IN THE HIGH COURT OF DELHI

ITA No.39/2010
ITA No.40/2010
ITA No.120/2010

COMMISSIONER OF INCOME TAX

Vs

M/s SAMSUNG INDIA ELECTRONICS LTD

A K Sikri And M L Mehta, JJ

Dated: April 20, 2011

Revenue's appeal dismissed

JUDGEMENT

Per: A K Sikri:

1. In these three appeals, though various questions of law are proposed, when these appeals came up for preliminary hearing on 11th January, 2011, notice was issued limited to one question only, which is common to all these appeals and reads as under:-

"A. Whether in the facts and circumstances of the present case, Ld. ITAT has erred in upholding the Order of CIT(A) in deleting the addition made by the A.O. under Section 40A(2)(b)."

It is for this reason that we have heard learned counsels for the parties only on the aforesaid question of law.

2. The assessee is a company jointly promoted by Samsung Electronics Company (SEC), Korea and its Indian associates. M/s Samsung Electronics Company, Korea is a trans-national or multinational company having its headquarters in Korea which works and operates in several parts of the world. It is a registered owner of the brand name and logo 'Samsung' and produces consumer durable and other white goods like television, washing machine, refrigerator, etc., under the brand name of 'Samsung'. SEC has 74% of equity in the assessee company and remaining 26 % of the equity are held and controlled by its Indian partner and associates. As per agreements entered into between SEC, Korea and the assessee, the SEC has granted a non-exclusive and non-transferable license to the assessee to use the technical information to produce the products at the facility of the assessee company in India for sale in Indian as well as international markets. The aforesaid rights were granted with certain conditions and it is not necessary to set out the same as far as these appeals are concerned.

3. We may, however, mention that apart from controlling stake of 74% in the form of equity of the assessee, the SEC has also obtained overriding and non-rectifiable

rights to nominate 5 out of every 7 directors in the assessee company. In addition, even the Managing Director to be appointed by the Board of Directors in the assessee company is designated by SEC, Korea. It is not in dispute that SEC, Korea, infact holds control and supervision on the functioning of the assessee company.

4. For the manufacturing of various products, the assessee company has been importing raw material from its parent company, i.e., SEC, Korea. In the assessment year 2000-2001 such raw material which was imported was to the tune of `131,27,62,956/-. Figures for other years are also of almost same magnitude. Keeping in view the controlling hand of the assessee company, the Assessing Officer was of the opinion that SEC, Korea was a person specified under Section 40A(2)(b) of the Income Tax Act (hereinafter, referred to as 'the Act'). Further he went into the issue as to whether the price on which the raw material was imported was arm's length price or it was an exclusive price paid by the assessee to its parent company.

5. The Assessing Officer asked the assessee to justify the rights on which various kinds of raw materials for production of different goods were imported. The explanation of the assessee company was that the raw materials were procured from SEC, Korea because the same were the best possible material available in the market and at the most competitive rates. It was also submitted by the assessee that the prices procured by it for importing of these very raw materials had been accepted by the customs authorities after appropriate verification. The assessee had even produced order, in original, passed by the custom authorities satisfying itself that the prices of various materials were at arm's length. It was also explained by the assessee that the custom authorities had infact referred the matter to Special Valuation Bench (hereinafter, referred to 'SVB') before accepting the reasonableness of the prices declared by the assessee for the import of the aforesaid raw materials. Additionally, it was submitted that purchases from SEC, Korea had been made at prices which were matching with the prices charged universally.

6. The Assessing Officer was not satisfied with this explanation rendered by the assessee. According to him, the claim of the assessee was very general in nature and no documentary evidence was produced to corroborate the same. The Assessing Officer was of the view that it was a standard practice used by multinational businesses to set up its subsidiaries in the other countries with the intention of making progress, and therefore, the prices on which the raw material were supplied to the assessee must be exclusive. He, thus, disallowed 2% of the aforesaid purchase price treating the same to be exclusive and made addition to that extent in the income of the assessee.

7. Feeling aggrieved by the aforesaid addition made by the Assessing Officer, the assessee preferred an appeal before the Commissioner of Income Tax (Appeals) [hereinafter, referred to as 'CIT(A)']. In these appeals, the assessee succeeded. The CIT(A) held that there was no basis or justification for invoking the provision of Section 40A(2) of the Act inasmuch as the imports were made at a reasonable price and there was no material before the Assessing Officer on the basis of which he could confirm the opinion that the same were excessive. The orders of the CIT(A) has been upheld by the Income Tax Appellate Tribunal (hereinafter, referred to as 'ITAT') which has, by common order dated 17th April, 2009, dismissed the appeals of the Revenue.

