

IN THE INCOME TAX APPELLATE TRIBUNAL, DELHI 'I-2' BENCH,
NEW DELHI

BEFORE SHRI N.K. BILLAIYA, ACCOUNTANT MEMBER, AND
SHRI KULDIP SINGH, JUDICIAL MEMBER

ITA No. 6700/DEL/2015
[A.Y 2009-10]

M/s Verizon India Pvt Ltd
A Wing, 3rd Floor,
Radisson Commercial Plaza
N H -8, New Delhi

Vs.

The Dy. C.I.T
Circle - 26(1)
New Delhi

PAN: AACCM 2423 N
(Applicant)

(Respondent)

Assessee By : Shri Shriram Seshadri, CA
Shri Prabhat Lath, CA
Ms. Amulya K. CA.

Department By : Shri H.K. Choudhary, CIT-DR

Date of Hearing : 06.05.2019
Date of Pronouncement : 10.05.2019

ORDER

PER N.K. BILLAIYA, ACCOUNTANT MEMBER,

This appeal by the assessee is preferred against the order of the
ld. CIT(A) - 44, New Delhi dated 03.09.2015 pertaining to assessment
year 2008-09.

2. Grievances of the assessee can be summarised as under:
 - a) Transfer Pricing [TP] adjustment;
 - b) Disallowance u/s 40(a)(i) of the Income-tax Act, 1961 [hereinafter referred to as 'the Act' for short];
 - c) Disallowance of reimbursement of conference call charges;
 - d) Disallowance of travel and conveyance charges.

3. In addition to the above, vide application dated 18.02.2019, the assessee has raised an additional ground in relation to the main ground against the TP adjustment and with this additional ground, the assessee contends for exclusion of Priya Ltd as comparable company based on subsequent judicial precedents in this regard.

4. We will first address to the additional ground raised by the assessee.

5. Facts on record show that the assessee itself has included Priya Ltd as a comparable company. Now the assessee contends that Priya is functionally not a comparable company and relies upon subsequent judicial decisions of the co-ordinate benches. In our considered opinion, whether a company is a good comparable or not is purely a

question of fact and no point of law is involved. In our considered view, the additional ground raised by the assessee is not tenable in law in the light of the decision of the Hon'ble Supreme Court in the case of NTPC 229 ITR 383. Since the inclusion or otherwise of a comparable company requires examination of new facts, hence there is no merit in the contention of the assessee. The additional ground so raised by the assessee is dismissed.

6. Coming to the alternative plea of the assessee, in relation to the allocation of unallocated expenses in the segmental reporting of Priya Ltd, we find force in the contention of the ld. counsel for the assessee.

The factual matrix can be understood from the following chart:

Particulars	Reference	As per TPO's Computation - based on segment revenue - Ref pg. 10 of CIT(A) order			As per Appellant's computation		
		Indenting Segment	Trading Segment	Total	Indenting Segment	Trading Segment	Total
Revenue(A)	Total revenue as	186.88	502.81	689.69	186.88	502.81	689.69
Segment Result (B)	As per segment financials	127.65	102.85	230.13	127.65		230.13
Allocated	C =(A-B)	(59.23)	(399.96)	(459.56)	(59.23)	(399.96)	(459.56)
Allocation of unallocated expenses	D = Unallocated expense	(41.83)	(117.62)	(159.45)	(91.21)	(68.24)	(159.45)
Total Cost	E = (C+D)	(101.06)	(517.58)	(618.64)	(150.44)	(468.20)	(618.64)
Operating Profit	F= (AE)	85.82	(14.77)	70.68	36.44	34.61	70.68
OP/TC	G =(F/E)	84.92%	-2.85%	11.43%	24.22%	7.39%	11.43%

7. The TPO observed that the assessee has incorrectly corrected the segmental margin of Priya Ltd. The assessee has treated the indenting segment as comparable and has allocated the unallocated expenses amounting to Rs. 1,63,21,400/- in the ratio of gross margin when it should have been allocated in the proportion of segmental revenue to total revenue. The TPO did not concur with this allocation of the assessee. The TPO found that the ratio of segmental revenue to total revenue is 27.06%. Accordingly, out of total unallocated expense of Rs. 1,63,21,400/-, a sum of Rs. 1,01,06,889/- has been allocated to the indenting segment. The TPO computed the segmental operating as under:

Segmental operating revenue	Rs. 18688202
Less:	
Allocated Expenses	Rs. 5923000
Unallocated Expenses	Rs. 4183889
Total operating expenses	Rs. 10106889
Operating Profit	Rs. 8581313
OP/TC	Rs. 84.90%

8. The Id. CIT(A), while deciding the issue, analysed the segmental result to arrive at direct cost allocated in these two segments i.e. indenting segment and trading segment of Priya Ltd, which is as under:

i) Cost allocated for indenting segment as per segmental results:-

The revenue	186.51 lacs
Less segment result i.e. profit of the segment without loading unallocated expense	127.28 lacs
Direct Cost allocated	59.23 lacs

ii) Cost allocated for Trading Chemicals:-

The revenue	502.81 lacs
Less segment result	102.85 lacs
Total Expense allocated	399.96 lacs
Less cost of material	373.16 lacs (as per profit & loss account)
Direct cost allocated to trading segment other than cost of material	26.8 lacs

9. The Id. CIT(A) further observed as under:

"Analysis of expenditure debited in the profit & loss account

"I have examined schedule P and Q of profit and loss account which contain entire expenses excluding cost of good traded. The schedule P is the expenditure related to employee cost amounting to 98.17 lacs and schedule Q is for other

expenses amounting to Rs. 144.19 lacs. Under the ahead other expenses there are certain items of expenses which prima facie relate to trading segment as other segment will not have handling of goods and related expense i.e warehousing charges, freight clearing and forwarding expenses, selling and advertisement expenses, commission on sells etc. The details of such expenses debited under the \ head other expenses are as under:-

Rents, service and warehousing charges	2437250
Sells promotion expense	407174
Freight clearing and forwarding	1068835
Selling and advertisement expenses	105923
Commission on sales	315090
Total	3927128

Against these apparent direct expenses for trading segment only 26.8 lacs has been allocated as direct expense to trading segments. At the most some portion of office rent may be pertaining to identity segment. Further, under the head travelling and conveyance Rs. 25,66,172/- has been debited out of these expenses, expenditure in foreign currency under the head travelling is rupee 3,85,495 only (item no. 6, page no. 19 of 26th annual PIL report) mention here that entire earning of indenting segment is through foreign exchange. Therefore, the share of indenting segment under the head travelling and conveyance expense will not be much in domestic travelling.

Conveyance expense is definitely local in nature which mostly will pertain to trading segment. If we exclude these above expenses, major remaining expenses are grouped as under:-

The nature of employment cost	98.17 lacs
Miscellaneous	25.35 lacs
Postage telephone, Fax expenses	13.92 lacs
Total	137.44 lacs

The total expenditure allocated to indenting segment by the TPO are as under:-

i)	Cost directly allocated in the segmental results	59.23 lacs
(ii	Unallocated expenses pertaining to this segment by the TPO	41.83 lacs
	Total	101.06 lacs

Therefore, out of total major expense not directly related to trading activity amounting to 137.44 lacs has been allocated to indenting segment to the extent of Rs. 101.06 lacs, which is 73% of remaining cost. In view of above analysis, it appears that allocation of unallocated expenses by the TPO matches with the financial statements of M/s Priya International Ltd, even on gross profit level. It may be mentioned here that

expense retable to indenting segment will either be employee cost or travelling cost or some secretarial cost mainly postage, telegraph, fax related to office expense.

Next arguments by the Ld. AR that my predecessor CIT appeal in appellant case for assessment year that has approved the allocation key on the basis of gross profit margin for unallocated expenses cannot be accepted as each assessment year has different facts in relation to the function performed and risk undertaken. It may further be mentioned that my predecessor has not apparently analyzed the financial results of M/s Priya International Ltd. before arriving at the conclusion.

