

IN THE INCOME TAX APPELLATE TRIBUNAL “K” BENCH, MUMBAI

BEFORE SHRI G.S.PANNU, VP AND SHRI AMARJIT SINGH, JM

आयकर अपील सं/ I.T.A. No.740/Mum/2016
(निर्धारण वर्ष / Assessment Year: 2011-12)

M/s. Everest Kanto Cylinder Ltd. 204, Raheja Centre, Free Press Journal Marg, Nariman Point, Mumbai - 400021	<u>बनाम/</u> Vs.	Asst. Commissioner of Income Tax (LTU)-2 29 th Centre No.1, World Trade Centre, Cuffe Parade, Mumbai - 400005
स्थायी लेखा सं./जीआइआर सं./PAN/GIR No. : AAACE0836F		
(अपीलार्थी /Appellant)	..	(प्रत्यर्थी / Respondent)

Assessee by:	Shri Shekhar Gupta
Revenue by:	Mrs. Malathi Shridharan

सुनवाई की तारीख / Date of Hearing: 05.09.2019
घोषणा की तारीख /Date of Pronouncement: 06.09.2019

आदेश / O R D E R

PER AMARJIT SINGH, JM:

The assessee has filed the present appeal against the assessment order passed u/s.144C(5) of the Income Tax Act, 1961 (in short “the Act”) in pursuance of the directions of Dispute Resolution Panel – I, Mumbai [hereinafter referred to as the “DRP”] dated 03.12.2015 relevant to the A.Y. 2011-12.

2. The assessee has raised the following grounds: -

- “1. *The learned assessing officer has erred in law and on the facts of the case in disallowing Rs.16,37,570/- u/s.14A of the I.T.Act pursuant to the directions of the DRP.*
2. *The learned assessing officer has erred in law and on the facts of the case in making addition of Rs.16,37,570/- u/s.14A to the book profits u/s.115JB of the Income Tax Act pursuant to directions of the DRP.*
3. *The learned assessing officer has erred in law and on the facts of the case in making an addition of Rs.4,30,87,250/- on account of guarantee commission pursuant to the directions of the DRP.*
4. *The learned assessing officer has erred in law and on the facts of the case in making an addition of Rs.56,97,769/- on account of interest charges to Associate Enterprise pursuant to the directions of the DRP.*

3. Brief facts of the case are that in the present case draft assessment order dated 23.03.2015 was passed u/s 144C(1) of the Act, 1961 and forwarded to the assessee. The assessee has filed the objection form no. 35 in respect of variations made by AO in the draft order dated 23.03.2015. The dispute resolution panel DRP-1 Mumbai offered an opportunity of being heard to the assessee. The assessee in pursuance of provision 144(C) of the I.T. Act, 1961 appeared before the DRP and raised the objection. The assessee company is engaged in the business of manufacturer of high pressure Seamless gas cylinder services and compressed natural gas cylinders. The TPO passed an order on 30.01.2015 u/s 52CA(3) of the Act and made the transfer pricing adjustment of Rs.13,73,10,992/-. Thereafter the Assessing Officer incorporated the TPO order and passed the draft order u/s 143(3) of the Act r.w. Rule 144C(1) of the Act on 23.03.2015 which was served on 30.03.2015. The assessee filed the objection in form no. 35A on 23.04.2015. The objections were decided by the DRP-1,

Mumbai and passed the direction on 03.12.2015. The assessee was not satisfied, therefore, the assessee has filed the present appeal before us.

