IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "J", MUMBAI

BEFORE SHRI C.N. PRASAD, HON'BLE JUDICIAL MEMBER AND SHRI N.K. PRADHAN, HON'BLE ACCOUNTANT MEMBER

ITA NO.2301/MUM/2015 (A.Y: 2009-10)
&
ITA.No. 3883/MUM/2016 (A.Y: 2010-11)

M/s. Reliance Life Sciences Pvt. Ltd., DALSC, R-282, TTC Area of MIDC Thane Belapur Road Rabale, Navi Mumbai – 400 701 **PAN: AABCR7594L**	*v.*	Asst. CIT-7(2) Aayakar Bhavan M.K. Road Mumbai-400 020
(Appellant)		**(Respondent)**

Assessee by	**:**	**Shri Madhur Agarwal**
		Ms. Rikita Joshi
Department by	**:**	**Shri Manish Kumar Singh**
Date of Hearing	**:**	**27.09.2019**
Date of Pronouncement	**:**	**30.09.2019**

O R D E R

PER C.N. PRASAD (JM)

1. These two appeals are filed by the assessee against different orders of the Learned commissioner of Income-tax (Appeals)-52, Mumbai [hereinafter in short "Ld.CIT(A)"] dated 13.02.2015 and 17.02.2016 for the A.Y. 2009-10 and A.Y. 2010-11 respectively.

2. First we take up the appeal for the A.Y. 2009-10 and the first ground of appeal is in respect of confirming the disallowance made u/s. 14A of the Act.

3. Briefly stated the facts are that, the Assessing Officer while completing the assessment u/s. 143(3) of the Act on 02.02.2012 noticed that assessee has earned dividend income of ₹.20.25 Crores and no disallowance was made for earning such dividend income which was claimed as exempt. Therefore, placing reliance on the decision of the Hon'ble Bombay High Court in the case of Godrej & Boyce Manufacturing Co. Ltd., [328 ITR 81] Assessing Officer computed the disallowance u/s. 14A r.w. Rule 8D at ₹.3,36,78,061/- comprising of direct expenses incurred towards demat charges of ₹.1,24,649/- under Rule 8D(2)(i) and ₹.3,35,53,412/- under Rule 8D(2)(iii) being 0.5% of the average value of investments.

4. On appeal the Ld.CIT(A) sustained the disallowance observing that the assessee has not maintained separate books of accounts and the taxable income has been credited in its books of accounts and also the expenditure was debited in the consolidated books of accounts and no bifurcation has been furnished before the assessing officer.

5. Before us, Ld. Counsel for the assessee submits that disallowance u/s. 14A of the Act could only be made in respect of expenditure incurred and cannot extend to notional expenditure which has not been incurred at all. Ld. Counsel for the assessee submits that all the expenses incurred are only in respect of main business of the assessee and not incurred for earning any dividend income. Ld. Counsel referring to para No. 4.4 of the Ld.CIT(A) order submits that, Ld.CIT(A) himself observed that 99% of the dividend has come from group Companies. Therefore, counsel submits that assessee has not incurred any expenditure for earning dividend income.

6. Ld. Counsel for the assessee further submits that in spite of filing detailed reply before the assessing officer why there was no expenditure incurred by the assessee for earning exempt income the Assessing Officer has not recorded any satisfaction in invoking the provision of Rule 8D of I.T. Rules. Ld. Counsel for the assessee referring to page No. 372 of the Paper Book which is the reply furnished before the assessing officer, submits that it was brought to the notice of the Assessing Officer that the assessee's major area of activity is in the field of life sciences and major expenditure was incurred during the year was on life sciences activity. It was submitted that since no specific expenditure has been incurred for earning exempt income no disallowance u/s. 14A is called for.

Ld. Counsel for the assessee submits that the Assessing Officer mechanically invoked Rule 8D(2)(iii) which refers to 0.5% of average value of investments for computing the disallowance under Rule 8D of I.T rules. Ld. Counsel for the assessee submits that since such amount not having been incurred by the assessee for which deduction has not been claimed by the assessee under any other head cannot be disallowed u/s. 14A mechanically following Rule 8D(2)(iii) of I.T. Rules. Ld. Counsel for the assessee submits that it was brought to the notice of the Assessing Officer since assessee being in the life sciences business most of the administrative and other expenditure has been incurred on the life sciences business to require utilization of the men, material and other concerns and a very small quantum of expenditure can be attributed to general administrative expenditure.

7. In the alternative, Ld. Counsel for the assessee submits that investments on which no exempt income earned should not be considered for calculation of average value of investments. Reliance was placed on the decision of the Hon'ble Bombay High Court in the case of Pr.CIT *v.* M/s. Ballarpur Industries Limited in ITA.No. 51 of 2016 dated 13.10.2016 and ACIT *v.* Vireet Investments Private Limited [165 ITD 27]. He also further submitted that investments in Foreign Companies income from which is taxable should not be considered for average value of

investments. Reliance is placed on the decision of the Delhi Bench of Tribunal in the case of ACIT *v.* Indian Farmers Fertilizer Cooperative Ltd., [95 taxmann.com 114].

8. Ld. DR vehemently supported the orders of the authorities below.

9. We have heard the rival submissions and perused the orders of the authorities below. On a perusal of the breakup of the dividend income earned by the assessee we notice that assessee has received dividend income of ₹.20,12,92,325/- from its group Company Reliance Industries Limited and dividend of ₹.12,86,468/- from Mutual funds. Therefore, the contention of the assessee that since 99% of the dividend was earned from its group company for which no expenditure has been incurred has considerable force. We also find that in the course of the assessment proceedings the assessee has furnished a detailed reply as to why there is no expenditure incurred for earning dividend income by the assessee as major expenditure has been incurred only for the purpose of life sciences business and no expenditure was incurred for earning any dividend income and therefore no disallowance should be made. However, the Assessing Officer has not recorded any satisfaction as to why there shall be any expenditure for earning dividend income more so when the assessee has received 99% of its dividend income only from its

group Company Reliance Industries Limited. Therefore, what could have been disallowed was only that part of expenditure attributable for earning the dividend income only out of administrative expenses. The direct expenses incurred for earning dividend income i.e. demat charges were already disallowed by the Assessing Officer. The Assessing Officer has not given any justification and satisfaction for invoking the provisions of Rule 8D but applied mechanically referring to the decision of the Hon'ble Bombay high court and the special Bench in the case of Daga Capital Management Pvt. Ltd., [117 ITD 169].

10. Assessee has clearly stated that for earning dividend income no expenditure has been incurred and all the expenditure which has been debited to P&L account is only with reference to the life sciences business activity. On a perusal of the expenditure debited to P&L account, we noticed that majority of the expenditure is on account of life sciences business activity except the administrative expenses i.e. on personnel which is at ₹.24.44 Crores. Even out of this expenditure only the expenditure incurred in the general administration department should be considered for disallowance and not entire personnel expenses of ₹.24.44 Crores can be attributable for earning the dividend income. At best only a part of expenditure can be attributable for earning dividend income where a decision making has happened for making investments and that

to all the investment are in group Company M/s. Reliance Industries Limited. Therefore, in our opinion the Assessing Officer shall find out the expenditure attributable for earning exempt income with reference to the submissions made by the assessee that it has not incurred any expenditure for earning dividend income. The assessee shall furnish the necessary details of expenditure incurred as the assessee itself admits that a very small quantum of expenditure can be attributable the general administrative expenditure and in the absence of any suomoto disallowance by the assessee. This issue is restored to the file of the assessing officer for re-quantification of disallowance only from out of general administrative expenditure where a decision making has happened for making investments.

11. We also direct the Assessing Officer to exclude investments on which no exempt income was earned following the decision of the Special Bench of Delhi, ITAT in the case of ACIT v. Vireet Investments Private Limited [165 ITD 27]. We also direct the Assessing Officer to exclude investment in Foreign Companies income from which is taxable and they should be excluded while calculating the average value of investments. This ground is partly allowed.

12. The next ground of appeal is in respect of disallowance made u/s. 35(2AB) of the Act.

13. Briefly stated the facts are that, the Assessing Officer while completing the assessment noticed that assessee claimed ₹.34,73,31,373/- as deduction u/s. 35(2AB) and assessee claimed to have incurred an expenditure of ₹.23,15,54,249/- for in-house research facility. Further, Assessing Officer also noticed on verification of the details of expenses that assessee has made a payment of ₹.49,24,573/- to M/s. Reliance Clinical Research Services Private Limited for carrying out clinical trial needed for R&D activity. Assessing Officer disallowed the expenditure of ₹.49,24,573/- which was incurred on clinical trials outside the R&D facilities of the assessee for which weighted deduction was claimed @150%. On appeal the Ld.CIT(A) following his own order for the A.Y. 2007-08 sustained the disallowance.

14. Before us, Ld. Counsel for the assessee submits that Ld.CIT(A) has erred in confirming the action of the Assessing Officer in disallowing the claim for deduction u/s. 35(2AB) of the Act. Referring to the decision of the Hon'ble Gujarat High Court in the case of CIT *v.* Cadila Healthcare Ltd., [31 taxmann.com 300], Ld. Counsel for the assessee submits that

even clinical trials conducted outside the approved laboratory facility is eligible for deduction u/s. 35(2AB) of the Act.

15. Without prejudice to the above, the Ld. Counsel for the assessee submits that the said expenditure is allowable as deduction u/s. 37(1) of the Act. Ld. Counsel for the assessee submits that for the A.Y. 2007-08 the Tribunal in ITA.No. 1575/MUM/2013 dated 19.10.2015 allowed the alternative claim of the assessee that the expenditure be allowed as deduction u/s. 37(1) of the Act. Copy of the order is placed on record.

16. Ld. DR vehemently supported the orders of the authorities below.

17. We have heard the rival submissions and perused the orders of the authorities below. We observe from the Assessment Order that the assessee in the course of the assessment proceedings vide letter dated 17.01.2011 revised its claim u/s. 35(2AB) of the Act and assessee itself claimed expenditure on clinical trials of ₹.49,24,573/- u/s. 37(1) of the Act. However, before the Ld.CIT(A) assessee made a claim for deduction u/s. 35(2AB) of the Act in respect of clinical trials made outside the in-house facility of the assessee and in the alternative claim was made u/s. 37(1) of the Act. The Ld.CIT(A) rejected both the claims of the assessee i.e. u/s. 35(2AB) and 37(1) of the Act following his earlier order for the A.Y. 2007-08 observing that there is no change in facts. For the

A.Y. 2007-08 the Tribunal decided this issue in ITA.No. 1575/Mum/2013 dated 9.10.2015. On a perusal of the order of the Tribunal, we find that identical issue arouse for the A.Y. 2007-08 and the Tribunal allowed the alternative claim of the assessee that expenditure incurred on clinical trials outside the in-house facility of the assessee is allowable as deduction u/s. 37(1) of the Act observing as under: -

> *"5.5. We have considered the submissions made by both the sides and gone through the orders passed by the lower authorities and material placed before us for our consideration. Since, main claim of assessee with respect to deduction u/s 35(2AB) was not seriously pressed before us, therefore, same is dismissed. With respect to alternate claim made by the assessee u/s 37(1) of the Act, it is noted that the invoice of M/s. Reliance Clinical Research Services Pvt. Ltd. dated 31.03.2007 is enclosed at page no. 3 of the paper book, showing that payment has been made to the said company under the head "Clinical Trial Fees" – for the month of March, 2007 for time spent on 1st March to 31st March, 2007 for conducting clinical trials, in support of to all 'K projects', for a sum of Rs.57,65,564/-. It is further noted that on the back side of the invoice, complete details have been given with respect to time spent by 22 employees of RCRS, also giving particulars of the studies done by these employees. Names of these employees have been given along with their rates per hour. It is further noted that ld. Assessing Officer has shown no doubts about the genuineness of these expenses. It was held by Ld. CIT(A) that since claim of assessee with respect to deduction u/s.35(2AB) has been denied, therefore, these expenses are capital in nature. It was further observed by ld. CIT(A) that Assessing Officer, as well as assessee, have treated these expenses as capital in nature. In our view, the observations of Ld. CIT(A) are misplaced and without any basis. We have gone through details of these expenses. In our considered view, these expenses are apparently revenue in nature. Ld DR also could not point out as to which expenses are capital in nature. Thus, in our view, these expenses are of revenue nature.*
>
> *5.6. The other argument of Ld DR was that assessee did not claim these expenses u/s 37 and did not treat them as revenue in nature, and therefore assessee should be precluded from claiming benefit of these expenses, now at this stage, irrespective of this fact that these expenses may have been held as allowable, if the assessee would have made its claim correctly as per law, at the time of filing of return.*

We have carefully considered this argument, but find that it is not sustainable in the eyes of law, in the given facts and circumstances of the case, and in view of well settled position of law. In our view, there are no estoppels against law. Even if, assessee agrees or consents for something contrary to law, the A.O. is obliged under the law, to discharge his duty of making fair assessment of income and to compute amount of tax payable as per law. As per Article 265 of the Constitution of India, "No tax can be collected except by authority of law". Hon'ble Supreme Court in the case of Ramlal vs Rewa Coalfield Ltd (AIR 1962 SC 361), held that the state authorities should not raise technical pleas if the citizens have a lawful right, which is being denied to them merely on technical grounds. The state authorities cannot adopt the attitude which private litigants might adopt. Further, we place our reliance on the judgment of Hon'ble Delhi High Court in the case of CIT vs Bharat General Reinsurance Co Ltd 81 ITR 303 (Del.) Relevant portion is reproduced below:

> *"It was true that the assessee itself had included that dividend income in its return for the year in question, but there was no estoppel in the Income-tax Act and the assessee having itself challenged the validity of taxing the dividend during the year of assessment in question, it must be taken that it had resiled from the position which it had wrongly taken while filing the return. Quite apart from it, it was incumbent on the income-tax department to find out whether a particular income was assessable in the particular year or not. Merely because the assessee wrongly included the income in its return for a particular year, it could not confer jurisdiction on the department to tax that income in that year even though legally such income did not pertain to that year. Therefore the income from dividend was not assessable during the assessment year 1958-59, but it was assessable in the assessment year 1953-54. It could not, therefore, be taxed in the assessment year 1958-59."*

Further reliance is placed by us on another judgment of Hon'ble Gujarat High Court, in the case of, S.R. Koshti 276 ITR 165 (Guj) in which relief was granted to assessee with following observations:

> *"The authorities under the Act are under an obligation to act in accordance with law. Tax can be collected only as provided under the Act. If an assessee, under a mistake, misconception or on not being properly instructed, is over-assessed, the authorities under the Act are required to assist him and ensure that only legitimate taxes due are collected."*

In the case of Snehlata 192 CTR 50, Hon'ble J&K High Court held that "when the substantive law confers a benefit on the assessee under a statute, it cannot be taken away by the adjudicatory authority on mere technicalities. It is settled proposition of law that no tax can

be levied or recovered without authority of law. Article 265 of the Constitution of India and section 114 of the State (J&K) Constitution imposes an embargo on imposition and collection of tax if the same is without authority of law."