Next argument of Ld. AR is that on ITAT Delhi in the case of DCIT v/s Corning essay ITA no. 2564/Del/2011 by order date 28/08/2015 has approved allocation of unallocated expenses in the ratio of gross profit. The decision of under rule ITAT is not applicable to the facts of the case as the financial result of Priya International Ltd. has been analyzed in detail above for allocation of unallocated expenses.

In view of the above analysis of financial results. I am convinced that unallocated expenses has been fairly allocated by the TPO to indenting segment. Accordingly the grounds of appeal relating to the determination of operating profit(OP by

TC)margin of M/s Priya International Ltd. is hereby dismissed. Profit margin of comparable M/s Priya International Ltd. is approved at the rate of 84.9%).

Considering the entire facts and circumstances of the case, the TPO's working of average profit margin of 23.32%(OP/TC) is hereby confirmed. Accordingly, adjustment . made under section 92CA for Rs. 3,18,27,587/- by AO/TPO is hereby confirmed. All these relevant grounds of appeal are hereby dismissed."

10. The ld. DR strongly relied upon the aforesaid findings of the ld. CIT(A).

11. The ld. counsel for the assessee drew our attention towards the chart exhibited elsewhere and pointed out that if the contention of the TPO is accepted, then it would result into absurd profitability margin in as much as the indenting segment is showing margin of 84.92% whereas the trading segment is showing loss of minus 2.85%. Whereas, if the gross profit ratio is adopted for allocation of unallocated expenses, then the indenting segment would show margin of 24.22% and trading segment would show a margin of 7.39%.

12. We have heard the rival submissions and have given thoughtful consideration to the orders of the authorities below. We find that the cost of allocation done by the Id. CIT(A) is adopted from the audited financial results of the assessee exhibited at page 506 of the paper book. Moreover, the exercise done by the Id. CIT(A) has nothing to do with unallocated expenses. We find that while analysing the expenses debited under the head 'Other expense", the Id. CIT(A) has completely ignored the fact that sales promotion expenses of Rs. 40,7,174/- is nothing but directly related to the indenting segment in as much as the commission earned by the assessee is in foreign currency and is directly related to the indenting segment. We find that the first appellate authority has simply presumed that the other expenses pertained to only trading segment.

13. We find that on identical set of facts in assessment year 2005-06, the Id. CIT(A) himself has approved the allocation key on the basis of gross profit margin for unallocated expenses. The Id. CIT(A) has declined to follow the decision of his predecessor given in assessment year 2005-06 because he is of the view that his predecessor has not apparently analysed the financial results of Priya Ltd before arriving at the conclusion. We do not find any force in this finding of the Id.

CIT(A). In assessment year 2005-06, the then Id. CIT(A) had considered the following chart:

Particulars	Financial year ended March 2009 ^A			
	Indenting	Trading Chemicals	Total Segments	Total
1				
income				
Income as per segmental information				
Total Revenue (including inter-	18,651,000	50,281,000	68,932,000	68,932,
Less: Inter-segment revenue				
1 Other allocated income			-	
otias Segmental income	18,651,000	50,281,000	68,932,000	68,932,
iSegmental revenue/Total operating	27.06%	72.943%		
(Gross Margin	18,651,000	12,964,638		
Gross Margin Ratio ^59%		41%		
Operating Income (as per P&I)				68,995,
Income to be allocated from P&L to segmental income (Allocated on the	37,202	25,859	63,061	63,061
Total operating income	18,688,202	50,306,859	68,995,061	
Segmental profit (Given)	12,728,000	10,289,000	23,017,000	
Expenses				
Allocated expenses (segmental)	5,923,000	39,992,000	45,915,000	
Add: Unallocated items of expense directly allocable to any				
Total Segmental expense	5,923,000	39,992,000	45,915,000	45,915,
Operating expenses (as per P& L)				61,376,
Expenses to be allocated from P&L to segmental expense allocated on the	9,121,213	6,340,315	15,461,528	15,461,528
otal operating expenses	15,044,213	46,332,315	61,376,528	
Segment cost/Total operation cost	24.51%	75.49%		
(Operating profit	3,643,989	3,974,544		
(Operating Profit/Total operating	24.22%	8.58%		
!				
*				

14. After considering the aforementioned chart, the Id. CIT(A) accepted the contention that the allocation key should be on the basis of gross profit margin for unallocated expenses.

