B refers to transactions being compared or comparison of the enterprises entering into such transactions likely to affect the price or cost charged, etc. A reading of rule 10C reassures and affirms that the general principle of plurality is not abandoned or discarded.*
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> *91. In case the tested party is engaged in single line of*

business, there is no bar or prohibition from applying the TNM method on entity level basis. The focus of this method is on the net profit amount in proportion to the appropriate base or the PLI. In fact, when transactions are interconnected, combined consideration may be the most reliable means of determining the arm's length price. There are often situations where closely linked and connected transactions cannot be evaluated adequately on separate basis. Segmentation may be mandated when controlled bundled transactions cannot be adequately compared on an aggregate basis. Thus, the taxpayer can aggregate the controlled transactions if the transactions meet the specified common portfolio or package parameters. For complex entities or where one of the entities is not "plain vanilla distributor", it should be applied when necessary and applicable comparables on functional analysis, with or without adjustments are available. Otherwise, the TNM method should not be adopted or applied on account of being an inappropriate method.

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137. The question of aggregation and disaggregation of transactions when the TNM Method or even in other methods is sought to be applied, must have reference to the strength and weaknesses of the TNM Method or the applicable method. Aggregation of transactions is desirable and not merely permissible, if the nature of transaction(s) taken as a whole is so inter-related that it will be more reliable means of determining the arm's length consideration for the controlled transactions. There are often situations where separate transactions are intertwined and linked or are continuous that they cannot be evaluated adequately on separate basis. Secondly, the controlled transaction should ordinarily be based on the transaction actually undertaken by the AEs as has been struck by them. We should not be considered as advocating a broad-brush approach but, a detailed scrutinized ascertainment and determination whether or not the aggregation or segregation of transactions would be appropriate and proper while applying the particular Method, is necessary.

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147. Tax authorities examine a related and associated parties' transaction as actually undertaken and structured by the parties. Normally, tax authorities cannot disregard the actual transaction or substitute the same for another transaction as per their perception. Restructuring of legitimate business transaction would be an arbitrary exercise. This legal position stands affirmed in EKL Appliances Ltd. (supra). The decision accepts two exceptions to the said rule. The first being where the economic substance of the transaction differs from its form. In such cases, the tax authorities may disregard the parties' characterisation of the transaction and re-characterise the same in accordance with its substance. The Tribunal has not invoked the said exception, but the second exception, i.e. when the form and substance of the transaction are the same, but the arrangements made in relation to the transaction, when viewed in their totality, differ from those which would have been adopted by the independent enterprise behaving in a commercially rational manner. The second exception also mandates that actual structure should practically impede the tax authorities from determining an appropriate transfer price. The majority judgment does not record the second condition and holds that in their considered opinion, the second exception governs the instant situation as per which, the form and substance of the transaction were the same but the arrangements made in relation to a transaction, when viewed in their totality, differ from those which would have been adopted by an independent enterprise behaving in a commercially rational manner. The aforesaid observations were recorded in the light of the fact in the case of L.G. Electronics (supra). Commenting on the factual matrix of L.G. Electronics case (supra) would be beyond our domain; however, we do not find any factual finding to this effect by the TPO or the Tribunal in any of the present cases. However, in L.G.Electronics decision (supra), it is observed that if the AMP expenses and when such expenses are beyond the bright line, the transaction viewed in their totality would differ from one which

would have been adopted by an independent enterprise behaving in a commercially rational manner. No reason or ground for holding or the ratio, is indicated or stated. There is no material or justification to hold that no independent party would incur the AMP expenses beyond the bright line AMP expenses. Free market conditions would indicate and suggest that an independent third party would be willing to incur heavy and substantial AMP expenses, if he presumes this is beneficial, and he is adequately compensated. The compensation or the rate of return would depend upon whether it is a case of long-term or short-term association and market conditions, turnover and ironically international or worldwide brand value of the intangibles by the third party."