Lastly, we find it useful to refer to judgment of Hon'ble Bombay High Court in the case of Central Provinces Manganese Ore 112 ITR 734, holding that, the mere fact that a deduction was not claimed before the Income-tax Officer, was not of much importance, since if the liability arises then a claim can be made in a bonafide manner at any stage before the higher authority, who is competent to grant relief.

Thus, in view of aforesaid discussion, coupled with facts and circumstances of this case and clear position of law, as discussed above, in our opinion there was no reason to deny the claim assessee u/s 37 of the Act. Therefore, the AO is directed to allow these expenses u/s 37 of the Act. Accordingly, ground no.2 of the assessee's appeal is partly allowed."

18. In view of our observations and also since facts being identical following the order of the Tribunal we allow the claim of the assessee that the said expenditure should be allowed u/s. 37 of the Act. Thus, the Assessing Officer is directed to allow this expenditure u/s. 37 (1) of the Act. This Ground is allowed.

19. Ground Nos. 3 and 4 are in respect of transfer pricing adjustment. In Ground no. 3 assessee challenged the order of the Ld. CIT(A) in sustaining the action of the Assessing Officer in determining arm's length interest chargeable in respect of interest free loan advanced to M/s. Reliance Life Sciences Inc. (hereinafter in short "RLSI") at ₹.1,75,70,642/-. It was contented in the grounds that Ld. CIT(A) failed to appreciate that no interest was charged on the above referred loan since

the same loan was an optionally convertible into share capital at a fair value to be determined at the time of Conversion.

20. The assessing officer made a reference u/s. 92CA(1) of the Act to the TPO for determining arm's length price of the international transactions reported by the assessee. The TPO observed that assessee has advanced interest free Loans to RLSI and charged no interest in respect of said loan transactions. The assessee contented that since as per clause (3) of the loan agreement the said loan zero coupon was optionally convertible into share capital at any time not later than 31.03.2011 at a fair value to be determined by independent accountant at the time of conversion as per the terms of the loan agreement, no interest was charged by the assessee from RLSI. The contentions of the assessee have been rejected by the TPO observing as under: -

> *(a) Section 92(1) mandates that any income arising from an international transaction shall be computed having regard to the arm's length price. The fact that the activities undertaken by the assessee were a part of the project under development and the capital structure of the company had been decided keeping in mind the project risk this company, does not justify non-charging of interest under the Indian transfer pricing regulations, as no 3rd party in the similar circumstances will grant the loan without charging interest at the market rate.*
>
> *(b) The fact that the conversion price would take care of non-charging of interest, which was not charged by the assessee from its AE, does not justify the same under the Indian transfer pricing regulations. The internal arrangement for issuance of shares in future by taking into consideration of accumulated interest, is not*

quantified in this loan agreement. Therefore, this claim for compensating for not charging of interest against issuance of shares in future is not acceptable.

(c) The assessee's argument that the said loan is to be treated as equity, since it was optionally convertible into share capital at any time not later than March 31, 2011 and it is a known fact that till date no share capital is issued against the loan and further at the option of the assessee/ lender of the loan, can be either returned the loan or issue the shares, thus assessee can get back its loan also. Further, the same is also not acceptable since, then the assessee should have made an equity contribution in the first instance instead of granting a loan. If the assessee had directly funded/ invested, from the said acquisitions, the assessee would be entitled to:

> *dividends as and when the same are declared and the same would be taxable in India and*

> It would also have been liable to capital gains tax on sale of share in future.

In view of the above, the *above* argument of the assessee is not acceptable.

Since no enterprise would advance interest-free loan to a third party in similar *circumstances*, therefore the interest-free loan given by the assessee do not comply with the arm's length principle.

Moreover, the assessee's in its own case, while providing a loan to its AE 'M/s. RLS BV, has charged *interest* @ 6% p.a. and hence interest should have also been charged on the loan provided to M/s. RLS Inc.

In view of the above discussions and in the facts and circumstances, the, benchmarking of interest free loan given by the assessee to this AE i.e. M/s. RLS Inc. is determined by applying interest rate of @ 6% p.a. charged by the assesses itself on the loan provided to its another AE M/s. RLS BV.

The working of adjustment is as under:

Amount in Rs.)

Particulars	**Amount of loan**		**Rate of interest taken for benchmarking p.a. (%)**	**Period of charging interest**	**Adjustment (in Rs.)**
	(in USD)	**(in Rs.)**			
-On Opening Balance	38,85,000	15,55,37,980	6	1.4.2008 to 31.3.2009	93,32,279
-During the year	43,47,000	18,65,21,883	6	30.4.2008 to 31.3.2009	82,38,363
Total	82,32,000	34,20,59,863			1,75,70,642

21. Accordingly, the TPO charged interest at the rate of 6% per annum and made an adjustment of ₹.1,75,70,642/. Before the Ld. CIT(A), the assessee contented that the entire loan has been converted into equity capital in its books as on 31.03.2011 and hence no interest should be charged. However, the Ld.CIT(A) sustained the adjustment observing as under: -

> *"7.3. I have considered the facts of the case, submission of the appellant as against the findings/ observations of the TPO/AO in orders u/s 92 CA (3) 143(3) of the I.T. Act. The contentions and submissions of the appellant are being discussed and decided here in under:*
>
> *i. The appellant contended that the entire loan has been converted into equity capital in its book as on 31,03.2011 and hence no interest should be charged. In this regard, it is mentioned that even accepting these facts it is noted that from the date loan was advanced to AE till 31.03.2011 the funds were used by the AE without any cost against which assessee was paying interest. In third party situation no entity would part with its funds without charging any interest in such a condition. Accordingly, during the intervening period this amount continued to be in nature of loan only, on which interest was chargeable as per TP provisions. Other objections raised by the appellant have already been dealt with by TPO in his order.*
>
> *ii- It was stated that rate of interest charged @ 6% was quite high. In this regard it is noted that as mentioned on page 4 of his*

order, the TPO has charged this interest on the basis of Axis Bank quotation which was treated CUP. Further 1% was advanced for risk and finally 6% rate was applied. Further in judgment dated 12.04.2013 Hon'ble IT AT in IT A No. 7872 Mum 201 1 in the case of Aurionpro Solutions Ltd. have held as

> *"8.10 The Transfer Pricing Regulation are based on the deeming principle by taking into account a hypothetical situation that instead of having transaction with AE had the assesses transacted with unrelated party what would have been the financial/commercial result of that transaction. Thus, the effect of transaction on the income of the assessee is to be seen and considered and not effect on the cost or income of the AE. Therefore, the tested party is always the tax payer and not the AE. None of the factors under the Transfer Pricing Regulations require to consider whether the AEs would have incurred or earned more or less; but it is always considered whether the assessee had earned more or less by doing a similar transaction with an unrelated parties.*
>
> *8.11 Even under Rule 10B of the IT Rules, the factors prescribed for inclusion or exclusion of comparables to determine the ALP are also based on the comparison of the assessee with the chosen entities and the AE has no role in the exercise of selecting the comparables. Thus, in our view, the interest that would have been earned by the assessee by advancing or placing the said amount with unrelated parties would be the Arm's Length interest in relation to the interest free loans/advances to the AE. The safest comparables, which can be taken as Arm 's Length interest rate in such a case would be the interest on FD with the bank for a term equivalent to the term for which the loans given to the AEs.*
>
> *8.12 It is pertinent to note that in case of FD with the Bank, the investment is safe as it is free from risk of credit and interest. On the other hand, if the loan/advance is given to the unrelated party, then always there is some risk of credit and interest involved in such transaction. There is one more reason for taking the FD as an appropriate and good comparable because the lending rate by financial institutions/bank varies depending upon the credit rating of the borrower and further on the guarantee and security provided to secure the loans".*

In view of the above observations it may be noted that FD rate has been considered to be one of the methods for benchmarking international transactions relating to interest receivable. Further risk factor has to be considered looking to the fact that the fixed deposits

are very secure being with banks as compared to loan advanced to parties like AE of the appellant. Since there is risk associated with the unsecured loan, one has to take into account the risk while deciding ALP. Taking into consideration all the kinds of Risk associated with such transaction like Forex risk, Country risk, Entity risk, and circumstances further mark up may be added. Similar observations were made by Hon'ble ITAT Mumbai vide their order dt 16.11.2012 in the case of Wipro Ltd. vs. DOT 33 taxmann.com 263. Considering all these facts the rate of 6% for charging interest is held to be reasonable and consequently adjustment made by the TPO is upheld."

22. Before us, Ld. Counsel for the assessee submits that during the F.Y.2008-09 assessee had advanced zero coupon i.e. optionally convertible loan [hereinafter in short "OCL"] pursuant to the loan agreement dated 28.01.2008 and no interest was charged by the assessee for the reason that RLSI was setup for developing global business opportunities in the field of pharmaceuticals, bio-pharmaceuticals, clinical, research services and research and development activities. The assessee intended to fulfill its own objective of gaining majority control in such overseas acquisitions made through him**.** Ld. Counsel for the assessee submits that as per clause (3) of the loan agreement, the loan was zero coupon and was optionally convertible into share capital at the option of the lender at a fair value to be determined at the time of conversion as per the terms of the loan agreement. Ld. Counsel for the assessee submits that as on 31.03.2011 RLSI has converted the entire loan amount outstanding in its books into paid in equity capital and this can be verified from the CPA certificate dated

12.10.2011 which is placed at Page No. 220 of the paper book. Therefore, Ld. Counsel for the assessee submits that the TPO disregarding submissions of the assessee adopted interest rate of 6% per annum as arm's length price rate of interest, which was charged by the assessee in respect of loan provided to its another AE i.e. M/s. Reliance Life Sciences BV [hereinafter in short "RLSBV"]. Ld. Counsel for the assessee further submits that no adjustment for interest should be made in respect of the said convertible loan provided to RLSI which has been entirely converted into paid in equity capital in subsequent year.

23. Ld. Counsel for the assessee further submits that erroneous benchmarking has been adopted by the TPO while determining arm's length price. Ld. Counsel for the assessee submits that the TPO has failed to determine the arm's length price of the optionally convertible loan on the basis of one of the methods prescribed u/s. 92C of the Act. It is submitted that the TPO adopted interest rate of 6% per annum charged by the assessee on the loan provided to another AE i.e. RLSBV which is a controlled transaction, as the arm's length price, which is not on the basis of any of the prescribed methods. Ld. Counsel for the assessee submits that adhoc determination of arm's length price by TPO dehors section 92C of the Act cannot be sustained. It is further submitted that arm's length price cannot be determined on the basis of another controlled

transaction i.e. transaction with another AE. It is submitted that u/s. 92C of the Act arm's length price can be determined only on the basis of independent and uncontrolled transactions. Reliance was placed on the decision of the Hon'ble Bombay High Court in the case of CIT *v.* Lever India Exports Ltd., in ITA.No. 1306, 1307 and 1349 of 2014 dated 23.01.2017 and CIT *v.* Merck Ltd., in ITA.No. 272 of 2014 dated 08.08.2016.

24. Ld. Counsel for the assessee further submits that the approach of TPO in adopting controlled transaction to benchmark another controlled transaction is rejected by the Hon'ble Jurisdictional High Court in the case of ADIT *v.* Barclays Bank Plc. In ITA.No. 584/Mum/2012 dated 12.01.2018. It is further submitted by the Ld. Counsel for the assessee that when TPO failed to adopt one of the prescribed methods of the Act, the matter cannot be restored to the file of the assessing officer. Reliance was placed on the decision of the Hon'ble Bombay High Court in the case of CIT *v.* Johnson & Johnson Limited in ITA.No. 1291 of 2014 dated 03.04.2017 and CIT *v.* Kodak India Pvt. Ltd., in ITA.No. 15 of 2014 dated 11.07.2016.