15. After considering the facts in totality, in light of the factual matrix exhibited elsewhere, we are of the considered opinion that the allocation key on the basis of gross profit margin is correct. We accordingly direct the Assessing Officer/TPO to allocate unallocated expenses on the basis of gross profit margin. Accordingly, this alternative ground is allowed.

16. Ground No. 2 has not been pressed. The same is dismissed as not pressed.

17. Facts relating to Ground No. 3 are that during the course of assessment proceedings, the A.O observed that the assessee has paid conference call charges payable to its AE, namely, Verizon, Hong Kong. The assessee was asked to explain why the same should not be disallowed u/s 40(a)(ia) of the Act.

18. The assessee, in its reply, contended that conference charges payment was made taxable in India as royalty by retrospective amendment by Explanation 6 of section 9(1) of the Act. Therefore, during the period of payment, there was no such definition of royalty. Accordingly, the said sum was not taxable in India, hence there is no

question of deduction of tax u/s 195 of the Act. It was further pointed out that the payment is in the nature of reimbursement, therefore, there is no element of income in the hands of the payee and hence section 195 of the Act does not apply on the facts of the case.

19. The contention of the assessee did not find any favour with the Assessing Officer who was of the strong belief that Explanation 6 to section 91 of the Act is clarificatory in nature and has been given a retrospective effect.

20. The ld. DR has also highlighted this fact by stating that the definition of Royalty u/s 91 of the Act always included impugned payment and it is only by way of clarification Explanation 6 has been inserted.

21. The Assessing Officer has also dismissed the alternative contention of the assessee that the payment is nothing but reimbursement. The Assessing Officer was of the opinion that the purpose of payment is important since such conference charges is royalty in India, therefore, the same is taxable in India.

22. The Assessing Officer further observed that merely because the payment is made first by the group concern of the assessee and then recovered from the assessee, does not alter the taxability of royalty.

23. We have given a thoughtful consideration to the orders of the authorities below. There is no dispute that the impugned payment is governed by Explanation 6 section 91 as it existed before Finance Act, 2012. It is only after Finance Act 2012 Explanation 4, 5 and 6 to section 91 have been inserted with retrospective effect. In our considered opinion, the assessee could not be held to be liable to deduct tax at source by relying on subsequent amendments.

24. Similar view taken by the co-ordinate bench at Kolkata in the case of SDV International Logistics Ltd in ITA Nos 501, 708 and 712/Kol/2016 reported in 172 ITD 505.

25. Coming to the issue of reimbursement, we find that there is no dispute that Verizon Hong Kong [AE of the assessee] has made payment and subsequently, cost was recovered from the assessee company which can be understood from the chart annexed as Annexure which will form part of this order.

26. Considering the facts of the case in hand in totality, in the light of decision of the co-ordinate bench [supra], we are of the considered opinion that no liability to deduct tax at source arose on the impugned payment qua insertion of Explanation to section 91 of the Act. Moreover, being reimbursement, no liability to deduct tax at source arose. Accordingly, Ground No. 3 is allowed.

27. Facts relating to Ground No. 4 are that during the course of scrutiny assessment proceedings, the Assessing Officer noticed that the assessee has incurred travelling expenses amounting to 80,38,766/-. The Assessing Officer further noticed that other than local travelling expenses of Rs. 80.38 lakhs, foreign travelling expenses were also booked amounting to Rs. 14,95,607/-. The Assessing Officer observed that the assessee has not provided details of some of the travelling expenses and further observed that there was no need for the assessee to take foreign travelling as major functions involved providing local contact point for customers in India and supporting the requirements of local customers in India.

