IN THE INCOME TAX APPELLATE TRIBUNAL
(DELHI BENCH 'I-1' : NEW DELHI)

BEFORE SHRI N.K. SAINI, ACCOUNTANT MEMBER
and
SHRI KULDIP SINGH, JUDICIAL MEMBER

ITA No.6082/Del./2012
(ASSESSMENT YEAR : 2008-09)

M/s. Ericsson India Private Ltd., 4th Floor, Dhakha House, 18/17, W.E.A. Pusa Lane, Karol Bagh, New Delhi – 110 005.	vs.	DCIT, Circle 11 (1), New Delhi.
(PAN : AAACE0138N)		
(APPELLANT)		**(RESPONDENT)**

ASSESSEE BY : S/Shri Ravi Sharma and
Anubhav Rustogi, Advocate
REVENUE BY : Shri Amrendra Kumar, CIT DR

Date of Hearing : 29.03.2017
Date of Order : 29.05.2017

O R D E R

PER KULDIP SINGH, JUDICIAL MEMBER :

The Appellant, M/s. Ericsson India Private Limited (hereinafter referred to as 'the assessee') by filing the present appeal sought to set aside the impugned order dated 28.09.2012, passed by the AO in consonance with the orders passed by the ld. DRP/TPO under section 143 (3) read with section 144C of the

Income-tax Act, 1961 (for short 'the Act') qua the assessment year 2008-09 on the grounds inter alia that :-

> ***"That on the facts and circumstances of the case, and in law;***
>
> ***1. That the assessment order passed by the Ld. Assessing Officer ("Ld. AO") under section 143(3) read with section 144C of the Income Tax Act, 1961 ("the Act"), in pursuance to the directions issued by the Learned Dispute Resolution Panel ("Ld. DRP") is a vitiated order as the Ld. DRP has erred both on facts and in law in confirming the addition to the extent of INR 16,60,70,145 in part made by the Ld. Transfer Pricing Officer ("TPO") to the Appellant's income, is without appropriate application of mind and in undue haste.***
>
> ***2. The reference made by the Ld. AO suffers from jurisdictional error as the Ld. AO has not recorded any reasons in the assessment order based on which he reached the conclusion that it was 'necessary or expedient' to refer the matter to the Learned Transfer Pricing Officer ("Ld. TPO") for computation of the Arm's Length Price ("ALP"), as is required under section 92CA(1) of the Act.***
>
> ***3. The Ld. AO pursuant to the directions of the Ld. DRP erred on facts and in law in enhancing the income of the Appellant by Rs 16,60,70,145 holding that the international transactions pertaining to the receipt of second line support services do not satisfy the arm's length principle envisaged under the Act and in doing so have grossly erred by:***
>
> > ***3.1. not appreciating that none of the conditions set out in section 92C(3) of the Act are satisfied in the present case;***
> >
> > ***3.2. disregarding the ALP, as determined by the Appellant in the Transfer Pricing (TP) documentation maintained by it in terms of***

section 92D of the Act read with Rule 10D of the Indian Income tax Rules, 1962 (,the Rules') without providing the Appellant with any cogent reason for rejection of the TP documentation maintained by the Appellant;

3.3. misinterpreting the concept of shareholder services and other concepts relating to intra group services contained in the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations released by the Organisation for Economic Cooperation and Development (OECD Guidelines);

3.4. disregarding the computation of cost submitted by the Appellant in support of the fee paid to Associated Enterprises for receipt of second line support services and instead, proposing a completely arbitrary methodology of cost allocation based on its own conjectures and surmises.

3.5. by proposing a flawed allocation methodology that allocates only 40% of the cost and does not take into account the business and commercial realities that would not allow any third party to absorb 60% of the cost which it incurs for rendering service.

3.6. not giving an opportunity of being heard before applying an arbitrary approach for allocation of cost, thus violating the principle of natural justice,

4. The Ld. AO pursuant to the directions of the Ld. DRP erred on facts and in law in ad-hoc disallowance of Rs.60,72,481 being 10% of the advertisement and business promotion expenses treating the same to be of capital in nature which provides enduring benefit to the company.