25. Without prejudice to the above, the Ld. Counsel for the assessee submits that interest free OCL is not a loan simplicitor and no interest

should be imputed. Ld. Counsel for the assessee submits that assessee intended to fulfill its own objective of gaining majority control in overseas acquisitions made through its AE, but intention was always to invest in equity and there was no intention to provide loan to earn any interest and as on 31.03.2011 the outstanding loan has been converted into paid in equity capital. It is further submitted that OCL is in the nature of quasi capital and not a routine loan simplicitor. It creates a valuable right in the hands of the lenders and the substantive reward is not interest but opportunity to own capital which in itself is a valuable right and which cannot be disregarded in determining the arm's length price by comparing the transaction with other simplicitor loan transactions.

26. Ld. Counsel for the assessee submits that identical issue came up in the case of DCIT *v.* Cadila Healthcare Ltd., in ITA.No. 2430/AHD/2012 dated 11.10.2013 wherein the assessee has subscribed to OCL issued by AE and no interest was payable in case the loan was convertible into equity within a period of five years from the date of disbursement. The TPO held that this OCL to be in the nature of debt and made adjustment for interest. Hon'ble Tribunal affirmed the order of the Ld.CIT(A) wherein it was held that the assessee had not granted the loan but invested in OCL and held it to be at arm's length.

27. Ld. Counsel for the assessee further submits that in the case of DLF Hotel Holdings Ltd *v.* DCIT in ITA.No. 6336/Del/2012 dated 30.06.2016 the Tribunal held that the quasi capital cannot justifiably be treated as debt simplicitor and deleted interest on the interest free loan given by the assessee to its subsidiary which was converted into equity.

28. Further reliance was also placed on the decision of the Ahmadabad Bench of the Tribunal in the case of Micro Inks Ltd *v.* ACIT in ITA.No. 1688/AHD/2006 dated 06.08.2013 reported in 92 DTR 186 wherein the Ahmadabad Bench while deciding arm's length price of advance given by holding Company to its wholly owned subsidiary, held that, on pure commercial factors, CUP for interest on such transaction where subsidiary plays strategically commercial role in assessee's business would be Nil. It is submitted that the Tribunal deleted the adjustment holding that the interest was not applicable in the said case. It is submitted that similar view is upheld in the case of Prithvi Information Solution Ltd *v.* ACIT in ITA.No. 1816/HYD/2012 dated 08.08.2014 by the ITAT Hyderabad Bench.

29. We have heard the rival submissions and perused the orders of the authorities below. It is an undisputed fact that the assessee advanced optionally convertible loans to its AE i.e. RLSI. It is not in dispute that the

OCL has been converted into Equity in subsequent years before the due date and before the prescribed date as agreed in the agreement. Assessee has charged no interest on OCL for the reason that RLSI was setup for developing global business opportunities in the field of pharmaceutical and bio-pharmaceutical, clinical research services and research and development activities. The assessee intended to fulfill its own objective of gaining majority control in such overseas acquisitions made through AE, for this reason assessee did not charged any interest on the investment made in its AE in the form of OCL. We also observe that as on 31.03.2011 RLSI has converted the entire loan amount outstanding in its books into paid in equity capital. We find that more or less on identical situation the Ahmadabad Bench in the case of DCIT *v.* Cadila Healthcare Limited (supra) held as under: -

> *"7. We have heard the rival submissions and perused the material on record. CIT(A) while deleting the addition has noted that as per the agreement, the interest was payable only if the conversion option was not exercised on the expiry of 5 year period. If at any time during the 5 year period conversion option was exercised and the loan was converted into equity, no interest accrued or become payable. He further noted that the funds were provided by the Assessee as per RBI guidelines and in the immediately next year, the entire loan given to subsidiary was converted into equity shares of Zydus International Pvt. Ltd. He has further held that since the Assessee has converted the loan into equity in the immediate next year, there was no question of taxing notional interest. He has further held that Assessee had not granted interest free loan but invested in optionally convertible loan with a clause of interest in case, Conversion option was not exercised and further held the Assessee's transaction with subsidiary was at arms length. Before us, the Revenue could not controvert the findings of CIT(A) by*

bringing any contrary material on record. In view of these facts, we find no reason to interfere with the order of CIT(A).

30. Similarly, in the case of Micro Inks Ltd *v.* ACIT (supra) the Ahmadabad Bench of the Tribunal held as under: -

"15. In the case before us now, there are two important factors pertaining to this interest free loan, and both of these aspect deserve to be examined in some detail. The first important aspect of this interest free advance is that the loan is said to be in the nature of quasi capital, and it was so given because out of EEFC (Exchange Earners Foreign Currency) account, while the assessee could have given loan upto US $ 50 million, it was not open to the assessee to subscribe to the equity capital without the permission of the Reserve Bank of India. There was thus, unlike the case of Perot Systems (supra) discussed above, indeed a technical problem in subscribing to the capital directly. It is also important to note that immediately upon obtaining the permission of the Reserve Bank of India, which assessee did obtain at later stages, the advances were converted into shares. Except for an amount of US $ 10,000, entire advances received by the step down subsidiary were converted into shares. It is also not in dispute that when RBI permission to convert loan into equity was sought it was sought effective from the date on which remittance was made. The second very important aspect of this interest free loan is this. In the present case, the entity receiving the interest free advances is not only a wholly owned subsidiary of the assessee company but is also playing a very significant role in its sale and distribution chain inasmuch as the assessee is sole vendor to the said concern so far as sales of raw material and semi finished goods is concerned, and it has a significant volume of transaction at almost 50% of entire sales and 90% of entire exports. Micro USA exists only to facilitate the marketing of assessee's products in US markets. The relationship on account of lending of money cannot thus be considered in isolation with these crucial business considerations. In this regard, it is useful to refer to the following extracts from the annual financial statements of Micro USA:

<u>Assessment year 2002-03</u>

In June 2000, the company entered into a loan agreement with HIRL and issued a note payable to HIRL. The note origina lly bore interest @ 9% and was due in five equal annual instalments, including interest accrued to the date of payment, beginning May 31, 2002 and ending May 31, 2006. In 2002, this note, with a balance of US $ 2,640,000 was forgiven by HIRL and converted to equity as a capital contribution. During the year ended March

31, 2002, the company borrowed an additional US$ 3,170,000 from HIRL. Purchase of raw materials from HIRL were approximately US$ 47.48 million for the year ended March 31, 2002. The company pays HIRL for these materials 165 days from the bill of lading date. These purchases formed the majority of company's inventory expenditure for the year ended March 31, 2002.....

Assessment year 2003-04

The company has an outstanding interest free loan payable to HIRL amounting to US$ 3,170,000 at March 2003. This loan is payable on demand and has therefore been classified as short term.

The company purchased approximately US $ 40.12 million of materials from HIRL for the year ended March 31, 2003. The company pays HIRL for these materials 165 days from the bill of lading date. These purchases account for the majority of the company's inventory expenditure for the year ended March 31, 2003. .....

Assessment year 2004-05

The company had an outstanding interest free loan payable to HIRL amounting to US$ 3,170,000 at March 31, 2003. The company also received an additional interest free loan of US $ 1,000,000 in September 2003. Pursuant to the unanimous written consent of the Board of Directors' resolution dated February 27,2004, US $ 4,160,000 of the above loan was converted into Series A Preferred Stock and the remaining US $ 10,000 was repaid to the parent in March 2004.

The company purchased approximately US $ 34.13 million and US$ 40.12 million of materials from HIRL for the year ended March 31, 2004 and 2003 respectively. The company pays HIRL for these materials 165 days from the bill of lading date. These purchases account for the majority of the company's inventory expenditure for the year ended March 31, 2004 and 2003 respectively. .....

16. It is also important to bear in mind the fact that at the relevant point of time the assessee could not have invested in the shares of the step down subsidiary, without the permission of the Reserve Bank of India – as is uncontroverted stand of the assessee, and, therefore, the assessee could not also have, without the permission of the Reserve Bank of India, entered into loan agreements with a provision of conversion of such loans equity either. It is only

elementary legal position that what could not have been done directly could not have done indirectly also. There is thus not much of a merit in the stand of the revenue authorities that in the absence of a specific mention about conversion of loan into equity, it cannot be presumed that the interest free loans could not have been in the nature of quasi capital. As to the position that the relationship between the assessee and Micro USA was not of a lender and borrower simplicitor – a relationship which is essence of a loan transaction, it will be clear from the following observations in the annual financial statement of Micro USA :

..... As of March 31, 2002, the company had generated an accumulated deficit of US $ 27.48 million and had a net w orking capital surplus of US $ 3.31 million. Net cash used in operating activities for the year ended March 31, 2002 was US $ 39.49 million.

Until the management is able to achieve its plan for profitable future operations, the company continues to be dep endent upon the availability of financial support from HIRL, including assistance in negotiating and guaranteeing debt arrangements with company's banks. Such financial support may be subject to the approval of Reserve Bank of India. HIRL has pledged its financial support to the company through March 31, 2003. The company has a US $ 3,170,000 note payable to HIRL and HIRL either guaranteed or secured all of the company's outstanding debts at March 31,2002. HIRL is company's principal supplier of raw materials.

.....

During the next twelve months, ending March 31, 2004, US $ 12.70 million of debt must be paid or refinanced, and US $ 29 million is payable to the parent. The company expects to meet these obligations with the continued support and guarantees of the parent

.....

During the next twelve months, ending March 31, 2005, US $ 19.42 million of debt must be paid or refinanced, and US $ 12.48 million is payable to the parent. The company expects to meet these obligations with the continued support and guarantees of the parent

17. As is evident from the above discussions, the relationship between the assessee and its step down subsidiary Micro USA was simply that of a lender and a borrower. Not only the Micro USA was a significant part of the marketing apparatus of the assessee, and the assessee and the Micro USA had significant commercial relationship on that count, the assessee was a de facto and de jure promoter of the Micro USA. In the light of this undisputed position,

an d in the light of the admitted position that, even as per revenue authorities, the transaction is at best for advance of money by holding to step down subsidiary , let us examine the correctness of the arm's length price adjustment in this cas e. In such a case, CUP method can be applied and the LIBOR or other bank rate linked rate is generally taken as a rate for comparable uncontrolled transaction. As has been held in a large number of cases, including in VVF (supra) and Perot Systems (supra), in the cases of arm's length prices of loans and advances, costs of funds have no relevance and it is only the rate applicable for comparable uncontrolled transaction that is to be taken into account. However, even while applying CUP method, one has to bear in mind the fact that in terms of Rule 10B (1) computation of ALP under the CUP method is a three step process which requires that

> *(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 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 arms length price in respect of the property transferred or services provided in the international transaction;*
>
> *(Emphasis by underlining supplied by us)*

18. Therefore, even when we take LIBOR plus rate as the base rate for an advance in step 1 of the above computation process, such base rate will have to adjusted inter alia for the differences…….. (a) between the international transaction and the comparable uncontrolled transaction, and (b) between the enterprises entering into such transactions, which could materially affect the price in the open market". On both of these counts, adjustments will have to be necessarily made in the LIBOR plus rate. While the international transaction before us is that of advancing an interest free unsecured loan for helping a entity overcome its teething problems and pending the approval for capital subscription is received from the Reserve Bank of India, a typical LIBOR plus rate transaction is the transaction in which banks gives secure advances, for making profits out of so lending the money, to its customers. Strictly speaking, there is no parity between these two types of transactions. Secondly, we are dealing with a situation in which the two enterprises are mutually dependent for commercial reasons. While Micro USA is dependent on the assessee for its sheer existence, the assessee is dependent

on Micro USA for its business. Let us assume for a while that Micro USA is unconnected with the assessee so far as its management, capital and control is concerned, but even then and without this management, capital and control relationship, the assessee, as an independent enterprises, will make sense in giving interest free advances to Micro USA so as to ensure its continued market access in USA and for other commercial reasons. This is quite unlike a typical transaction on LIBOR plus rate in which only motivation for giving advance is earning interest. Clearly, thus, LIBOR plus rate cannot be adopted in this situation for two fundamental reasons – (i) first, that it is not a simplictor financing transaction between the assessee and Micro USA, as it is a transaction of investing in a step down subsidiary as quasi capital pending formal capital subscription with the approval of Reserve Bank of India; and (ii) second, that it is not a case of granting advance to a business concern without significant and decisive commercial considerations, as the monies are given for strengthening assessee's marketing apparatus in US and to keep alive its biggest exports customer. There is a difference in the nature of transaction and there is also a difference in the nature of the enterprises, including their inter se commercial relationship, entering into this transaction. The differences are so fundamental that these differences, to use the phraseology employed in Rule 10 B (1)(a)(ii), "could materially affect the price in the open market". On account of these peculiar factors, the application of LIBOR plus rate or, for that purpose, any bank rate will be inappropriate to this case.

19. The next logical question, therefore, is as to what would be the price at which such interest free advances coul d be given in comparable uncontrolled transactions. In other words, in case the assessee and the Micro USA were not associated enterprises in legal sense of that expression, at what rate the assessee would have granted advances pending approval for capital subscription in a company which is playing such a vital role in its business plans. It is so for the reason, as we begun by pointing out, the whole purpose of the arm's length price adjustment is to nullify the impact of management, capital and control interrelationship between the associated parties. In our humble understanding, on the pure commercial factors and notwithstanding the management, capital and control relationship between the parties, such non interest bearing advances were equally justified even if the assessee and Micro USA were independent enterprises. Of course, we are alive to the fact that but for the management, capital and control interrelationship, Micro USA could not have played such a strategically significant role in assessee's business but then right now we are concerned with a comparable uncontrolled transaction between independent enterprises, in which all other factors, except the commonality of management, control and capital, remain the same. The comparable uncontrolled price for interest on such a

transaction in which advances are made pending capital subscription in a company which plays strategically significant commercial role in assessee's business , in our considered view, would be nil. The levy of interest would not come into play in such a case, except to the extent of refund of US $ 10,000 for which no shares were allotted. When it was so pointed out during the hearing, learned counsel for the assessee very fairly did not press his grievance to the extent of this amount. In the light of these discussions, the variations in the nature of transactions between the assessee and Micro USA and variations in the nature of relationship between the assessee and Micro USA are so fundamental that the entire LIBOR plus rate, which was the starting point of our computation of ALP of these interest free loans, is to be reduced to zero to take care of the differences in terms of Rule 10B(1)(a)(ii) of the Income Tax Rules. The impugned ALP adjustment, to this extent and in the terms i ndicated above, is unsustainable in law and we delete the same."