28. Before the CIT(A), the assessee submitted complete details of travelling and conveyance expenditure such as complete ledger providing details of air fare, visa charges for foreign travel, sample invoice of air fare and cabs hired by the assessee and detail breakup of travelling and conveyance expenses. It was pointed out that all the details and vouchers are certified by the internal auditor and final accounts are duly audited by statutory auditors. It was further contended that the assessee provided services to its customer on a cost plus basis. Therefore, the entire cost has been duly compensated by its AEs.

29. After considering the facts and detailed submissions, the Id. CIT(A) held as under:-

"I have examined and considered facts of the case and arguments of Ld. AR. I do not agree with the reasoning of the assessing officer that no. foreign travel is "required by the employee of the appellant for its business. The appellant is getting revenue from its AE abroad for services rendered by it. Therefore, it is the business need of the appellant to incur such expenses. Other grounds of disallowance by the assessing officer is that the appellant has claimed some part of the expense on provision basis apparently from the break up filed by the appellant.

Ld. AR has claimed that each expense is backed up by bills and vouchers and filed bills and vouchers as fresh evidences. I have perused these bills and voucher & Mostly, the bills are in name of the appellant. However, few bills issued by Auto Quick (P) Ltd. are in the name of M/s Verizon Business', AE of the appellant. As these invoices are not in the name of the appellant, the expenditure cannot be said to pertain to the appellant. The assessing officer is directed to verify the bills and vouchers in respect of travelling and conveyance expense. If the bills and vouchers are not in the name of the appellant, the disallowance should be restricted to the extent of such bills /vouchers.

I would also like to consider the arguments of Ld. AR that the appellant is getting the revenue on the basis of expense with mark up of 11%. This model of business is to compute the revenue. After crediting such revenue on this basis, the appellant has to claim expense in its books of accounts which is actually incurred. Undoubtedly, the expense under the head 'traveling and conveyance' are claimed by the appellant and the appellant has to substantiate these expense to arrive at income. Therefore, just because the appellant is getting revenue on the basis of expenditure does not absolve the appellant from its onus to prove the genuineness of the expenditure claimed by it in its book of account. Therefore, this argument is not acceptable.

30. Before us, the Id. AR reiterated what has been stated before the lower authorities.

31. Per contra, the Id. DR strongly supported the findings of the CIT(A).

32. We have given a thoughtful consideration to the orders of the authorities below. We find that even the first appellate authority has dismissed the reasoning of the Assessing Officer that no foreign travel is required by the employee of the assessee for its business.

33. We find that the CIT(A) has categorically observed that few bills issued by Auto Quick [P] Ltd are in the name of M/s Verizon Business, the AE of the appellant. As these invoices are not in the name of the appellant, the CIT(A) observed that the expenditure cannot be stated to pertain to the appellant.

34. The CIT(A) directed the Assessing Officer to verify the bills and vouchers in respect of travelling and conveyance expenses. If the bills and vouchers are not in the name of the assessee, the disallowance should be restricted to the extent of such bills/vouchers. We do not

find any error or infirmity in such directions of the CIT(A). The assessee is directed to produce all the bills/vouchers for verification and the Assessing Officer is directed to verify the same and if some invoices/bills are not found in the name of the assessee, only such expenses should be disallowed. With these directions, Ground No. 4 is partly allowed.

35. In the result, the appeal of the assessee in ITA No. 6700/DEL/2015 is partly allowed.

The order is pronounced in the open court on 10.05.2019.

Sd/-

**[KULDIP SINGH]
JUDICIAL MEMBER**

Sd/-

**[N.K. BILLAIYA]
ACCOUNTANT MEMBER**

Dated: 10th May, 2019

VL/

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR

Asst. Registrar,
ITAT, New Delhi

Date of dictation	
Date on which the typed draft is placed before the dictating Member	
Date on which the typed draft is placed before the Other Member	
Date on which the approved draft comes to the Sr.PS/PS	
Date on which the fair order is placed before the Dictating Member for pronouncement	
Date on which the fair order comes back to the Sr.PS/PS	
Date on which the final order is uploaded on the website of ITAT	
Date on which the file goes to the Bench Clerk	
Date on which the file goes to the Head Clerk	
The date on which the file goes to the Assistant Registrar for signature on the order	
Date of dispatch of the Order	