8. During the course of arguments, Mr. Satyen Sethi, learned counsel for the assessee produced copies of three orders before us, in original, passed by the Commissioner of Customs (General). The first order is dated 13th April, 1998. It, inter alia, accepts the same fact, namely, SEC, Korea is a holding company of the assessee herein, and is following collaboration for a setting of technical know-how and components of the assessee company. For this reason, the case was taken as a case of relationship under Rule 2(2) of the Customs Valuation [Determination of Price of Imported Goods] Rules, 1988. A detailed questionnaire was issued to the assessee and provisional assessment of all Bills of Entry of the assessee was ordered. The assessee had submitted the reply to the questionnaire sent by the SVB. The reply of the assessee and the material produced was examined by SVB. Commissioner of Customs (General), thereafter, examined the issue in the light of the said report and the explanation furnished by the assessee. This order further reveals that the commissioner formulated three points which were to be decided by him in the said case. The first point was as to whether the apparent relationship between SEC and the assessee has influenced the invoice values being charged by SEC in respect of imports of capital goods, CBUs and components. This point was answered in negative holding that the declared price of the imported components had not been affected by the said relationship between the SEC and the assessee. The price, as declared, was accordingly accepted at arm's length price and the goods cleared after charging customs duty on the basis of prices declared by the assessee in the import documents. Other two orders, in original, passed by the office of the Commissioner of Customs are dated 23rd March, 2001 and 23rd January, 2003, where the conclusion arrived at is in identical terms as contained in the order dated 13th April, 1998.

9. We may additionally observe that in the order, in original, dated 23rd March, 2001, findings are recorded in respect of different material/components imported, i.e., to say color monitors of different dimensions and hard disk drive, etc. and findings given in respect of all these materials is that the prices at which the goods are imported are reasonable and not excessive and the relationship of SEC, Korea with the assessee has not influenced the said price. In view of the aforesaid categorical findings by the custom authorities, after getting the valuation done from its SVB, when this material was produced before the Assessing Officer, the Assessing Officer glossed over the same and only on the ground that SEC, Korea was a parent company of the assessee herein and was controlling the affairs of the assessee company presumed that the prices at which the assessee imported the aforesaid materials from the said parent company must be excessive and unreasonable.

10. Apart from this presumption, based on the relationship between the parent company and the assessee company, there was no other material before the Assessing Officer to come to such a conclusion. This would be clear from the following observations of the Assessing Officer in the impugned order.

"... in view of the standard practice, uses etc of multinational business activities and its very motive and purpose of the business whether in one country or in another as the case may be, it is considered that there is a case of making a disallowance u/s 40A(2)(b) of the IT Act, 1961. Since, Samsung Electronics Company, Korea is a established and ongoing business enterprise, the normal presumption will be that it must have made a reasonable profit from its transactions to the assessee company. The representatives of the company were therefore asked to provide either the balance sheet and P & L A/c of the Samsung Electronics Company, Korea or the

margin of profit in the hands of Samsung Electronics Company, Korea from the transaction with the assessee company to quantify the amount of disallowance u/s 40A(2)(b) of the IT Act, 1961 in a logical, fair and reasonable manner. However, the assessee company expressed its inability in providing this information on the plea that same was not available with it. The contention of the assessee may be correct, as it may not be in the possession of the information pertaining to Samsung Electronics Company, Korea. However, considering the close relationship between the assessee company and the Samsung Electronics Company, Korea and near complete conversion of their interests, same could not have been a difficult job had assessee company made serious attempt to obtain this information."

11. In the process, weighty and substantial submissions made by the assessee before the Assessing Officer were totally ignored and brushed aside. We may note in this behalf that the assessee had specifically argued on the basis of material produced that sales by the parent company to the assessee made in various years of different items were more or less at constant price and difference if any was mainly on account of fluctuation in the rate of foreign exchange. It is discernable from the order dated 24th November, 2003 passed by CIT(A) in respect of assessment year 2000-01 that the assessee had filed a comparative chart of the gross margin earned on such trade.

12. The CIT(A) had also recorded the said finding of fact that the prices were competitive in nature with respect to the other suppliers of such components and there should not be any allegation that higher price had been paid for such import. It was also submitted by the assessee that assessee deals in white goods, a sector in which there is huge competition and therefore there could not have been a reason to over view the components and raw materials as it would adversely affect the business of the Assessee company. It was also submitted that such an invoicing would have resulted in paying substantial custom duty to the customs authority which was much less than the rate of income tax and thus, such an invoicing would have increased the liability of the assessee and would have gone against the interest, not only of the assessee company but the Korean company as well.