31. In the case of DLF Hotel Holdings Ltd *v.* DCIT (supra) the Delhi Bench of the Tribunal held as under: -

"7. We have heard the rival submissions and perused the material available on record. It would be appropriate to first bring out the salient facts from the orders available on record. It is seen that the assessee made the following disclosure in its Form No. 3CEB:-

S.No.	***Nature of transaction***	***Method used by Assessee***		***Value of Transaction (USD)***
		Method	***PLI***	
1.	*Interest free loan*	*NA*	*NA*	*72,580,000*

7.1. The advancing of interest free loan of USD 72580000 to its AE, DLF Global Hospitality Ltd., Cyprus (DHHL/DLF) Cyprus has been reflected as an interest free loan of Rs.2,91,99,60,465. The relevant extract from the TPO's order addressing the specific date and amounts on which the loans were given is reproduced hereunder:-

"It is seen from the Form No.3CEB and Transfer Pricing Study that the assessee company has advanced loans to its AE in Cyprus, DLF Global Hospitality Limited, as per the table below:-

Date of initial Loan to DGHL	***Loan (US $) DHHL-DGHL***	***Amount in INR***
30.07.2007	*51,000,000*	*2,069,582,692*
18.09.2007	*500,000*	*20,306,910*

Date of initial Loan to DGHL	***Loan (US $) DHHL-DGHL***	***Amount in INR***
20.11.2007	*16,000,000*	*629,918,780*
11.12.2007	*5,080,000*	*200,152,084*
		2,919,960,466

7.2. The assessee in support of its claim has stated before the TPO that the loan was advanced with the intention of converting it into equity and has shown that it was converted into equity within 3 months. The assessee as per record has explained that the loan was so structured as the assessee was not sure of the subsidiary company's capacity to utilize the funds for the intended purposes. It has been argued that on the utilization of the funds it was capitalized as equity hence it has been explained that it was never a loan and was always a quasi debt. For ready-reference the relevant extract from the TPO's order incorporating the explanation of the assessee is reproduced hereunder:-

> *"As per the "Notes to Form 3CEB" it is stated that "in respect of interest free loan to the associated enterprises, even though the Company granted a loan initially the intention was to always invest and convert the funds to equity within short period of time. The debt funds were converted to equity with in short period of three months. The Company opted for debt only to retain some flexibility to get its money back in case the associate enterprise is not able to utilize the funds from the intended purpose. However, once the associated enterprise utilized the funds for intended purpose, the debt amount was capitalized by issuing equity shares to the Company. Hence, given that the nature of debt was quasi-debt, the transaction involving granting interest free loan can be considered to be at arm's length as provided under Section 92C of the Act."*

7.3. It is seen from the record that the said explanation was not accepted by the TPO who rejected it holding as under:-

> *"From the above statement it is clear that no benchmarking has been carried out in respect of these loans. The fact that the decision regarding the treatment of this amount as loan or debt was to be taken when it was felt this amount could be utilized for the purpose for which it was intended, clearly shows that it was a loan. As no independent enterprise would extend an interest free loan to a third party this action is obviously not in keeping with the arm's length principle, as enunciated in the transfer pricing guidelines as per the Income Tax Act. The arm's length interest is determined by following*

the CUP method, wherein the interest rate is determined under the circumstances in which the tax payer and its subsidiaries are operating i.e. what is the interest that would have been earned if such loans were given to unrelated parties in similar situation as that of subsidiaries. Since the tested party is the tax payer, the prevalent interest that could have been earned by the tax payer by advancing a loan to an unrelated party in India, with the same weak financial health as that of the tax payer 's AE, will be considered.

2. As mentioned above, under the CUP method, the interest that is charged between unrelated parties under similar circumstances would be the arm's length interest. The main issue is to decide the interest rate at which the tax payer would have earned, in advancing loan of above amounts to unrelated third parties with similar financial strength as that of the AE. It is also to be mentioned that there is no security provided by the AE's /subsidiaries against the loans advanced."

7.4. The following extract brings out the reasoning of the TPO justifying the application of the rate which has been upheld by the DRP and heavily relied upon by the Ld.CIT. DR:-

3. "Financial institutions generally weigh four elements in determining whether or not to issue loans and, if so, at what conditions and fees:

Financial Risk: In order to gauge the financial risk incurred by the lender, the debtor's financial position is reviewed based on its balance sheet and income statement;

Credit Risk: In order to gauge the credit risk, three elements are weighed, namely the availability of guarantees, the purpose of the loan and the loan's term to maturity;

Business Risk: The lender's views on the industry in which the debtor operates its business is reflected in this risk; and

Structural Risk: In gauging this risk, the qualifications of external rating agencies awarded to the debtor are weighed.

4. Corporate bonds issued by companies in India also give an indication of interest that could be earned if the amount is

lent to the companies. Government bonds are subject only to interest rate risk. However, corporate bonds are subject to credit risk in addition to interest rate risk. Interest rate risk refers to the risk of a bond changing in value due to changes in the structure or level of interest rates. The credit risk of a high yield bond refers to the probability of a default (i.e., debtor unable to meet interest and principal obligations) combined with the probability of not receiving principal and interest in arrears after a default. A credit rating agency attempts to describe the risk with a credit rating such as AAA. In India, CRISIL is the leading credit rating agency. The rating scales vary; the most popular scale uses (in order of increasing risk) ratings of AAA, AA, A, BBB, BB, B, C, with the additional rating D for debt already in arrears. Government bonds are often considered to be in a zero-risk category i.e. above AAA; and categories like AA and A may sometimes be split into finer subdivisions like "AA-". Bonds rated BBB and higher are called investment grade bonds. The safety level of these grading, as adopted by CRISIL, are as under:

AAA (Triple A) Highest Safety	*Instruments rated 'AAA' are judged to offer the highest degree of safety, with regard to timely payment of financial obligations. Any adverse changes in circumstances are most unlikely to affect the payments on the instrument.*
AA (Double A) High Safety	*Instruments rated 'AA' are judged to offer a high degree of safety, with regard to timely payment of financial obligations. They differ only marginally in safety from AAA ' issues.*
A Adequate Safety	*Instruments rated 'A' are judged to offer an adequate degree of safety, with regard to timely payment of financial obligations. However, changes in circumstances can adversely affect such issues more than those in the higher rating categories.*
BBB (Triple B) Moderate Safety	*Instruments rated 'BBB' are judged to offer moderate safety, with regard to timely payment of financial obligations for the present; however, changing circumstances are more likely to lead to a weakened capacity to pay interest and repay principal than for instruments in higher rating categories.*

BB (Double B) Inadequate Safe	*Instruments rated 'BB' are judged to carry inadequate safety, with regard to timely payment of financial obligations; they are less likely to default in the immediate future than instruments in lower rating categories, but an adverse change in circumstances could lead to inadequate capacity to make payment on financial obligations.*
B High Risk	*Instruments rated 'B' are judged to have high likelihood of default; while currently financial obligations are met, adverse business or economic conditions would lead to lack of ability or willingness to pay interest or principal.*
C Substantial Risk	*Instruments rated 'C are judged to have factors present that make them vulnerable to default; timely payment of financial obligations is possible only if favourable circumstances continue.*
D Default	*Instruments rated 'D' are in default or are expected to default on scheduled payment dates*

5. From the above, it is seen that bonds in the rating range of AAA to BBB have some kind of safety, with a minimum level of 'moderate safety' (BBB). Therefore, it is clear that 'unsecured loan', like that of taxpayer, cannot fall in the credit rating range from AAA to BBB, as the unsecured loan advanced by the taxpayer is not backed by any guarantee or security.

Under the facts and circumstances of the case and also considering the financial health of the AE of the taxpayer, it would be reasonable to consider that the loan advanced by the taxpayer would fall somewhere between BB and D ratings. Information about the average yield on long term instrument during FY 2007-08 was collected u/s 133(6) of the IT Act from M/s CRISIL."

7.4.1. Accordingly, Considering the information received from CRISIL which is the Credit Rating Agency in India where the ratings were ranging from AAA; AA+; AA-; BB; BBB; BBB-; BBB; A+; A- to A the TPO was of the view that the assessee's case was to be considered ranging between the range of BB to D where either there is no safety or the safety is inadequate. In the said range, BB rate it was noted denotes the highest level of safety or in other words minimum level of risk. The annual average yield for BB rated bonds for 5 years was calculated at 17.26% and it was held that 17.26%

rate of interest appeared to be most reasonable and appropriate which was proposed to be applied on monthly closing balances from the period 01.04.2007 to 31.03.2008.

7.5. It may be pertinent to consider the purpose of the interest free loan to the AE as per the reply of the assessee before the TPO and the DRP. A perusal of the record shows that on behalf of the assessee the following reply was given:-

> *5. Reply of the Assessee: The assessee has stated that this amount was in the form quasi equity since it was the intention of the assessee was to convert it into equity capital from the very beginning. It also states that to maintain flexibility, in case the funds were not used for the intended activity within the proposed period, it was initially granted as debt.*
>
> *It states that DHHL, being the parent company undertakes stewardship activities through the provision of funds and is not required to be compensated.*
>
> *It is stated that being a new entity, DGHL could not have accessed funds from any other source. This quasi equity was converted into equity and this became the basis to borrow from third party banks.*
>
> *The assessee has stressed on the commercial expediency of the transaction.*
>
> *The assessee has objected to the use of S.133(6) to gather information stating that it might not be authentic, it is not available in the public domain and it is like using secret comparables." (emphasis provided)*

7.6. The assessee's objection that the TPO cannot question the commercial expediency of its activities was not accepted by the TPO. The TPO was of the view that the OECD guidelines clearly held the view that "when independent enterprises transact with each other, the conditions of their commercial and financial relations (e.g. the price of goods transferred or services provided and the conditions of the transfer or provision) ordinarily are determined by market forces. When associated enterprises transact with each other, their commercial and financial relations may not be directly affected by external market forces in the same way, although associated enterprises often seek to replicate the dynamics of market forces in their transactions with each other. (OECD para 1.2).

7.6.1. The TPO was of the view that the OECD Guidelines say that the relationship among members of an MNE group may permit the

group members to establish special conditions in their intra group relations that differ from those that would have been established had the group members been acting as independent enterprises operating in open market. Thus, intra group transactions he noted needed to be examined in the light of the special provisions contained in Chapter X of the Act and not merely in the context of section 37(1). He was further of the view that there were several highly relevant issues requiring consideration, namely whether the transaction was really a commercial one; whether in similar circumstances an independent person would have paid similar amount; whether the taxpayer really needed the services; whether the taxpayer really got some tangible or direct benefit; whether the amount paid was commensurate with the benefit (or the expected benefit) from such services, etc. We need not directly address the entire sweep of issues referred to by the TPO at this stage. Suffice it to say that the said broad sweeping view of the tax authorities has not been approved judicially by various High Courts. Thus though we have quoted the view expressed by the TPO. We take note that it is not the correct view as admittedly in various decisions including CIT vs Cushman & Wakefiled India Pvt.Ltd. of the Delhi High Court, the view expressed by the TPO does not have judicial acceptance.

7.7. The TPO concluded that the benefit of conversion into equity could be granted only to the extent of 20% of the loan. We find no rationale has been brought out in the order for arriving at this magic figure of 20%. In order to decide what rate of interest was to be charged to the remaining amount. Information u/s 133(6) was obtained over ruling the objections of the assessee who had pleaded that no such powers were vested with the TPO. We find that the TPO's conclusion that section 92C(3) authorized him to use the information in his possession and the power to gather material under the said provision was similar to the power vested with the AO in the proceedings under section 143(3) was correct as the wording is almost the same in both the sections i.e. 92CA(3) and 143(3). Further we find that the view that subsection (7) of section 92CA empowers the TPO to utilize the same under section 133 (6)/131 and any falsity in the information given under the provisions of the Income Tax Act, 1961 is liable for penal action. Accordingly, we find that the conclusion drawn by the TPO that he had the power to seek information u/s 133(6) in principle is the correct view in law and the conclusion so drawn by the TPO is upheld by us. Whether the same was necessitated or relevant on facts before us is an area which, if need be, shall arise later.