8. It is urged that international commercial transactions cannot be looked into by tax authorities in a manner so as to place themselves in the position of businessmen. If in a given case, seemingly different transactions are placed together, because of purely commercial compulsions, the autonomy in the decision making of the tax payer should not be lightly disturbed as it would strike at the root of economic viability of the concern. Mr. Vohra here submitted that the purpose of making technical fee payments was to obtain access to technology and services that went to the establishment of the unit. Royalty was a recurring payment, in accordance with the agreement; however technical service charges were not recurring annual payments. Without agreeing to this payout, the assessee would not have been able to secure access to the entire repertoire of products and services that it eventually used to manufacture the car models in question. The law being flexible on the issue, de-segregation or separation of the said fee component and subjecting it to separate examination was not justified. On the second question, it was argued that the findings of the TPO were erroneous and

inconsistent. Having upheld the deployment of the TNMM, it was not open to use the CUP method for only one part of the transaction, i.e the one payment for technology.

9. Ms. Vibhuti Malhotra, counsel for the revenue, refuted the assessee's submissions. She urged firstly that *Sony Ericsson (supra)* does not stipulate any invariable rule with respect to aggregation or desegregation of transactions. Rather, it merely endorsed the view that aggregation is desirable. It was argued that while the commercial decision- making and choices of an entity are to be largely left intact, this court recognized that in ALP determination, it is essential that there are two exceptions to the principle:

(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.

10. Learned counsel argued that the TPO in this case had noticed that the payment for 'technical assistance fees was not benchmarked; the assessee's explanation that this was necessary, was rejected and it was concluded that the cost- benefit analysis provided did not explain why such a large amount was paid to the AE, when royalty was separately paid. Counsel argued that more importantly, the TPO noticed that large sums of money were paid towards travel expenditure of the AE's personnel, which was not explained. The inadequacy of the assessee's explanation led to the addition. Counsel contended that though the TPO's rejection of the TNMM was erroneous, that

aspect was corrected. Still, the benchmarking needed for the technical fee had to be undertaken. Counsel relied on *Denso India Limited v. Additional Commissioner Income Tax* (ITA No. 443/2013 and ITA No. 451/2013) to say that whether to permit aggregation or desegregate bundled transactions is entirely dependent on facts of each case. On the second question, it was submitted that the ITAT left it to the AO to determine the most appropriate method to benchmark the transaction, i.e. the payment and that this finding does not call for interference.

Analysis and Conclusions

11. Sections 92-A to 92-E were introduced into the Income Tax Act, to address a gap, i.e the evaluation of true income, which transnational entities strive to locate within a more friendly tax regime, as opposed to where they are in reality to be subjected to assessment. The Income Tax Rules were also appropriately amended to give effect to this Parliamentary intent. Broadly, the Act and rules posit the disclosure of various international transactions by domestic tax-payers to their "Associated Enterprises" (AE) with which they have disclosed nexus. The methodology indicated by law for identification of amounts, which otherwise would be income, but are shown as some form of payment, to the AEs, is the "Arm's Length Price" (or ALP) determination, where the particular business of the enterprise taxed is taken into consideration. Rule 10-B which is relevant, reads as follows:

> *"10B. (1) For the purposes of sub-section (2) of section 92C, the arm's length price in relation to an international transaction or a specified domestic transaction shall be determined by any of the following methods, being the most appropriate method, in the following manner, namely :—*

(a) comparable uncontrolled price method, by which,—
(i) the price charged or paid for property transferred or services provided in a comparable uncontrolled transaction, or a number of such transactions, is identified;
(ii) such price is adjusted to account for differences, if any, between the international transaction or the specified domestic transaction and the comparable uncontrolled transactions or between the enterprises entering into such transactions, which could materially affect the price in the open market;
(iii) the adjusted price arrived at under sub-clause (ii) is taken to be an arm's length price in respect of the property transferred or services provided in the international transaction or the specified domestic transaction;