4.1. The Ld. AO pursuant to the directions of the Ld, DRP erred on facts and in law in not appreciating that .advertisement and business promotion expenses constitute revenue expenditure for the applicant.

5. That on the facts and in the circumstances of the case and in law, the Ld. AO erred in adding provision for leave encashment of Rs. 5,40,47,748 and provision for gratuity of Rs.4,85,96,365 treating the same as unascertained liabilities made on estimated basis while computing the book profits under section 115JB of the Act.

6. The Ld. AO erred by proposing to compute interest under section 234B and 234D of the Act mechanically and without recording any satisfactory reasons for the same."

2. Briefly stated the facts necessary for adjudication of the controversy at hand are : the assessee company, a wholly owned subsidiary of Telefonaktiebolaget LM Ericsson, Sweden, which is incorporated under the Indian Companies Act, 1956, which is the ultimate holding company of all Ericsson Group Companies situated across the globe. Assessee company, during the year under assessment, was into the business of trading, manufacturing/ assembly of telecommunication carrier equipment for sale to the independent customers, providing implementation, commissioning and support services relating to telecommunication systems and marketing of telecommunication equipment manufactured by

Group Companies and contract telecommunication software development services.

3. During the year under assessment, the assessee company entered into following international transactions :-

S.No.	Description of transaction	Method Selected	Total value of Transaction (Rs.)
1.	Purchase of raw material, spares etc.	Transactional Net Margin Method ('TNMM')	18,766,728,990
2.	Sale of material		113,386,404
3.	Purchase of Finished goods		10,579,698,565
4.	Purchase of Assets		33,914,309
5.	Software License Fee		1,696,093,685
6.	Rendering of Services		1,098,558,479
7.	Receipt of Service		2,480,993,865
8.	Contract Cost Credit		1,840,359,800
9.	Cost Recharge paid		18,289,837
10.	Cost Recharge received	Comparable Uncontrolled Price Method ('CUP') Method	40,929,591

4. During TP proceedings, the assessee was called upon to provide nature of break down of the intra group services received by the assessee during the year under assessment, regarding the following intra group services :-

1.	Receipt of Consultancy Services	388,410,433
2.	Administrative Fee and reimbursement of expat Salary	186,076,089
3.	Receipt of Information Systems and Information (IS/IT) Services	866,504,561
4.	Receipt Support Services (including Second line support services of Rs.342,913,561)	972,466,791
5.	Training & Seminar	67,535,991
	Grand Total	2,480,993,866

5. Ld. TPO noticed the receipt of aforesaid services being similar in nature to those undertaken by the assessee in the previous year and was accordingly called upon to justify the payment for receipt of second line support services (SLS) and the benefit obtained from such services. However, assessee claimed that the transactions are interlinked, therefore, they should be benchmarked together. However, TPO came to the conclusion that appropriate method is required to be applied for each of the transactions and as such applied CUP method for analyzing the arm's length nature of this payment by assessee to its AE. Ld. TPO on the basis of his TP analysis came to the conclusion that by applying the CUP method, the arm's length price of the transaction of payment for services availed for the "second line support including software related errors" is determined as nil as against Rs.34,29,13,561/- determined by the assessee and thereby enhanced the income of the assessee by Rs.34,29,13,561/-.

6. The assessee carried the matter before the ld. DRP by raising objections who disposed off the objections. Feeling aggrieved, the assessee has come up before the Tribunal by way of filing the present appeal.

7. We have heard the ld. Authorized Representatives of the parties to the appeal, gone through the documents relied upon and

orders passed by the revenue authorities below in the light of the facts and circumstances of the case.