7.8. To revert back to the proceedings before the TPO the record shows that he concluded the issue in the following manner:-

"In view of the above discussion, while the assessee will be given benefit of conversion of the loan into equity during a reasonable time frame, the benefit will be limited to 20% of the loan. The rest will be treated as a loan on which an appropriate interest, as determined in the show cause notice, needs to be charged. The calculation of the same is as under:-

month End	***Opening balance (Rs.) (after taking to account the revised closing^ balance)***	***Funds extended (Rs.)***	***Conversion into Equity (Rs.)***	***Closing balance (Rs.) (as per assessee)***	***Closing balance after allowance for 20% (as per TPO)***	***Revised interest @ 17.26%***
7 -Apr						
7-May						
7- June						
7 -July		*2,069,582,691*		*2,069,582,692*		*29,767,498*
7-Auq	*2,069,582,692*			*2,069,582,692*		*29,767,498*
7-Sep	*2,069,582,692*	*20,306,910*		*2,089,889,602*		*30,059,579*
7-Oct	*2,089,889,602*		*2,069,582,692*	*20,306,910*	*1,675,973,064*	*24,106,079*
7-Nov	*1,675,973,064*	*629,918,780*		*650,225,690*	*2,305,891,844*	*33,166.411*
7-Dec	*2,305,891,844*	*200,152,084*		*850,377,774*	*2,506,043,928*	*36,045,265*
8-Jan	*2,506,043,928*			*850,377,774*	*2,506,968,373*	*33,599,012*
8-Feb	*2,506,043,928*		*850,377,774*	*Nil*	*2,335,968,373*	*33,599,012*
8-Mar	*2,335,968,373*			*2,335,968,373*	*2,335,968,373*	*33,599,012*
Total						*286,155,618*

7.9. On a perusal of the objections posed by the assessee before the DRP, it is seen that findings of the TPO were assailed on various ground including the ground that the TPO has treated the loan as loan simplicitor and as a pure debt instrument and not as an instrument of hybrid funding having traits of equity. The alleged modification misconstruing of facts by the TPO was assailed to be incorrect and misleading. Extracts from these Objection numbering 5.2.2 and 5.2.3 which has further being elaborated in Objection 5.2.9 before the DRP are extracted hereunder:-

> *5.2.9. Factual and legal arguments against the addition proposed by the Learned TPO*
>
> *……*
>
> *"A category of debt taken on by a company that has some traits of equity, such as having flexible repayment options or being unsecured. Examples of quasi-equity include mezzanine debt and subordinated debt."*
>
> *The definition/meaning of subordinated debt is provided as under:*

"Debt that is either unsecured or has a lower priority than that of another debt claim on the same asset or property, also called junior debt."

The assessee entered into a written arrangement in the form of agreement with its associated enterprise that the funds provided would be in the nature of quasi equity and not in the nature of debt. In assessee's case, it was clear that the funds would be converted into equity within the next 3 to 4 months which clearly reflects that it was actually meant to be a capital contribution.

The support was also sought by the assessee from the guidelines issued by the Organisation for Economic Cooperation and Development on Transfer Pricing in 2010 ("OECD Guidelines"), an extract of which is appended below:

"D.2 Recognition of the actual transactions undertaken

1.64. A tax administration's examination of a controlled transaction ordinarily should be based on the transaction actually undertaken by the associated enterprises as it has been structured by them, using the methods applied by the taxpayer insofar as these are consistent with the methods described in Chapter II. In other than exceptional cases, the tax administration should not disregard the actual transactions or substitute other transactions for them. Restructuring of legitimate business transactions would be a wholly arbitrary exercise the inequity of which could be compounded by double taxation created where the other tax administration does not share the same views as to how the transaction should be structured.

1.65. However, there are two particular circumstances in which it may, exceptionally, be both appropriate and legitimate for a tax administration to consider disregarding the structure adopted by a taxpayer in entering into a controlled transaction. The first circumstance arises where the economic substance of a transaction differs from its form. In such a case the tax administration may disregard the parties' characterisation of the transaction and re-characterise it in accordance with its substance. An example of this circumstance would be an investment in an associated enterprise in the form of interest-bearing debt when, at arm's length, having regard to the economic circumstances of the borrowing company, the investment would not be expected to be structured in this way. In this case it might be appropriate

for a tax administration to characterise the investment in accordance with its economic substance with the result that the loan may be treated as a subscription of capital.

From the above, it can be clearly inferred that the funds provided by DHHL to DLF Cyprus can be considered to be quasi equity/capital requiring no interest payment in return.

While there is no guidance available in the Indian Transfer Pricing Regulations, guidance issued by the ATO in Taxation Ruling TR 92/11 may also be referred to in this regard. It clearly states that contributions made or amounts extended by one company to the other may be considered as equity. The relevant extracts from the stated ruling is provided below:

> *"60. In the context of applying Australia's transfer pricing rules, the principal factors that will be taken into account in determining whether a particular loan agreement should be treated as equivalent to a contribution to equity are detailed below....."*

7.10. The reproduction of the following extract of Objection No.5.3.9 further brings out the fact that the tax payer justified its action of advancing of loan as a shareholders activity guided by commercial expediency etc.:-

5.3.9. Factual and legal arguments against the addition proposed by the Learned TPO

"During FY 2007-08, since DLF Cyprus was a newly formed company, it could not manage to obtain funds initially from third parties. Hence, in order to further the business objectives of DLF Cyprus, the assessee advanced loans in the form of quasi equity to retain control and have absolute ownership of profits subsequent to conversion.

In addition to the above, assessee wishes to submit that after the conversion of the quasi-equity into equity, DLF Cyprus was able to secure additional funds from third party banks. This was critical for DLF Cyprus since the additional funds were required for completion of acquisitions, and the independent banks would not have provided any funds to DLF Cyprus without it having an acceptable debt/equity ratio. The third party banks which may have refrained from providing loans to DLF Cyprus at the time of set-up, advanced loans to DLF Cyprus only on the basis of restructured capital gearing of the company.

The assessee wishes to submit that it was commercially expediency which necessitated DHHL to provide advances to DLF Cyprus. These advances were made as a part of capital for further investment by its associated enterprise and to obtain return in future. The assessee had full control over its associated enterprise which reduces the credit risk."

(emphasis provided)

7.10.1. Elaborating the argument that by way of this funding the assessee was engaged in stewardship activities, the following submissions have been advanced:-

"As explained above, stewardship activities do not require any payment since they directly benefit the shareholder, and in an independent scenario, a recipient of any corresponding benefit would not have been required to pay any charge for the same.

In the instant case, since DHHL is the sole shareholder in DLF Cyprus, the provision of funding may be considered to be part of its shareholder activity, since it is providing support to its subsidiary as a shareholder. Additionally, any benefit accruing to DLF Cyprus from use of the funds is eventually transferred/ added to the value of DHHL as sole shareholder. Hence, it may be concluded that granting of funds by DHHL is for its own benefit, and hence, DLF Cyprus is not required to pay any interest on the same.

The Hon'ble Panel would appreciate that the aforesaid assistance provided by the Assessee is necessary and expedient given the facts of the instant case." (emphasis provided)

7.11. In the above facts, submissions and arguments advanced on behalf of the assessee, we find that the consistent claim of the assessee has been that it had aims and goals focused towards building its portfolio in premium segment hotels, resorts, serviced apartments, family recreational clubs in major cities and tourist destination. The decisions so taken had been guided by a vision to make its mark globally in countries like Sri Lanka, Thailand, Moracco, Bhutan, France, USA, Indonesia etc. We find that this is an accepted position as brought out from the following extract from the TPO's order itself which forms a part of the final assessment order also :-

4.2. "DHHL was set up on 31 August 2006 as an integrated hospitality development and ownership company focused on

premium segment hotels, resorts, serviced apartments, and family recreational clubs- DHHL has a vision to be. India's leading hospitality development and asset Ownership Company, and amongst the largest such companies globally. The company has been established as the hospitality arm of DLF Limited, which is its holding company. The company develops, acquires, finances and actively manages a rapidly growing hospitality portfolio. With approximately 6,000 rooms under current development in most major cities and tourist destinations in India, DHHL is on track to create a portfolio of 25,000 rooms in the next 5 years.

DLF Hotels recently acquired controlling stake in Amanresorts, one of the pre-eminent and most innovative luxury hotel groups in the world. "Aman" - an outstanding brand and winner of over 500 awards since 1968, such as Conde Nast, "The Gold List", Gallivanter's Guide "Best Hotel Worldwide" etc. - owns and operates 18 boutique resorts across countries such as Indonesia, Thailand, Sri Lanka, India, Morocco, Bhutan, France and the USA." (emphasis provided)

7.12. Guided by the above aims and vision, funds were advanced to its AE in Cyprus on the following dates:-

"It is seen from the Form No.3CEB and Transfer Pricing Study that the assessee company has advanced loans to its AE in Cyprus, DLF Global Hospitality Limited, as per the table below:-

Date of initial Loan to DGHL	***Loan (US $) DHHL-DGHL***	***Amount in INR***
30.07.2007	*51,000,000*	*2,069,582,692*
18.09.2007	*500,000*	*20,306,910*
20.11.2007	*16,000,000*	*629,918,780*
11.12.2007	*5,080,000*	*200,152,084*
		2,919,960,466

7.13. Admittedly these loans were converted into equity within 3 months as per the following chart:-

Month End	***Opening (Rs.)***	***Funds Extended (Rs.)***	***Conversion into equity (Rs.)***	***Closing Balance***
Apr-07				
May-07				
June-07				
July-07		*2,069,582,691*		*2,069,582691*
Aug-07	*2,069,582,691*			*2,069,582691*

Month End	***Opening (Rs.)***	***Funds Extended (Rs.)***	***Conversion into equity (Rs.)***	***Closing Balance***
Sep-07	*2,069,582,691*	*20,306,910*		*2,089889602*
Oct-07	*2,089,889,602*		*2,069,582,692*	*20.306910*
Nov-07	*20,306,910*	*6,29,918,780*		*650.225690*
Dec-07	*650,225,690*	*200,152,084*		*850377774*
Jan-08	*850,377,774*			*850377774*
Feb-08	*850,377,774*		*850,377,774*	*NIL*
Mar-08	*Nil*			*NIL*

7.14. Though we find that the claim that these advances were converted into equity is not disputed by the Revenue, however, for the sake of completeness it is worth referring that this claim has been supported by following documents placed before the TPO/AO; the DRP and now before us in the Paper Book filed:-

S.No.	***Particulars.***	***Page No***
1	*Documents relating to share capital in the wholly owned subsidiary i.e. DLF Global Hospitality Ltd. (A) Initial Investment for equity shares: • Debt Authority to HSBC Bank alongwith ODI Form • Form A2-Application for remittance abroad • Chartered Accountants Certificate • Declaration cum undertaking under FEMA 1999 (B) Copies of resolution and other documents relating to issue of equity shares; • Written resolutions taken by the sole shareholder of DGHL*	*1-47* *48-49*

7.15. Apart from placing on record the copy of the audited balance sheet and profit and loss account of DLF Global Hospitality Limited for financial year 2007- 08 at pages 50 to 80 of their Paper book (available with the AO/TPO and the DRP)the assessee had also placed the following supporting documents:-

S.No.	***Particulars.***	***Page No***
1	*Details of Original shareholders of DLF Global Hospitality Ltd. • Copy of Instrument of Transfer • Copy of Certificate of Shareholding of Register of Companies • Notification dated 06.08.2007 for conversion of shares given to Registrar of companies • Certificates dated 25.08.2007 for change of name from Gunbarrel Investment Ltd. to DLF Global Hospitality Ltd. issued by ROC, Cyprus*	*81-84*

7.16. We find that the documents filed by the assessee right from the stage of assessment before the AO/TPO till date have not been assailed by the Revenue. We note that neither there is a rebuttal on facts nor is there any effort to assail their correctness. In the light of the above facts, we find that the assessee has successfully

demonstrated that the explanations offered were supported by actual conduct. The loans were advanced as an activity of increasing its foothold in opportunities outside as part of capital to be converted into equity. The stated intent of realizing the aims and vision of the assessee company was to fund its AE so that the benefits of the efforts of the AE in increasing the foothold/portfolio would directly benefit the tax payer in India and the fact that the interest free loan has been converted in equity after fulfilling the necessary legal requirements within three months is an evidence on record.