(b) resale price method, by which,—
(i) the price at which property purchased or services obtained by the enterprise from an associated enterprise is resold or are provided to an unrelated enterprise, is identified;
(ii) such resale price is reduced by the amount of a normal gross profit margin accruing to the enterprise or to an unrelated enterprise from the purchase and resale of the same or similar property or from obtaining and providing the same or similar services, in a comparable uncontrolled transaction, or a number of such transactions;
(iii) the price so arrived at is further reduced by the expenses incurred by the enterprise in connection with the purchase of property or obtaining of services;
(iv) the price so arrived at is adjusted to take into account the functional and other differences, including differences in accounting practices, if any, between the international transaction or the specified domestic transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of gross profit margin in the open market;
(v) the adjusted price arrived at under sub-clause (iv) is taken to be an arm's length price in respect of the purchase of the

property or obtaining of the services by the enterprise from the associated enterprise;

(c) cost plus method, by which,—
(i) the direct and indirect costs of production incurred by the enterprise in respect of property transferred or services provided to an associated enterprise, are determined;
(ii) the amount of a normal gross profit mark-up to such costs (computed according to the same accounting norms) arising from the transfer or provision of the same or similar property or services by the enterprise, or by an unrelated enterprise, in a comparable uncontrolled transaction, or a number of such transactions, is determined;
(iii) the normal gross profit mark-up referred to in subclause (ii) is adjusted to take into account the functional and other differences, if any, between the international transaction or the specified domestic transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect such profit mark-up in the open market;
(iv) the costs referred to in sub-clause (i) are increased by the adjusted profit mark-up arrived at under subclause (iii);
(v) the sum so arrived at is taken to be an arm's length price in relation to the supply of the property or provision of services by the enterprise;

(d) profit split method, which may be applicable mainly in international transactions or specified domestic transactions involving transfer of unique intangibles or in multiple international transactions or specified domestic transactions which are so interrelated that they cannot be evaluated separately for the purpose of determining the arm's length price of any one transaction, by which—
(i) the combined net profit of the associated enterprises arising from the international transaction or the specified domestic transaction in which they are engaged, is determined;
(ii) the relative contribution made by each of the associated enterprises to the earning of such combined net profit, is then

evaluated on the basis of the functions performed, assets employed or to be employed and risks assumed by each enterprise and on the basis of reliable external market data which indicates how such contribution would be evaluated by unrelated enterprises performing comparable functions in similar circumstances;

(iii) the combined net profit is then split amongst the enterprises in proportion to their relative contributions, as evaluated under sub-clause (ii);

(iv) the profit thus apportioned to the assessee is taken into account to arrive at an arm's length price in relation to the international transaction or the specified domestic transaction:

Provided that the combined net profit referred to in sub-clause (i) may, in the first instance, be partially allocated to each enterprise so as to provide it with a basic return appropriate for the type of international transaction or specified domestic transaction in which it is engaged, with reference to market returns achieved for similar types of transactions by independent enterprises, and thereafter, the residual net profit remaining after such allocation may be split amongst the enterprises in proportion to their relative contribution in the manner specified under sub-clauses (ii) and (iii), and in such a case the aggregate of the net profit allocated to the enterprise in the first instance together with the residual net profit apportioned to that enterprise on the basis of its relative contribution shall be taken to be the net profit arising to that enterprise from the international transaction or the specified domestic transaction ;

(e) transactional net margin method, by which,—

(i) the net profit margin realised by the enterprise from an international transaction or a specified domestic transaction entered into with an associated enterprise is computed in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise or having regard to any other relevant base;

(ii) the net profit margin realised by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction

or a number of such transactions is computed having regard to the same base;

(iii) the net profit margin referred to in sub-clause (ii) arising in comparable uncontrolled transactions is adjusted to take into account the differences, if any, between the international transaction or the specified domestic transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of net profit margin in the open market;

(iv) the net profit margin realised by the enterprise and referred to in sub-clause (i) is established to be the same as the net profit margin referred to in subclause (iii);

(v) the net profit margin thus established is then taken into account to arrive at an arm's length price in relation to the international transaction or the specified domestic transaction;

(f) any other method as provided in rule 10AB."