ISSUE NO.1 TO 2:-

4. Under these issues the assessee has challenged the disallowance u/s.14A. The assessee has earned the dividend income to the tune of Rs.1,26,70,862/- which has been claimed exempted u/s.10(33) of the Act. The assessee did not make any disallowance u/s.14A of the Act. The notice was issued and thereafter a revised computation of disallowance u/s.14A r.w. Rule 8D of the Act to the extent of Rs.9,05,594/- was submitted. However, the assessee requested to not to disallow any expenditure because the assessee did not borrow any funds for the investment to earn the exempt income but the Assessing Officer applied the provision u/s.14A r.w.Rule 8D of the Act and disallowed the expenditure under the provision of 14A read with rule 8D(2)(i) and 8D(2)(iii) of the Act to the tune of Rs.16,37,570/- and also disallowed the same u/s.115JB of the Act. The learned representative of the assessee has argued that the assessee was having his own fund more than the investment, therefore, in view of the law settled in *HDFC Bank Ltd. Vs. DCIT (Bombay) 383 ITR 529*, the investment was liable to be treated from its own funds and no expenditure of any kind was liable to be assessed to earn the said income in accordance with law. However, on the other hand the learned representative of the department has strongly relied upon the order passed by the Assessing Officer under challenge. By giving the careful thoughts to the contention raised by the learned representative of the parties and perusing the record carefully, it came into the notice that assessee was having more funds in

comparison to the investment. The balance sheet and profit and loss account has been filed which lies at page 1 to 69 of the paper book. The balance sheet lies at Page 30 of speaks that the assessee was having the funds in lacs to the tune of Rs.52,129.05. The said balance sheet speaks about the investment to the tune of Rs.14,237.24. According, to the said balance sheet, it is not in dispute that the assessee was having more funds then his investments. In view of the law settled in *HDFC Bank Ltd. Vs. DCIT (Bombay) 383 ITR 529*, it is presumed that the assessee made the investment from his own funds to earn the exempt income. In the said circumstances, no disallowance on account of interest expenditure is permissible u/s.14A of the Act. Under the said circumstances no disallowance of interest expenditure is justifiable. Therefore, we delete the addition on account of interest expenses made in view of the provision u/s.14A r.w.Rule 8D of the Act and addition on account of the provision u/s.115JB of the Act. We restrict the claim to the extent of 9,05,594/- made in view of provision rule 8D(2)(III) of the Act. Accordingly, we set aside the finding of the DRP Mumbai(1) and decide this issue in favour of the assessee against the revenue.

ISSUE NO.3:-

5. The present issue relates to addition of Rs.4,30,87,250/-on account of guarantee commission pursuant to the directions of the DRP. The issue is in relation to an addition of Rs.4,30,87,250/- made to the total income on account of transfer pricing adjustments with respect to the corporate guarantee issued by the assessee on behalf of its foreign associated enterprises namely, EKC International FZE, UAE, EKC Industries

(Tianjin), China and CP Industries Ltd., USA. In this context brief facts are that the assessee was found to have entered into certain international transactions with its associated enterprise within the meaning of section 92B of the Act and consequential reference under section 92CA(1) was made by the Assessing Officer to the Transfer Pricing Officer (TPO) for determination of arm's length price of such transactions. The TPO had passed an order u/s. 92CA(3) dated 30-01-2015 making an adjustment on account of corporate guarantee as under:

Name of the AE	Corporate guarantee commission charged	Percentage	ALP of the corporate guarantee commission	Percentage	Adjustment
EKC International FZE, UAE	51,34,750	0.5%	1,02,69,500	1%	51,34,750
EKC Industries (Tianjin), China	Nil	Nil	89,30,000	4%	89,30,000
CP Industries Ltd. USA	Nil	Nil	9,04,16,250	4.5%	9,04,16,250
	51,34,750		10,96,15,750		10,44,81,000

6. The assessee filed its objections before the Hon'ble DRP and the Hon'ble DRP vide their directions dated 03-12-2015 modified the order of the TPO and directed that the guarantee commission shall be charged @ 1% for corporate guarantee issued to EKC International FZE, UAE, 1.25% corporate guarantee issued to EKC Industries (Tianjin), China and 1.75% corporate guarantee issued to CP Industries Ltd., USA. The relevant portion of the order of the Hon'ble DRP is as under:

"In the present case also, the assessee had issued financial guarantee to the bank on behalf of its AEs. It has relied on the order of the Hon'ble Tribunal in its case for AY 2009-10 for applying rate of 0.5% in respect of all the three guarantees issued by it. On the other hand, it has been

pointed out by the TPO that financial guarantees issued by the assessee should not be compared with the bank guarantee because the bank guarantee is secured against assets whereas a financial guarantee issued by the assessee is not. Thus, risks taken in issuing an unsecured financial guarantee issued by the assessee is much higher. We are in agreement with the TPO on this issue. Bombay High Court has also, in the case of the assessee itself for AY 2007-08 (Everest Kanto Cylinders Ltd. 119 DTR Born (0394), has held that a corporate guarantee cannot be compared with bank guarantee. Further, the guarantee rates charged to the assessee cannot be the same as the guarantee rate chargeable to its AEs since both are different and independent from each other. Hence, the guarantee rates, charged by YES Bank to the assessee cannot be taken as internal CUP. However, this secured guarantee can be taken as a guide for bench marking the unsecured guarantees issued by the assessee. Looking to the rate at which assessee has taken bank guarantee from YES Bank, considering the financial position of other AEs and also considering the fact that the assessee has issued unsecured financial guarantees we are of the opinion that charging guarantee commission at the rate of 1% for unsecured corporate guarantee issued to UAE subsidiary, 1.25% for unsecured corporate guarantee issued to Chinese subsidiary and 1.75% for unsecured corporate guarantee issued to CP Industries Ltd., USA would be appropriate. The AO shall modify the amount accordingly."

7. Thus, pursuant to the order of the AO, the assessee is in further appeal before us. The Ld. Representative of the assessee has argued that the rates adopted by the Hon'ble DRP in order to determine the arm's length rate of the impugned international transaction was untenable and relied upon the decision of the Hon'ble Bombay High Court in its own case wherein the Hon'ble Bombay High Court has upheld the order of the Tribunal the guarantee commission rate of 0.5%. The observations of the Hon'ble Bombay High Court reads as under:

"..... In the matter of guarantee commission, the adjustment made by the TPO were based on instances restricted to the commercial banks providing guarantees and did not contemplate the issue of a Corporate guarantee. No doubt these are contracts of guarantee, however, when they are commercial banks that issue bank guarantees which are treated as the blood of commerce being easily encashable in the event of default, and if the bank guarantee had to be obtained from commercial banks, the

higher commission could have been justified. In the present case, it is assessee company that is issuing corporate guarantee to the effect that if the subsidiary AE does not repay loan availed of it from ICICI, then in such event, the assessee would make good the amount and repay the loan. The consideration which applied for issuance of a corporate guarantee are distinct and separate from that of bank guarantee and accordingly we are of the view that commission charged cannot be called in question, in the manner TPO has done. In our view the comparison is not a between like transactions but the comparisons are between guarantees issued by the commercial bank as against a corporate guarantee issued by holding company for the benefit of its AE, a subsidiary company. In view of the above discussion we are of the view that the appeal does not raise any substantial question of law and it is dismissed. There will be no order as to on costs".

8. Considering the entirety of facts and circumstances of the case and on the basis of the material available on record, we, therefore, proceed to uphold the rate of 0.50% for the purpose of determining the arm's length rate of the guarantee commission fee. In this view of the matter, we direct the Assessing Officer to determine the addition in view of our aforesaid direction. Thus, on this aspect assessee succeeds.

ISSUE NO. 4

9. The issue no. 4 is in connection with the addition of Rs.56,97,769/- on account of interest charged to associate enterprises pursuant to directions of the DRP. In this context, the interest charged by the assessee on loan given to associate enterprises and the rate of interest applied by the TPO is as under:

Name of the AE	Interest charged	Percentage	ALP of the Interest	Percentage	Adjustment
EKC International FZE, UAE	21,16,958	LIBOR+1	1,60,78,033	10.25%	1,39,61,075
EKC Industries (Tianjin), China	1,79,70,397	5%	3,68,39,314	10.25%	1,88,68,917

Total	2,00,87,355		5,29,17,347		,328,29,992
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10. The assessee filed its objections before the Hon'ble DRP and the Hon'ble DRP vide their directions dated 03-12-2015 directed that the interest shall be charged @6 months LIBOR + 350 Basis point to EKC International FZE, UAE and 6 months LIBOR + 500 basis point to EKC Industries (Tianjin), China. The relevant portion of the order of the DRP is as under:

"In the aforesaid order Hon'ble Delhi High Court has held that interest rate applicable in case of loan transactions should be market determined interest rate applicable to the currency in which the loan has to be repaid. The currency in which the loan is to be repaid determines the rate of return on the money lent. In this case, the loan to both subsidiaries have been given in USD. Under these circumstances, we are of the opinion that USD rates for unsecured loan as applicable to the party whose credit rating is equivalent to that of the subsidiary should be applicable. The assessee has submitted that the I7-AT has held in its case for AY 2009-10 that charging of interest at the rate of LIBOR + 2% will be appropriate. The assessee has also submitted that its UAE subsidiary has taken loan from ICICI Bank were in facts three months LIBOR + .95% whereas Chinese subsidiary has taken loan in Chinese Yuan from Citi Bank at the rate of 5.95%. The AO has applied rate of 10.25% in respect of both the subsidies. So far as loan taken by the UAE subsidiary from ICICI Bank is concerned, it is seen that the loan is only USD 5 million. It is a secular loan with no charge on assets of the subsidiary and a corporate guarantee provided by the assessee. Besides, the UAE subsidiary has also to incur cost on insurance, upfront fee of 1% etc. Looking to the fact that the loan given by the assessee was a long term unsecured loan, no details have been provided by the assessee regarding the credit rating of the AEs and credit rating of the UAE subsidiary as determined by the AO is lower than that of the assessee, we are of the opinion that a of six months LIBOR + 350 basis points will be appropriate for UAE subsidiary and a rate of six months LIBOR + 500 basis points would be appropriate for the Chinese subsidiary. The AO/WO is directed to make that adjustments accordingly."

11. Thus, pursuant to the order of the AO, the assessee is in further appeal before us. Before us, the assessee has primarily argued that the rates

adopted by the Hon'ble DRP in order to determine the arm's length rate of the impugned international transaction was untenable and relied upon the order of the Hon'ble Tribunal in assessee's own case for the Assessment Year 2010-11 wherein it was held as under:

"Following the earlier order of this Tribunal in assessee's own case, we hold that the arm's length rate in respect of loan provided to the AE should be LIBOR +2%. Accordingly, the Assessing Officer is directed to recompute the arm's length rate in respect of the loan transactions to each AE of the assessee by clubbing all the loan transactions of each AE and compare the interest charged by the assessee with arm's length rate at LIBOR + 2%. It appears that as regards the transactions of loan to its AF at China, the said transaction is at arm's length as the assessee has charged the interest at 796, therefore, only with respect to the transaction of loan to AE at Dubai are required to be re-computed for the purpose of TP adjustment."

12. The assessee further pointed out that there has been a mistake in the order of the Tribunal in respect of the above directions since the assessee had filed additional evidences with regard to interest charged to its AC in China, EKC Industries (Tianjin), which was not considered in the proper perspective. The assessee further pointed out that pursuant to the Miscellaneous Application, the Hon'ble Tribunal considered the Miscellaneous Application and vide order dated 08-09-2017 directed the Assessing Officer to consider the additional evidence produced before the Hon'ble Tribunal and decide the issue with respect to the interest chargeable to the AE in China.

13. Keeping in view of the facts and circumstances of the present case and on the basis of the material available on record, we, therefore, proceed to uphold the rate of interest @ LIBOR + 2% in respect of AE in Dubai and in respect of interest chargeable to AF in China, the Assessing Officer may follow the decision taken by him in the proceedings for Assessment Year

2010-11 pursuant to the order of the Tribunal dated 08-09-2017. Thus, on this aspect assessee partly succeeds.

14. In the result, the appeal filed by the assessee is hereby partly allowed.

Order pronounced in the open court on 06/09/2019

Sd/-

(G.S.PANNU)
VICE PRESIDENT

मुंबई Mumbai; दिनांक Dated : 06/09/2019
Vijay/Sr. PS

Sd/-

(AMARJIT SINGH)
JUDICIAL MEMBER

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. आयकर आयुक्त(अपील) / The CIT(A)-
4. आयकर आयुक्त / CIT
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, मुंबई / DR, ITAT, Mumbai
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

सत्यापित प्रति //True Copy//

**उप/सहायक पंजीकार / (Dy./Asstt. Registrar)
आयकर अपीलीय अधिकरण, मुंबई / ITAT, Mumbai**