7.16.1. In the facts as they stand we are now called upon to decide whether in the peculiar facts and circumstances of the case it is an International Transaction or not. The Revenue claims that the fact of showing the interest free loan as an International Transaction to its subsidiary AE in Form 3CEB ipse dixit as considered in Perot Systems TSI vs DCIT [2010] 130 TTJ 685 (Del.) and also VVF Ltd. attracts the provisions of Chapter X of the Income Tax Act, 1961. The consistent objections posed by the tax payer though have been acknowledged by way of reproduction in the orders have not been considered necessary to address whether adjustment under Chapter X is warranted. The specious and facile reasoning that international transaction is acknowledged in Form 3CEB by the assessee itself cannot form the basis of the conclusion. At best it can form the starting point of the enquiry. In the light of the evidences on record and considering the arguments, we are inclined to hold that mere disclosure of the interest free loan as an international transaction by the tax payer in Form 3CEB would neither act as an estoppel nor fore close the tax payer from claiming the same as not being an international transaction. The transaction will become international transaction necessitating arm's length adjustment if the ingredients of the transaction bring it within the purview of Chapter X. The disclosure made by way of abundant caution or due to ignorance of law on facts cannot be the basis of the decision of the tax authorities more so if the assessee raises objections questioning the same. The decision of the tax authorities has to be based on facts supporting the conclusion. The tax authorities cannot shy away from addressing the arguments that it was a shareholder activity necessitating immediate availability of funds in the hands of the AE in order to attain the aims and vision of the holding company. The law does not permit or contemplate an Appellate forum or an Authority any justification for ignoring the arguments of the tax payer based on facts made available to them. The consistent fact on record is that the tax payer was the sole shareholder in its newly created subsidiary AE whose success in the venture of increasing its portfolio directly impacted the business interests. The fact that incapability to

generate resources and experience was clearly lacking is not in doubt. Though the commercial expediency by way of need or necessity of the same cannot be questioned by the Revenue however facts leading to and justifying the argument need to be addressed. It is well settled that the tax assessors cannot sit in the arm chair of the businessman. We hold considering the provisions that it is not within the domain of the tax authorities to insist that the aim of enhancing the global reach of the portfolio should be attained through a pure loan and not by way of shareholding activity. There is nothing on record to disbelieve the explanation that the AE did not have the demonstrated capability to fully utilize the funds for the intended purpose in a new area being a new territory. Thus the argument that in order to maintain control and command over the funds advanced fulfilling regulatory conditions at Cyprus etc. were required to be given due consideration. The stated intent of the tax payer that when the funds were fully utilized and exhausted by applying towards the intended purposes it was to be converted into equity which has been done. Thus the arguments that the funds advanced till then as an interest free loan, if it has to be disbelieved, has to be shown as sham or bogus transaction. The facts are not so. In the face of the above consistent claim demonstrated by the assessee by way of facts and supporting evidences which stand unassailed by the Revenue on record, we therefore find no justification either in fact or law to uphold the Revenue's stand that the tax payer must necessarily be bound by the disclosure made in Form No.3CEB Report. There is nothing on record to support the conclusion that the interest free loan must necessarily be deemed to be an interest earning activity and not an activity to capitalize the opportunity cost for investing in new territories. We hold that for the tax authorities to consider re-characterizing the transaction the tax authorities must necessarily demonstrate that the transaction as claimed and documented is a sham or on the basis of facts and evidences is at a substantial variance with the stated form. In the absence of any such exercise the tax authorities are entering at their peril in the realm of arbitrariness. In the facts of the present case there is not even a whisper of a suggestion that it was a bogus transaction, as admittedly shares have been allotted. There is nothing in the provisions of the Act which empowers the tax authorities to insist that the interest free loan towards its AE for capitalization the opportunity of cost of entering in new territories must necessarily by modified and re-characterized into a loan simplicitor and considered to be an activity for earning interest. The tax authorities must bring on record facts and evidences impacting the veracity of the claim of the assessee and demonstrate the hollowness of the assessee's claim. No such exercise has been done

to counter the consistent claim of the assessee demonstrated by facts on record that the intention was to capitalize the opportunity cost and not to encash the opportunity to best utilize the available funds. In the facts as they stand, we find that the claim of the assessee has to be allowed.

7.16.2. The order of the Co-ordinate Bench dated 07.07.2015 in the case of Soma Textiles and Industries Ltd vs CIT in ITA 262/AHD/2012 supports the view taken as the assessee's conduct in exploiting the opportunity for capital investment in the peculiar facts takes the issue out of the purview of Chapter X of the Income Tax Act, 1961. A brief reference to the said order at this place would be relevant as it is seen that the Co-ordinate Bench was also seized of facts where investment in share capital by the assessee holding company in India in its subsidiary in United Arab Emirates was held by the tax authorities to be covered within the scope of "international transactions" as defined in Section 92CA(3). Therein also the commercial expediency for advancing of interest free loans by the assessee was not accepted by the tax authorities and as in the facts of the present case reliance therein was also placed on Perot Systems TSI vs DCIT [2010] 130 TTJ 685 (Del.) and also VVF Ltd. (cited supra) wherein more or less identical claim of the assessee was rejected by the TPO and the said finding had been upheld by the CIT(A). The Co-ordinate Bench considering the facts accepted the assessee's argument that in the case of Perot Systems (cited supra) the argument that loan being quasi-capital was rejected on facts and the core legal issue was left open namely whether ALP adjustments will also be warranted in case of interest free loan extended as quasi-capital. The Co-ordinate Bench examined and considered the decisions rendered in Perot Systems TSI vs DCIT [2010] 130 TTJ 685 (Del.); Micro Inks Ltd vs ACIT [2013] 157 TTJ 289 (Ahd.); Four Soft Pvt. Ltd. vs DCIT [2014] 149 ITD 732 (Hyd); Prithvi Information Solutions Pvt. Ltd. vs ACIT [2014] 34 ITR (Tri) 429 (Hyd.) and thereafter came to the conclusion that none of these decisions had thrown any light on what constitutes "quasi capital" in the context of transfer pricing and its relevance in ascertainment of the arms length sales price of a transaction in the said context. The Coordinate Bench has quoted the decision of the Hon'ble Delhi High Court in the case of Chryscapital Investment Advisors India Ltd Vs ACIT [(2015) 56 taxmann.com 417 (Delhi)] wherein their Lordships have begun by quoting the thought provoking words of Justice Felix Frankfurter to the effect that "A phrase begins life as a literary expression; its felicity leads to its lazy repetition; and repetition soon establishes it as a legal formula, undiscriminatingly used to express different and sometimes contradictory ideas". The reference so

made to the words of Justice Frankfurter was in the context of the concept of "super profits". The Co-ordinate Bench observed that it is equally valid in the context of concept of "quasi capital" also observing that as in the case of the "super profits" there has been a "lazy repetition" (in the words of Felix Frankfurter J.) with regard to "quasi capital" as there appears to be no independent analysis of the provisions of the Act and the rules with regard to "quasi capital" also.

7.16.3. We find that the Co-ordinate Bench considering the term "quasi capital" has correctly understood "that a quasi-capital loan or advance is not a routine loan transaction simplictor. The substantive reward for such a loan transaction is not interest but opportunity to own capital. As a corollary to this position, in the cases of quasi capital loans or advances, the comparison of the quasi capital loans is not with the commercial borrowings but with the loans or advances which are given in the same or similar situations." The decisions considering the expression were held to be inapplicable as "The reward for time value of money in these cases was opportunity to subscribe to the capital, unlike in a normal loan transaction where reward is interest, which is measured as a percentage of the money loaned or advanced." We find that quasi capital can be said to be a category of debt taken by a company which in the context of transfer pricing issues is not only an instrument of legitimate funding but is also a hybrid instrument pre-stipulated to be a loan for a transitory period, the economic purpose of which is a future capital investment in all its forms including contribution to equity or subscription of capital and cannot be justifiably be treated as a debt simplicitor.

7.17. Reliance has also been placed on the case of Bharti Airtel Ltd. vs ACIT in ITA No.5816/Del/2012 dated 11.03.2014 (Copy of which has been placed at book pages 38 to 94). Though reliance on the said decision has primarily been placed qua Ground No.2 in order to argue that without prejudice to the main issue if at all interest was to be charged on the interest free advances then the LIBOR rate would apply. The said proposition it has been argued is also supported by the decision of the Jurisdictional High Court in the case of Cotton Naturals India P. Ltd.(cited supra). However, apart from the issue agitated in Ground No.2, Bharti Airtel Ltd. (cited supra) has also been relied in support of the primary issue for the proposition that the activity of interest free advances ultimately to be converted into equity by a holding company to a subsidiary company does not give rise to an international transaction.

7.18. Considering the said decision, we find that the Co-ordinate Bench was called upon to decide whether Chapter X was attracted in facts where the assessee had advanced interest free loans to its

AE for the stated purpose of share application. These material facts and issue would be evident from the very wordings of Ground No.15 and 15.1 raised by the assessee before the Co-ordinate Bench. These grounds when read alongwith other related grounds agitated before the Co-ordinate Bench are being reproduced so as to bring out the gamut of issues agitated and considered:-

> *43. "In ground no. 15, the assessee has raised the following grievance:*
>
> *15. That the assessing officer/TPO erred on facts and in law in making addition of Rs.19,15,45,943 on account of notional interest calculated @ 17.26% p.a. on the amount of share application money advanced by the appellant to its AEs.*
>
> *15.1. That the assessing officer/TPO erred on facts and in law in not appreciating that the transaction of advancement of share application money was not in the nature of "international transaction" as defined in section 92B and hence was outside the purview and scope of Chapter X of the Act.*
>
> *15.2. That the assessing officer/TPO erred on facts and in law in treating the amount of investments made by the appellant in its associated enterprises in the form of share application money for allotment of shares as interest free loans and consequently, applying transfer pricing provisions to the said transaction(s) and while doing so making an improper comparison by:*
>
> *(a) Considering rate of interest suggested by rating agency and banks to general investor which are subject to various conditions like credit rating, loan, tenure, etc. and ignoring the fact that such rates can vary according to these variables;*
>
> *(b) Undertaking a flawed analysis by applying the rate of interest used in relation to - Indian currency loan given in India to an intercompany transaction of advancement of money outside of India, thereby completely ignoring the difference in the, economic environment and geographical conditions prevalent in India and overseas jurisdictions;*
>
> *(c) alleging that the financial health of the associated enterprises was weak and further in determining the credit rating of the associated enterprises as ranging between BB to D, being high risk category, without providing any cogent or germane reason for the same;*

(d) making additional arbitrary and adhoc adjustments to the rate of interest on account of security and single customer and transaction cost, thereby completely ignoring the on-ground reality of the inter--company transaction that there is no significant risk in advancing loans to 100% subsidiary companies and demonstrating an intention to arrive at a very high interest rate of 17.26% p.a. with the single-minded intention of making an addition to the returned income of the appellant. 15.3 That the assessing officer/TPO erred in relying upon the rate of interest charged by various domestic banks on advancement of foreign currency loans obtained by the TPO under section 133(6) of the Act, without affording opportunity to the appellant to rebut the same, in violation of principles of natural justice.

15.4 That the assessing officer/TPO erred in relying upon the information obtained under section 133(6) of the Act, without appreciating that such information was not available in the public domain and therefore, could not have been relied upon for the purpose of determining the arm's length price.

15.5. Without prejudice, that the assessing officer/TPO erred in computing the amount of interest at Rs.19,15,45,943, by applying rate of interest of 17.26% p.a. for the whole year on the consolidated amount of share application money, without considering the monthly balance of share application money.

15.6 That the assessing officer/TPO erred on facts and in law by disregarding established judicial pronouncements in India in making the Transfer Pricing adjustment."

7.18.1. The facts and the legal precedent with which the Coordinate Bench was seized of are set out in Paras 44 to 45 of the said order and are reproduced hereunder for the purposes of bringing out the similarity on the material facts:-

44. So far as this grievance of the assessee is concerned, the relevant material facts, to the extent necessary for our adjudication, are as follows. It is not in dispute that during the relevant previous year the assessee has made following payments towards share application money in its foreign subsidiaries:

Name of associated Enterprises	***Amount of advance (Rs.)***	***Date of share application***	***Date of issue of shares***
Bharti Airtel (U.S.A.) Ltd.	*40,45,14,1 09*	*29.11.2007*	*31.03.2009*
Bharti Airtel (U.K.) Ltd.	*3,17,72,666*	*31.01.2008*	*12.03.2009*
Bharti Airtel (Singapore) Ltd.	*2,01,39,150*	*24,09.2007*	*1.04.2009*

Name of associated Enterprises	***Amount of advance (Rs.)***	***Date of share application***	***Date of issue of shares***
Bharti Airtel (Hongkong) Ltd.	*1,81,48,200*	*24.09.2007*	*10.12.2008.*
Bharti Airtel (Lanka) Ltd	*63,51,93,795*	*Various dates*	*31.07.2008*
		Total	*110,97,67,920*

45. These transactions were not benchmarked as, according to the assessee, these were in the nature of share application money payments. While the TPO did not question the character of payment, he noted that "from the information on record, it is seen that these amounts were extended by the AE which have not been converted into equity for quite a long time after the initial advancement". It was also noted that time taken in actual allotment of shares has taken place as much as 13, 16 and 14 months in the cases of UK, US and Hong Kong based subsidiaries, and that the assessee has not earned any interest for this long period. The TPO was of the view that "any independent entity would not have left the amount in the hands of another entity without the same being converted into equity within a reasonable period or receiving interest on the same". It was in this backdrop that the TPO proceeded to treat these amounts as interest free loans extended to the AEs. He then referred to the provisions of Section 92 B, in the light of which, according to the TPO, lending or borrowing of the money comes within the ambit of 'international transactions'. He thus justified determination of arm's length price of the transaction of, what he termed, as interest loans to the AEs. Reliance was placed on the decisions of the coordinate benches in the cases of VVF Ltd Vs DCIT (2010 TIOL 55 ITAT MUM TP) and Perot Systems TSI India Ltd Vs DCIT (2010 TII 3 ITAT TEL TP). The TPO then proceeded to determine ALP of the deemed interest free loans to the AE, but, for the reasons we will set out in a short while, it is not really necessary to deal with facts relating to ALP determination part. When assessee raised the objection before the DRP on this issue, it was rejected by observing that," we agree with the TPO that capital locked up for want of transfer of shares for reasonably long period would partake the nature of loan". It was in this backdrop that payments for share application money were treated as interest free loans given to the AEs and ALP adjustment was made for interest thereon. Aggrieved, assessee is in appeal before us." (emphasis provided)

7.18.2. Considering the arguments on these facts and the legal precedent the Coordinate Bench came to the following conclusion:-

> *46. "We have heard the rival contentions, perused the material on record and duly considered factual matrix of the case in the light of the applicable legal position.*
>
> *47. We find that in the present case the TPO has not disputed that the impugned transactions were in the nature of payments for share application money, and thus, of capital contributions. The TPO has not made any adjustment with regard to the ALP of the capital contribution. He has, however, treated these transactions partly as of an interest free loan, for the period between the dates of payment till the date on which shares were actually allotted, and partly as capital contribution, i.e. after the subscribed shares were allotted by the subsidiaries in which capital contributions were made. No doubt, if these transactions are treated as in the nature of lending or borrowing, the transactions can be subjected to ALP adjustments, and the ALP so computed can be the basis of computing taxable business profits of the assessee, but the core issue before us is whether such a deeming fiction is envisaged under the scheme of the transfer pricing legislation or on the facts of this case. We donot find so. We donot find any provision in law enabling such deeming fiction. What is before us is a transaction of capital subscription, its character as such is not in dispute and yet it has been treated as partly of the nature of interest free loan on the ground that there has been a delay in allotment of shares. On facts of this case also, there is no finding about what is the reasonable and permissible time period for allotment of shares, and even if one was to assume that there was an unreasonable delay in allotment of shares, the capital contribution could have, at best, been treated as an interest free loan for such a period of 'inordinate delay' and not the entire period between the date of making the payment and date of allotment of shares. Even if ALP determination was to be done in respect of such deemed interest free loan on allotment of shares under the CUP method, as has been claimed to have been done in this case, it was to be done on the basis as to what would have been interest payable to an unrelated share applicant if, despite having made the payment of share application money, the applicant is not allotted the shares. That aspect of the matter is determined by the relevant statute. This situation is not in pari materia with an interest free loan on commercial basis between the share applicant and the company to which*

capital contribution is being made. On these facts, it was unreasonable and inappropriate to treat the transaction as partly in the nature of interest free loan to the AE. Since the TPO has not brought on record anything to show that an unrelated share applicant was to be paid any interest for the period between making the share application payment and allotment of shares, the very foundation of impugned ALP adjustment is devoid of legally sustainable merits.