12. In short, the relevant provisions, i.e Sections 92, 92-C, 92-D and 92-E read together with Rule 10-B and 10-D indicate the approach of the TPO tasked with the obligation to discern, if in a given set of circumstances, the assessee has disclosed international transactions, as well as an ALP. The assessee has to –each year that international transactions are entered into with AE, file transfer pricing reports. These TP reports should be factually correct; and the assessee has to satisfy the queries of the TPO. Section 92-C underlines that the method appropriate to the transaction, amongst the four specified ones, is to be applied. In the judgment of this court, reported as *Commissioner of Income Tax v. EKL Appliances Ltd.* (2012) 345 ITR 241 (Del), it was held as follows:

"It is very imperative on the part of the assessee, to establish before the TPO, that the payments made were commensurate to the volume and quality of services and such costs are

comparable. No such efforts was made. No ALP was computed by the assessee. As held by the Assessing Officer, as well as the Commissioner (Appeals), the assessee has not furnished personnel have rendered marketing services to the assessee company. In fact, the assessee company has no revenue which has been derived as a result of these marketing expenses. At the cost of repetition, we state that in the TP report, the company's submission is recorded at Page-30, and it states that the software services obtained by the Deloitte from the third party, are not similar to the services obtained by the Deloitte from the assessee company on account of requirements of different skill, experience, knowledge level, complexity of software projects handled, risk bearing capacity, etc. The entire revenue of the assessee are from the Deloitte. The evidence filed in support of the fact that services are rendered in the form of e-mails show that they are not e-mails relating to marketing, but that they relate only to billing. As rightly pointed out by the learned Departmental Representative, the assessee has no role in interacting with the client to modify, cancel, renew or extend the contract. The assessee cannot, even after expiry of the agreement between the Deloitte and its client, supply services without written consent of Deloitte. Deloitte has to pay the assessee irrespective of it getting payment or not within sixty days of raising invoices. Deloitte is responsible for generation of sales management, delivery of projects, maintaining customer relationship and billing and collection. The assessee has no market risk. The argument of the learned Counsel for the assessee that these three marketing personnel project the capabilities of the assessee company so that Deloitte gets work, is not supported by any evidence and, hence, without basis. In our view, under similar circumstances a uncontrolled comparable company would not incur such expenditure. Hence, the ALP is rightly determined at "nil". As no expenditure would have been incurred, there is no necessity to apply a particular method to arrive at such conclusion. In fact, by all the five methods or any one of them, when applied to the fact that there is no necessity of payment, the result of "nil" ALP will come."

13. *Sony Ericsson Mobile* is a later decision by another Bench of this Court, which reviewed the methodology that TPOs are to adopt while determining ALP. There are observations, undoubtedly, in that judgment indicating that aggregation of various payments and outgoings is permissible under the Act and the rules. At the same time, *Denso India (supra)* – while endorsing that view- also stated that whether to permit aggregation or not is a fact dependent decision, driven by the materials in any given case.

14. The assessee/appellant during 2008-09 entered into four License & Technology Assistance Agreements (LTAAs) with its overseas AE for four products for obtaining ECU technology. In return for the technical know-how, the assessee agreed to compensate the AE through a fee amounting to US $ 2 million for each LTAA (total US$ 8 million equivalent to over ₹ 38 crores) on installment basis. It explained that the overseas AE provides crucial and pivotal support to the assessee in carrying out its business in India by providing access to patented products and technology developed by it. The assessee argued that without receiving such technology/technical know-how/ information/assistance from the overseas AE, the assessee would not be able to conduct/carry out manufacturing and sales of ECUs in India at all. The assessee strengthened this contention by saying that it earned revenue of ₹ 42.23 crores from the sale of ECUs using the above mentioned technical know-how as a result of payment of ₹ 38.59 crores during FY 2008-09. Further, the assessee also earned aggregate revenue of ₹ 174.89 crores during a period of 3 consecutive years (i.e. FY 2008-09, FY 2009-10 and FY 2010-11) against a total payment of US $ 8,000,000, equivalent to ₹ 38.59 crores paid in FY 2008-09. During the transfer price proceedings, the