GROUNDS NO.3, 3.1, 3.2, 3.3, 3.4, 3.5 & 3.6

8. Ld. AR for the assessee challenging the impugned order relied upon the order passed by the Tribunal in assessee's own case for AY 2007-08 vide order dated 11.05.2012 in ITA No.5141/Del/2011 and this factual position has not been controverted by the ld. DR for the Revenue. It is also not in dispute that the facts of the present case are similar to that of AY 2007-08 qua receipt of second line support services from associated enterprises. AO/TPO enhanced the income of the assessee by Rs.34,29,13,561/- on the ground that international transaction of receipt of second line support from AE does not satisfy the arms length principle under the Act.

9. Now, the sole question arises for determination in this case so far as transfer pricing issue is concerned :-

> ***"as to whether AO/DRP have erred in making upward adjustment of Rs.16,60,70,145/- to the returned income of the assessee on account of ALP of the second line support services (SLS) provided by the AE to the assessee?"***

9. This issue has already been dealt with by the coordinate Bench of the Tribunal in assessee's own case for AY 2007-08 and

the operative part of which is reproduced as under for ready perusal:-

> ***"29. We have carefully considered the rival submissions in the light of material placed before us. The facts have already been discussed in detail in the above part of this order. Mainly it is the case of the Revenue that assessee does not require to make any payment with regard to Second Line Support (SLS) obtained by it from its AE. As against that it is the case of the assessee that SLS services have been availed to minimum level where the assessee on its own is not able to resolve the problem as most of the problems have been resolved at the level of the assessee. It has been submitted that during the relevant assessment year the assessee has received customer service request to the tune of 11,108 out of which 1,245 have been addressed for SLS. No doubt that equipment has been supplied by the parent company of the assessee and the parent company of the assessee, who has supplied the instruments, can only resolve the complicated problems. During the warranty period, it is the liability of the parent company to resolve the problem without any charge. Therefore, reference to the warranty period is not relevant in the present case more particularly as AMC itself stands on different footings for which separate revenue has been received by the assessee. Supply of equipments is one thing and service of the equipments after the warranty period is another thing. In commercial words it is well known that after the expiry of warranty period the AMC is obtained for the faultless working of the equipment. The assessee is receiving separate consideration on account of AMC after the expiry of the warranty period and the figures relating to that have already been mentioned. The gross revenue has been earned at Rs.118,94,04,863/-. To ensure the faultless working of the equipment the assessee, as a matter of business expediency, has to resolve all the problems relating to that instrument. The assessee has its own set up for resolving the minor problems***

which it has resolved at its own. The assessee is aware of the fact that it has to incur expenditure with respect to each of the SLS invoked by him, therefore, from the data it is clear that minimum number of problems have been referred to the AE. Therefore, for availing the services of the AE for resolving the complicated problems the prerogative is of the assessee and the Department cannot say that the assessee does not require to make any payment for resolving the complicated problems of the instruments. Anybody obtaining AMC must have intention that the instrument which he is operating for his use should run continuously and effectively and it is for that purpose only one would avail AMC. Anticipating that some problems may not be resolved at the level of the assessee's own staff available with as the said staff may not be having the skill upto the level which requires to resolve complicated problem and in turn assessee adopted a mode according to which it is ensured that all the problems arising in the functioning of the instrument are efficiently resolved. That decision of the assessee is business expediency of the assessee so that the customers to whom the instruments have been supplied remain satisfied about the functioning of the equipment. Therefore, we find no force in the claim of the Revenue that for availing these services the assessee was not required to make any payment. The assessee has the right to enter into an arrangement according to which its business interests are protected and for protection of such interests of the business of the assessee, it has entered into an agreement with its AE. To hold that is the prerogative of the assessee to see and decide the business expediency, the reference can be made to the decision of Hon'ble Delhi High Court referred to by learned AR in the case of CIT vs. EKL Appliances Ltd.(supra) wherein their Lordships have observed that even Rule 10B(1)(a) does not authorize disallowance of any expenditure on the ground that it was not necessary or prudent for the assessee to have incurred the same or that in view of the expenditure was unremunerative or that in view of the continued

losses suffered by the assessee in his business, he could have fared better had he not incurred such expenditure. Whether or not to enter into the transaction is for the assessee to decide. It will be relevant to reproduce these observations of their Lordships which is contained in para 22 of the order as under:

> ***"22. Even Rule 108(1)(8) does not authorize of any expenditure on the ground that it was not necessary or prudent for the assessee to have incurred the same or that in view of the expenditure was unremunerative or that in view of the continued losses suffered by the assessee in his business, he could have fared better had he not incurred such expenditure. These are irrelevant considerations for the purpose of Rule 10B. Whether or not to enter into the transaction is for the assessee to decide. The quantum of expenditure can no doubt be examined by the TPO as per law but in judging the allowability thereof as business expenditure, he has no authority to disallow the entire expenditure or a part thereof on the ground that the assessee has suffered continuous losses. The financial health of assessee can never be a criterion to judge allowability of an expense; there is certainly no authority for that. What the TPO has done in the present case is to hold that the assessee ought not to have entered into the agreement to pay royalty/brand fee, because it has been suffering losses continuously. So long as the expenditure or payment has been demonstrated to have been incurred or laid out for the purposes of business, it is no concern of the TPO to disallow the same on any extraneous reasoning. As provided in the OECD guidelines, he is expected to examine the international transaction as he actually finds the same and then make suitable adjustment but a wholesale disallowance of the expenditure, particularly on the grounds***

which have been given by the TPO is not contemplated or authorized."

30. Keeping in view the aforementioned decision of Hon'ble Delhi High Court, we are of the opinion that it will be wrong to hold that the expenditure should be disallowed only on the ground that these expenses were not required to be incurred by the assessee. At the same time it has also to be seen that whether the price paid by the assessee is at arm's length. The term 'arm's length price' has been defined in section 92F which means a price which is applied or proposed to be applied in the transactions between the persons other then Associate Enterprises in uncontrolled conditions. It is only because of that their Lordships in the aforementioned decision have observed that "the quantum of expenditure can no doubt be examined by the TPO as per law but in judging the allowability thereof as business expenditure, he has no authority to disallow the entire expenditure or a part thereof on the ground that the assessee has suffered continuous losses.· Earlier to this they have observed that Revenue cannot disallow any expenditure on the ground. that it was not necessary or prudent for the assessee to have incurred the same or that in the view of the Revenue the expenditure was unremunerative. Looking into observations of their Lordships, it has to be held that reasonableness of an expenditure has not been excluded from determination. Here it can be mentioned that the formula, which was placed before the Assessing Officer, TPO, and DRP, was different from the formula according to which the impugned amounts have been calculated. For the first time it is brought to our notice that an amended formula has been adopted to calculate the impugned amount. Though it is the case of the learned AR that this formula is more logical and reasonable but at the same time this formula has not been examined by the authorities below. Though on the face of it the arguments of learned AR appear to have force but unless the new formula is also confronted to the

> ***Assessing Officer, it will be wholly unjustified to uphold the correctness & reasonableness of this formula which has been placed before us for the first time. Therefore, we consider it just and proper to restore the issue regarding determination of arm's length price with regard to the impugned transaction to the file of the Assessing Officer redetermine the same in the light of the aforementioned observations. Needless to observe that assessee should be given reasonable and sufficient opportunity of hearing for presenting its case.***
>
> ***31. With these observations, grounds relating to addition of Rs.31,34,48,369/- are disposed of and are considered to be partly allowed for statistical purposes."***