13. The aforesaid discussion would clearly demonstrate that the two authorities below have arrived at a specific finding of fact that the raw materials are imported by the assessee from SEC, Korea at reasonable/competent rates which are neither excessive nor unreasonable. Once such a finding is recorded, which is a pure finding of fact, the question of applicability of provision 40A(2)(b) would not arise at all. It is held by Apex Court in *Upper India Publishing House P. Ltd. v. CIT (1979) 117 ITR 569 (SC)* that such a finding is a finding of the fact and in this backdrop the provision of Section 40A(2)(b) cannot be invoked which becomes an academic question. The brief order of the Supreme Court in the said case reads as under:-

"There are two questions in respect of which a reference has been directed by the High Court on the application of the Revenue under Section 256(2) of the Income-tax Act 1961. So far as the first question is concerned, it is undoubtedly a question of law and could properly form the subject-matter of a reference but the second question as framed is clearly a question of fact and we fail to see how it could be directed to be referred by the High Court. The question whether a particular expenditure on rent is excessive and unreasonable or not is essentially a question of fact and does not involve any issue of law and hence we are of the view that the second question ought not to have been directed to be referred by the High Court.

But if the second question could not form the subject-matter of a reference, then obviously the first question becomes academic, because Section 40A(2)(a) cannot have any application, unless it is first held that the expenditure on rent was excessive or unreasonable. We, accordingly, allow the appeal and set aside the order of reference made by the High Court. There will be no order as to costs of the appeal."

14. To the same effect is the judgment of this Court in the case of *Shriram Pistons and Rings Ltd. (1990) 181 ITR 230 Del*.

15. Learned counsel for the appellant has strongly relied upon the judgment of Madras High Court in *CIT v. NEPC India Ltd. (2008) 303 ITR 271 (Mad)* to contend that onus would be upon the assessee to place relevant material on record and to demonstrate that the prices on which the goods were imported were reasonable and not exclusive and in the instant case this onus had not been discharged by the assessee. In the first place such a condition is not permissible when it is concluded by us that provision of Section 40A(2)(b) of the Act are not applicable. That apart, the narration of facts stated above, clearly, proves to be contrary and demonstrates that the assessee had discharged the initial onus. The assessee had shown that the purchase price had been more or less the same in dollar terms in this and earlier years. The import of goods was subject to levy of customs duty and the price declared to the custom authorities had been accepted by them, as noted above. By placing this material on record, the assessee had discharged initial onus cast upon it. Thereafter, the onus thus shifts on the department to demonstrate as to how the price was excessive or unreasonable. In NEPC India Ltd. (supra), the assessee had failed to discharge such an initial onus otherwise the principal of law which was stated by the Madras High Court in that case would hit the balance in favour of the assessee herein when applied on the facts of this case, as is clear from the following discussion therein:-

"8. Now, let us analyse the power and jurisdiction conferred on the Assessing Officer under Section 40A(2)(a) of the Act, which revolves on the discretion conferred on him in the context of "Assessing Officer is of opinion". The words "is of opinion" indicate that the opinion must be formed by the Assessing Officer and it is of course, implicit that the opinion must be an honest opinion, having been formed based on the circumstances available before him. In other words, what all, therefore, Section 40A(2)(a) of the Act contemplates is that there should be some material available before the Assessing Officer for invoking Section 40A(2)(a) of the Act to initiate action to disallow or refuse to deduct the excessive or unreasonable expenditure mentioned thereunder. But, at the same time, before taking any final decision by invoking the power under Section 40A(2)(a) of the Act, either allowing or disallowing such expenditure incurred as excessive or unreasonable, such decision of the Assessing Officer should be based on reasons well-founded, which are judiciously acceptable and in which event, the finding or decision arrived at stating that the expenditure is excessive or unreasonable and the same cannot be allowed or deducted, certainly would become purely a question of fact, which the Court cannot interfere, in view of the ratio laid down in Commissioner of Income Tax v. T.T. Krishnamachary & Co. [2002] 256 ITR 82 (Mad), whereunder it is held that the finding that the payment was not excessive, as another party has also purchased at increased price, is one of the facts."

16. Therefore, even if we presume that section 40A(2)(b) is attracted in the instant case, on the facts of this case still the outcome has to be against the Revenue.

17. We, therefore, do not find any merit in this appeal and the same is hereby dismissed.