assessee was unable to substantiate the need for payment of technical assistance fees to its foreign AE. The TPO has observed that the assessee tried to establish its case for the arm's length nature of the transaction by stating that it gained in the form of higher sales. The TPO observed that neither any cost benefit analysis nor any benchmarking exercise was undertaken at the time of entering into the agreement. The TPO's rejection of the TNMM method at entity level was undoubtedly not correct. That, however, would not conclude the issue.

15. The assessee's argument that the technology itself would not have been given to it, but for the substantial fee (paid over and above the royalty payable), in the opinion of this court, requires a closer scrutiny. The initial burden is always upon the assessee to prove that the international transaction was at Arm's Length. Its TP report necessarily had to draw a comparison with other entities (maybe competitors) to show the general degree of profitability of the venture in question. The lower authorities quite correctly turned down the method of explaining the justification of the technical fee- with "proof" of its necessity by relying on profits. Undoubtedly the assessee was obliged to make the payment and that obligation arose from the agreements, a pre-incorporation binding contract. However, that such contractual obligation existed cannot *ipso facto* be the end of the enquiry. ALP determination in respect of every payment that is part of an international transaction is to be conducted irrespective of such obligation undertaken by the parties. If the transactions are, in the opinion of the TPO, not at arm's length, the required adjustment has to be made, as provided in the Act, irrespective of the fact that the expenditure is allowable under other provisions of the Act. There can conceivably be various reasons not to

subject such payments, such as for instance, if no similar data exists at all; or that sectional data for such payments is absent. Quite possibly, this may also be a general pattern of expenditure which AEs may insist to part with technology; further, similarly, other models of payment- deferred or lump sum, along with royalty or inclusive of it, may be discerned in comparable transactions. However, to say that such a substantial amount had to necessarily be paid and that it was a commercial decision, dictated by need for the technology, in the light of a specific query, it could not be said by the assessee that later profits justified it, or that has essentiality precluded the scrutiny.

16. In the light of the above discussion, this court holds that the explanation by the assessee that the payment of ₹ 38.58 crores in the circumstances was correctly not accepted. The first question is answered against the assessee. The remit directed by the impugned order is, therefore, upheld.

17. As far as the second question is concerned, the TPO accepted TNMM applied by the assessee, as the most appropriate method in respect of all the international transactions including payment of royalty. The TPO, however, disputed application of TNMM as the most appropriate method for the payment of technical assistance fee of ₹ 38,58,80,000 only for which Comparable Uncontrolled Price ("CUP") method was sought to be applied. Here, this court concurs with the assessee that having accepted the TNMM as the most appropriate, it was not open to the TPO to subject only one element, i.e payment of technical assistance fee, to an entirely different (CUP) method. The adoption of a method as the most appropriate one assures the applicability of one standard or criteria to judge an international

transaction by. Each method is a package in itself, as it were, containing the necessary elements that are to be used as filters to judge the soundness of the international transaction in an ALP fixing exercise. If this were to be disturbed, the end result would be distorted and within one ALP determination for a year, two or even five methods can be adopted. This would spell chaos and be detrimental to the interests of both the assessee and the revenue. The second question is, therefore, answered in favour of the assessee; the TNMM had to be applied by the TPO/AO in respect of the technical fee payment too.

18. In view of the above conclusions, the appeal has to fail; subject to the findings and observations regarding applicability of TNMM, it is dismissed.

S. RAVINDRA BHAT
(JUDGE)

DEEPA SHARMA
(JUDGE)

OCTOBER 25, 2016