10. Following the decision rendered by the coordinate Bench of the Tribunal, we are of the considered view that the TPO has erred in holding that a subsidiary does not have to pay for audit accounting and such other functions performed by the parent company as owner of the subsidiary company and in further holding that if the subsidiary was independent company, it would neither require such services nor it would pay for the same. Hon'ble jurisdictional High Court in CIT vs. EKL Appliances Ltd. (ITA No.1068 / 2011) followed by the coordinate Bench in assessee's own case for AY 2007-08, held that, *"it would be wrong to hold that the expenditure should be disallowed only on the ground that these expenses were not required to be incurred by the assessee or those expenses have not benefited the assessee."* So, in

the instant case also, the duty of the TPO is to examine the quantum of expenditure as per law but the allowability of the expenses as business expenditure is required to be examined by the AO. So, following the decision rendered by the coordinate Bench of the Tribunal in assessee's own case for AY 2007-08, we hereby restore the issue regarding determination of arms length price with regard to receipt of second line support services to the file of TPO/AO to redetermine in the light of the observation made by the coordinate Bench vide order dated 11.05.2012 rendered in ITA No.5141/Del/2011 in assessee's own case by providing adequate opportunity of being heard to the assessee. Grounds No.3, 3.1, 3.2, 3.3, 3.4, 3.5 & 3.6 are determined in favour of the assessee.

GROUNDS NO.4 & 4.1

11. AO in accordance with the direction issued by DRP made ad hoc disallowance of Rs.60,72,481/- being 10% of the advertisement and business promotion expenses by treating the same to be capital in nature providing enduring benefit to the company. Despite the fact that in case of ***Sony India Private Limited vs. ACIT cited as 114 ITD 448 (Del.)***, coordinate Bench of the Tribunal has deleted similar disallowances on the ground that expenditure incurred by the assessee company on advertisement and sales promotion has not resulted in accrual of

any advantage of enduring nature and the same are in the nature of Revenue field and not in the capital field so as to treat the same as capital in nature. Ld. DRP has merely directed the AO to make disallowance of 10% of advertisement expenses only after ascertaining the fact that if the department has accepted the judgment of Tribunal rendered in case of ***Sony India Private Limited*** (supra). But till date the department has not come up if findings returned by the Tribunal in ***Sony India Private Limited*** (supra) have been overturned. So, in these circumstances, ad hoc disallowance of Rs.60,72,481/- made by the AO is not sustainable. So, grounds no.4 & 4.1 are determined in favour of the assessee.

GROUND NO.5

12. AO has added back provisions for leave encashment to the tune of Rs.5,40,47,748/- and provision for gratuity to the tune of Rs.4,85,96,365/- for computation of income treating the same as unascertained liability made on estimated basis while computing book profit u/s 115JB of the Act. However, in the face of the undisputed fact that the issue as to the allowability of provision of gratuity and leave encashment for the purpose of section 115JB of the Act has already been determined by the Tribunal in assessee's own case for AY 2001-02 to 2004-05 and for AY 2005-06, CIT (A) has deleted the addition made by the AO and no such addition

has been made in the preceding AY 2007-08, the addition is not sustainable. This addition has only been made as directed by the ld. DRP on the basis of assumption that in case, the department has already accepted the Hon'ble High Court and Tribunal's order in favour of the assessee for earlier assessment years by not filing further appeal the benefit should be extended to the AO otherwise AO shall retain the aforesaid additions. However, the Revenue has failed to bring on record if decisions rendered by Tribunal in assessee's own case have been overturned by the higher forum. So, in these circumstances, the addition of Rs.5,40,47,748/- and of Rs.4,85,96,365/- on account of provision for gratuity and leave encashment as unascertained liability respectively is not sustainable in the eyes of law. Hence, ground no.5 is determined in favour of the assessee.

GROUND NO.6

13. Ground No.6 needs no adjudication as the same is consequential in nature.

14. Resultantly, the appeal of the assessee is allowed for statistical purposes.

Order pronounced in open court on this 29th day of May, 2017.

Sd/-	sd/-
(N.K. SAINI)	**(KULDIP SINGH)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Dated the 29th day of May, 2017/TS

Copy forwarded to:

1.Appellant
2.Respondent
3.CIT
4.CIT (A)
5.CIT(ITAT), New Delhi.

AR, ITAT
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