48. Let us also deal with two judicial precedents which have been heavily relied upon by the TPO, as also by the learned Departmental Representative, on which their case rests. None of these decisions, however, deal with the core issue before us i.e. whether a capital contribution can be deemed to be partly an interest free loan, for the period till the shares were actually allotted, and partly as capital contribution, after the subscribed shares were issued by the subsidiary in which capital contribution was made. In the case of Perot Systems TSI India Ltd Vs. DCIT (supra), a coordinate bench of this Tribunal had an occasion to deal with the arm's length price adjustment with regard to interest free advances to the subsidiaries. That was a case in which the assessee, an Indian company, advanced interest-free loans to its 100% foreign subsidiaries. The subsidiaries used those funds to make investments in other step- down subsidiaries. On the question whether notional interest on the said loans could be assessed in the hands of the assessee under the transfer pricing provisions of Chapter X, the assessee argued that the said "loans" were in fact "quasi - equity" and made out of commercial expediency. It was also argued that notional income could not be assessed to tax. However, both of these arguments were rejected by a coordinate bench of this Tribunal. While doing so, the coordinate bench observed that there was no material on record to establish that the loans were in reality not loans but were quasi -capital and that there is also no reason why the loans were not contributed as capital if they were actually meant to be a capital contribution. It was observed that, "It is not the case that there was any technical problem that the loan could not have been contributed as capital originally, if it was meant to be a capital contribution". The argument of loan being in the nature of quasi capital was thus rejected on facts. It was not even a case of quasi capital, and, therefore, this case has no bearing on the question before us i.e. whether ALP adjustments can be made in respect of payments towards share application

money in a situation in which the shares have been issued several months after the payments for share application money have been made. Similarly, in VVF's case (supra), the transaction was admittedly in the nature of interest free loan between AEs and the commercial expediency in advancing interest free loans was on account of ownership and control of subsidiary being in the hands of the assessee, which was recognized as a significant factor for commercial expediency. However, as we have seen in the earlier discussions, such commercial expediency of granting interest free loans is wholly irrelevant because it is the impact of this interrelationship, on account of management, capital and control, which is sought to be neutralized by arm's length price adjustments. This was also not a case in which a capital contribution was deemed to be partly an interest free loan (i.e. for the period till the shares were actually allotted) and partly as capital contribution (i.e. when the subscribed shares were allotted by the subsidiary). Revenue, therefore, does not derive any advantage from these judicial precedents either.

49. In any event, it is not open to the revenue authorities to recharacterize the transaction unless it is found to be a sham or bogus transaction. While there are no specific powers vested in the TPO to recharacterize the transaction, even under the judge made law, such rechracterization can be done by the revenue authorities when the transactions are found to be substantially at variance with the stated form. In the present case, there cannot even a suggestion to hold that this is a bogus transaction because admittedly the subscribed shares capital has indeed been allotted to the assessee. The transaction is thus accepted to be genuine in effect.

50. In view of these discussions, as also bearing in mind entirety of the case, we are of the considered view that the authorities below were in error in treating the payment of share application money, as partly in the nature of interest free loans to the AEs, and, accordingly, ALP adjustment based on that hypothesis was indeed devoid of legally sustainable merits. We delete the impugned adjustment of Rs.19,15,45,943. The assessee gets the relief accordingly. As we have decided this ground of appeal on the fundamental issue that the payment of share application money could not be partly treated as interest free loan to AE, we see no need to deal with other aspects of the matter." (emphasis provided)

7.18.3. When the facts as considered by the Co-ordinate Bench in the case of Bharti Airtel Ltd. are seen and the facts of the present case are considered, we find that there is a striking similarity on the material issues and the above conclusion and reasoning fully supports the view taken. In fact as argued on behalf of the assessee the facts of the assessee's case in the present case are on a better footing as there is no perceived inordinate delay in converting the interest free loan into equity which exercise admittedly has been completed in 3 months as opposed to 13 to 14 months. Thus, the said decision fully supports the allowability of assessee's claim."

32. We also observe that the TPO while charging interest at the rate of 6% compared another AE of the assessee namely RLSBV which is a controlled transaction with that of the RLSI for benchmarking the transaction. Following the decisions of the Hon'ble Bombay High Court in the case of the CIT *v.* Lever India Exports Ltd (supra) and CIT *v.* Merck Ltd*. (*supra*),* we hold that arm's length price cannot be determined on the basis of another controlled transaction as was done by the TPO. Therefore, respectfully following the above decisions, we hold that no interest ought to have charged on the OCL advanced to payee RLSI and thus we direct the Assessing Officer to delete the adjustment made towards interest.

33. Ground No. 4 is in respect of interest charged on the amount paid towards subscription to share capital of AE's. In the grounds of appeal assessee contends as under: -

(i) The learned CIT(A) erred in confirming the action of the A.O., in re-characterizing the transaction of amount being paid by the

appellant towards subscription to share capital of its AE's M/s. RLS BV and M/s. RLS Inc, by treating the same as interest free loan.

(ii) The learned CIT(A) erred in confirming the action of the A.O., in determining the ALP of interest chargeable in respect of the amount paid towards subscription to share capital of its AE's M/s. RLS BV and M/s. RLS Inc, at Rs. 60,87,235/- and Rs. 10,65,5547-, respectively.

(iii) He failed to appreciate that that subscription money was paid towards subscribing to the shares of M/s. RLS BV and M/s. RLS Inc, which have been subsequently allotted by the respective AE's as on 31st March 2011 and which is corroborated from the filing made with the Reserve Bank of India while remitting the funds to M/s. RLS BV and M/s. RLS Inc.

(iv) The appellant prays that the action of the A.O, as confirmed by the CIT(A), of re-characterizing a transaction, is not permitted under the provisions of the Income-tax Act, 1961 for said assessment year and hence the same ought to have been rejected.

Consequently, the appellant prays that the transfer pricing adjustment confirmed by the CIT(A), of charging interest on the amount paid towards subscription to share capital of the AE's is unjustified and ought to be deleted."

34. Briefly stated the facts are that, during the financial year 2008-09, the assessee had paid share application money towards subscription of Paid-in-Equity/ Capital surplus of RLS Inc [for short "RLSI"] and towards subscription of preference shares of RLSBV and since no shares were allotted against the share application money TPO treated the amounts as interest free loan and calculated interest at the rate of 6% p.a., which was charged by the assessee in respect of loans provided to its AE RLSBV. The Ld. CIT(A) upheld the adjustment made by the TPO.

35. Ld. Counsel for the assessee submits that pursuant to the share application money paid by the assessee the amount has been converted

into paid-in-equity/ Capital surplus by RLSI and preference shares were allotted by RLSBV to the assessee as on 31st March 2011. This is evidenced from CPA certificate dated 12.10.2011 and deed of issue of preference shares by RLSBV which are placed at pages 220 and 221 of the Factual paper book. Ld. Counsel for the assessee submits that computing interest on the share application money would amount to recharacterization of paid-in-equity/ preference capital into debt which is not permissible under the Act. Reliance in this regard is placed on the decision of the Hon'ble Jurisdictional High Court in the case of DIT *v.* Besix Kier Dabhol SA in ITA.No. 776 of 2011 dated 30.08.2012 wherein it has been held that recharacterization of transaction is not permitted in absence of specific provisions under the Act. Ld. Counsel for the assessee also submitted that TPO cannot question commercial expediency of transactions, it is a case of investment in share capital and it cannot be given different colour to expand the scope of TP. Reliance in this regard is placed on the decision of the Hon'ble Bombay High Court in the case of Pr CIT *v.* Aegis Ltd in ITA.No. 1248 of 2016 dated 28.01.2019 wherein the assessee had made payments towards subscription of preference shares of its AEs, the TPO treated this as interest free loan to AEs and determined the addition towards notional interest. The Jurisdictional High Court has disapproved of this action of

recharacterization by the TPO. Reliance is also placed on the decision in case of Pr CIT *v.* PMP Auto Components Pvt Ltd in ITA.No. 1685 of 2016 dated 20.02.2019 (Bombay HC).

36. It is also the contention of the Assessee that a transaction of capital contribution, the character of which is not under dispute, cannot be treated as interest free loan merely due to delay in allotment of shares. It is submitted that the Jurisdictional Tribunal in case of ITO v/s Sterling Oil Resources Pvt Ltd in ITA.No. 1791/Mum/2014 dated 29.02.2016 observed that as long as the subsidiary is a wholly owned subsidiary, non-allotment or delay in allotment of shares does not prejudice the interests of the Assessee. The Tribunal also observed that revenue's reliance on Perot System's case, was wholly misplaced inasmuch as it was a case of loan which was stated to be in the nature of quasi capital, whereas in the present case the payment was right from the initial stage towards subscription for shares. Thus, Hon'ble Tribunal deleted the adjustment of notional interest on the share application money.

37. Ld. Counsel for the assessee submits that transfer pricing provisions are not applicable to amount paid towards capital of subsidiaries outside

India as there is no income arising from the transaction. Reliance in this regard is placed on following decisions:

(i) Aries Agro Ltd v/s DCIT (ITA No. 1452/M/2017) (delay in allotment was more than 5 years)

(ii) Hill County Properties Ltd (ITA No 1644/Hyd/2014) (Hyderabad ITAT)

38. Without prejudice to the above, even if it is treated as an international transaction, since the TPO has not brought any comparable on record to show that an unrelated share applicant was to be paid any interest for the period between making payment and allotment of shares, the very foundation of impugned ALP adjustment is devoid of any legally sustainable merits. It is submitted that this view is upheld by the Jurisdictional Tribunal in the case of Pan India Network Infravest Pvt Ltd., in ITA.No. 7026/Mum/2013 dated 04.12.2015 wherein the delay on allotment was 3 years 6 months.

39. Without prejudice to the above, it is submitted that even if capital financing is to be held as an international transaction, even then the provision cannot be applied retrospectively. The provisions of the Act which were on the Statute as on 1.04.2012 only will apply for the FY 2012-13 (ie AY 2013-14) and onwards. Without prejudice to the above, it is submitted that the argument of the assessee in respect of

erroneous benchmarking adopted by the TPO in Ground No 3 above also applies to the transaction of share application money.

40. Ld. DR vehemently supported the orders of the authorities below. Ld. DR further submits that the share application money was not recharectersed as loan but it was essentially a loan. Ld. DR submits that the preference shares carry coupon of 5% therefore, it is in the nature of loan and the arm's length price of interest determined by the TPO is justified.

41. In reply referring to page Nos. 329 to 358 of the Paper Book the Ld. Counsel for the assessee submits that the amount remitted as share application money is evidenced from the RBI filings. Referring to page Nos. 9 and 17 of the Paper Book Ld. Counsel for the assessee submits that the finances of RVSBV and RLSI also reported the amounts under shareholders paid in equity. He further submits that the TPO in the order itself has given a finding that he is recharactersing the transaction to one of loans. Ld. Counsel for the assessee further submits that preference share form part of share capital and not debt of the Company. Therefore, even though they may carry the preferential coupon rate the same cannot be regarded as loan. Referring to Page No. 25 of the Ld.CIT(A) order Ld. Counsel for the assessee submits that as per the terms of the issues

of preference shares there shall carry coupon of 5% in case of distribution of profits. It is submitted that this cannot be equated with interest coupon. It is submitted that the dividend is payable only on the availably of sufficient profits itself proves that the investment is in the nature of share capital and not debt.

42. We have heard the rival submissions and perused the orders of the authorities below. On a perusal of the order of the Ld. TPO, we find that assessee subscribed to equity shares of RLSI and RLSBV as a part of its capital investment in its 100% subsidiary. The assessee submitted before the TPO that since the basic objective of the above investment in the form of share application was to fund its AE's for developing global business opportunities for further expanding the assessee's business operations outside India, the specification to the shares of AE's at fair value has been shown at arm's length price. Assessee also contended that since subscription to equity shares does not have a bearing on the determination of income of the assessee the provisions of section 92(1) of the Act are not applicable to the international transaction of such nature as defined in section 92B(1) of the Act. However, the TPO held that since no shares have been allotted by AE's to the assessee in respect of the amount paid towards share application the same would be characterized as being in the nature of interest free loan provided to AE's. TPO also

observed the fact that AE's were setup for developing global business opportunities for further expanding the assessee's business operations outside the India is not a valid ground for non-allotment of shares by AE's to the assessee. Therefore, in the absence of allotment of shares the share application money is treated as loan given by the assessee to its AE's and applied interest rate at 6% per annum and accordingly made adjustment. The Ld.CIT(A) upheld the adjustment.

43. Before us, Ld. Counsel for the assessee placing reliance on the decision of the Hon'ble Bombay High Court in the case of Director of Income-tax *v.* Besix Kier Dabhol Stay Application in ITA.No. 776 of 2011 dated 30.08.2012 and PCIT *v.* Aegis Limited in ITA.No. 1248 of 2016 dated 27.01.2019 contends that recharecterisation of transaction is not permitted in the absence of specific provisions under the Act.

44. We have gone through the judgment of the Hon'ble Bombay High Court referred to above in the case of DIT *v.* Besix Ker Dabhol SA (supra). The Hon'ble Bombay High Court while answering the following question observed as under: -

> *"Q.1. Whether on the facts and circumstances of the case and in law the Tribunal was right in holding that in the absence of any specific thin capitalization rules in India, the Assessing officer cannot disallow the interest payment on debt capital after having observed the abnormal thin capitalization ratio of 248:1?*
>
> *…..*

4) The respondent-assessee is a company incorporated under the laws of Belgium. The sole business of the respondent assessee is to carry out the project of construction of fuel jetty near Dabhol in India. The respondent-assessee had fully paid capital of 25.00 lacs (Belgium Francs) divided into 2500 shares of 1000 Belgium Francs each. This equity capital was divided in the ratio of 60:40 between the two joint venture partners N V Besix SA, Belgium and Kier International (Investment) Limited of U.K. The respondent assessee also borrowed from its shareholders in the same ratio as the equity share holding amount of Rs.57.09 crores from N.A. Basix SA and Rs.37.01 crores from Kier International Investment Limited. In the circumstances, the respondent had equity capital of Rs. 38.00 lacs and debt capital of Rs.9410 lacs. Thus, debt equity ratio worked out is to 248:1.

5) The respondent assessee paid interest of Rs. 5.73 crores on the aforesaid borrowing of Rs.57.09 crores and Rs.37.01 crores from NV Basix SA and Kier International (Investments) Limited respectively. However, the Assessing Officer disallowed the payment of interest in view of the Reserve Bank of India's approval letter dated 3/11/1998 granting approval to the assessee to do business in India. The approval letter dated 03/11/1998 specifically provided that India Branch Office will not borrow or lend from/to any person in India without specific permission of the Reserve bank of India. The Assessing officer further observed that in view of India Belgium Double Taxation Avoidance Agreement interest on monies paid by the Head Office to the branches was not allowable as a deduction.

6) In appeal, the Commissioner of Income Tax (Appeals) by an order dated 29/3/2007 upheld the order of the Assessing officer and disallowed the deduction on account of interest of Rs.5.73 crores paid to Joint Venture Partners. The Commissioner of Income Tax (Appeals) held that Article 7(3)(b) of the Double Taxation Avoidance Agreement forbids allowance of any interest paid to the head office by permanent establishment in India as a deduction. Further, the payment of interest also directly violates the conditions imposed by RBI in its letter dated 3/11/1998. Therefore, the order of the Assessing Officer was upheld.

7) However, the Tribunal allowed the respondent-assessee's appeal. During the course of the proceedings before the Tribunal the revenue contended that the borrowings on which the interest has been claimed as a deduction are in fact capital of the assessee and brought only under the nomenclature of loan for tax consideration. It was the case of the appellant-revenue before the Tribunal that debt capital is required to be re-characterized as equity capital. However, the Tribunal held that in India as the law stands there were no rules with regard to thin capitalization so as to consider debt as an equity.

It is only in the proposed Direct Tax Code Bill of 2010 that as a part of the General Anti Avoidance Rules it is proposed to introduce a provision by which a arrangement may be declared as an impermissible avoidance arrangement and may be determined by recharactersing any equity into debt or vice versa.

8) We find no fault with the above observations of the Tribunal. There were at the relevant time and even today no thin capitalization rules in force. Consequently, the interest payment on debt capital cannot be disallowed. In view of the above, the question (i) raises no substantial question of law and is therefore, dismissed."

45. In the case of PCIT *v.* Aegis Limited (supra) the Hon'ble Jurisdictional High Court while answering the following question observed as under: -

"Q1. Whether on the facts and circumstances of the case and in law, the Income Tax Appellate Tribunal erred in not considering the fact that the assessee had actually advanced/lent money to its AE in the garb of preference shares leading to attraction of provisions relating to Transfer Pricing in the ease of the assessee in view of Section 92B of the Act, without appreciating the fact that these preferential shares do not carry any dividend and are beyond scope of any capital appreciation ?

….

2. The respondent-assessee is a Company registered under the Companies Act. For the Assessment Year 2009 10, the assessee was subjected to transfer pricing regime. Question no.1 arises out of the action of the Revenue to tax notional interest in the hands of the assessee through transfer pricing. The facts are that, during the period relevant to the assessment year in question, the assessee had subscribed to redeemable preferential shares of its Associated Enterprises ("AE" for short) and redeemed some of its shares at par. The Transfer Pricing Officer ("TPO" for short) held that the preference shares were equivalent to interest free loans advanced by the assessee and accordingly charged the interest on notional basis. The Tribunal by the impugned judgment, deleted the addition observing that the TPO had re-characterised the transaction of subscription of shares into advancing of unsecured loans. The Tribunal did not accept such conclusion, inter-alia on the grounds

that the TPO cannot disregard the apparent transaction and substitute the same without any material of exceptional circumstances pointing out that the assessee had tried to conceal the real transaction or that the transaction in question was sham. The Tribunal observed that the TPO cannot question the commercial expediency of the assessee entered into such transaction.

3. We are broadly in agreement with the view of the Tribunal. The facts on record would suggest that the assessee had entered into a transaction of purchase and sale of shares of an AE. Nothing is brought on record by the Revenue to suggest that the transaction was sham. In absence of any material on record, the TPO could not have treated such transaction as a loan and charged interest thereon on notional basis. No question of law arises."

46. Similar view has been taken by the Hon'ble Bombay High Court in a recent Judgement in the case of Pr.CIT *v.* Concentrix Services India Pvt. Ltd., in ITA.No. 778 of 2017 and 867 of 2017 dated 04.09.2019. Further, the Ld. DR has not brought any contrary decisions to our notice. The ratio of the above decisions squarely applicable to the facts of the assessee's case. The TPO has recharectersied the transaction of investment of preference shares into loan which is not permissible in view of the judgments of the Hon'ble Bombay High Court. Thus, respectfully following the above decisions, we direct the Assessing Officer to delete the adjustment made towards interest on subscription to share capital of AE's.

ITA.No. 3883/MUM/2016 (A.Y: 2010-11)

47. Ground No.1 of grounds of appeal is in respect of disallowance u/s.14A of the Act. At the outset it was submitted by the Ld. Counsel for

the assessee that during the assessment year under consideration assessee has not earned any exempt income and therefore no disallowance is warranted u/s. 14A of the Act. Reliance was placed on the decision of the Hon'ble Bombay High Court in the case of Pr.CIT *v.* M/s. Ballarpur Industries Limited in ITA.No. 51 of 2016 dated 13.10.216.

48. We have heard the rival submissions, perused the orders of the authorities below. We agree with the submissions of the Ld. Counsel for the assessee that since assessee has not earned any exempt income and therefore no disallowance is warranted u/s. 14A of the Act. In the case of Joint Investments Pvt. Ltd. *v.* CIT [372 ITR 694] the Hon'ble Delhi High Court held that the disallowance u/s. 14A of the Act should not exceed the exempt income. The Revenue filed SLP against this decision and the Hon'ble Supreme Court dismissed the SLP filed by the Revenue. Similar view has been taken by the Hon'ble Delhi High Court in the case of Cheminvest Limited *v.* CIT [378 ITR 33].

49. In the case of ACIT *v.* M/s. Ballarpur Industries Ltd., in ITA.No. 346 to 379/NAG/2014 dated 04.12.2015 the Nagpur Bench of the Tribunal following the decision of the Hon'ble Delhi High Court in the case of Cheminvest *v.* CIT (supra) held as under: -

> *"6. We have heard both the sides at some length and carefully perused the orders of the authorities below in the light of the precedence*

cited. As far as the exemption for the years under consideration were concerned, it was an admitted factual position that the AO has not mentioned any such amount. Meaning thereby, there was no exempt income earned by the assessee for the years under consideration. In reply to one of our questions, the learned AR, Mr. K. P. Dewani has also made a statement at Bar that no dividend was declared, hence, there was no earning of exempted dividend income. He has also clarified that for the purpose of invocation of the provisions of section 14A of the IT Act, the AO has applied the formula only in respect of disallowance of proportionate interest expenditure. There was no allegation of the AO that the exempt income was earned by the assessee. In the light of the undisputed finding on facts, we have perused the decision of the Hon'ble Courts. We may like to mention that a view has been expressed consistently that if there is no exempted profit then there is no question of invocation of the provisions of section 14A of the IT Act but, we have also carefully perused that very decision of the Tribunal namely Cheminvest Ltd. (supra) was reversed by the Hon'ble Delhi High Court, copy placed in the compilation. The Hon'ble Delhi High Court in ITA No.749/2014 vide order dated 02-09-2015 titled as "Cheminvest Ltd. Vs CIT" has decided the substantial question of law that whether disallowance u/s 14A of the Act can be made in a year in which no exempt income has been earned or received by the assessee. The Final verdict was as under: -

> *"23. In the context of the facts enumerated hereinbefore the Court answers the question framed by holding that the expression 'does not form part of the total income' in Section 14A of the envisages that there should be an actual receipt of income, which is not includible in the total income, during the relevant previous year for the purpose of disallowing any expenditure incurred in relation to the said income. In other words, Section 14A will not apply if no exempt income is received or receivable during the relevant previous year."*

7. In short, in a situation when that very order of the Tribunal which was the basis for invocation of the provisions of Section 14A of the IT Act got reversed by the Hon'ble Delhi High Court, hence, the very said basis do not survive any more. As a result, we hereby confirm the findings of the learned CIT (A) on this issue. We hereby also hold that in view of the numbers of decisions on this issue in favour of the tax payers, we find no force in this ground of appeal of the Revenue. The same is dismissed."

50. This decision of the Tribunal has been affirmed by the Hon'ble Bombay High Court in the case of Pr.CIT *v.* M/s. Ballarpur Industries Limited in ITA.No. 51 of 2016 dated 13.10.216 by rejecting the appeal of

the Revenue and held that no substantial question of law arises. While holding so the Hon'ble High Court observed as under: -

> *"On hearing the learned Counsel for the Department and on a perusal of the impugned orders, it appears that both the Authorities have recorded a clear finding of fact that there was no exempt income earned by the assessee. While holding so, the Authorities relied on the judgment of the Delhi High Court in Income Tax Appeal No. 749/2014, which holds that the expression "does not form part of the total income" in Section 14A of the Income Tax Act, 1961 envisages that there should be an actual receipt of the income, which is not includible in the total income, during the relevant previous year for the purpose of disallowing any expenditure incurred in relation to the said income. The Income Tax Appellate Tribunal held that the provisions of Section 14A of the Income Tax Act, 1961 would not apply to the facts of this case as no exempt income was received or receivable during the relevant previous year. It is not the case of the Assessing Officer that any actual income was received by the assessee and the same was includible in the total income. In the facts of the case, the Authorities held that since the investments made by the assessee in the sister concerns were not the actual income received by the assessee, they could not have been included in the total income.*
>
> *The findings of facts recorded by both the Authorities do not give rise to any substantial question of law.*
>
> *Since no substantial question of law arises in this income tax appeal, the income tax appeal is dismissed with no order as to costs."*

51. The Hon'ble Jurisdictional High Court held that if there is no exempt income there cannot be any disallowance. Respectfully following the said decision, we direct the Assessing Officer to delete the disallowance made u/s. 14A of the Act. Ground raised by the assessee is allowed.

52. The next ground of appeal is in respect of disallowance u/s. 35(2AB) of the Act.

53. Briefly stated the facts are that, the Assessing Officer while completing the assessment noticed that assessee claimed ₹.10,35,105/- as deduction u/s. 35(2AB) and find that assessee claimed to have incurred an expenditure of ₹.17,89,22,845/- for in-house research facility. Further, he also noticed on verification of the details of expenses that assessee has made a payment of ₹.20,70,211/- to M/s. Reliance Clinical Research Services Private Limited for carrying out clinical trial needed for R&D activity. Assessing Officer disallowed the expenditure of ₹.20,70,211/- which was incurred on clinical trials outside the R&D facilities of the assessee for which rated deduction was claimed @150%. On appeal the Ld.CIT(A) following his own order for the A.Y. 2007-08 sustained the disallowance.

54. Before us, Ld. Counsel for the assessee submits that Ld.CIT(A) has erred in confirming the action of the Assessing Officer in disallowing the claim for deduction u/s. 35(2AB) of the Act. Referring to the decision of the Hon'ble Gujarat High Court in the case of CIT *v.* Cadila Healthcare Ltd., [31 taxmann.com 300], Ld. Counsel for the assessee submits that even clinical trials conducted outside the approved laboratory facility is eligible for deduction u/s. 35(2AB) of the Act.

55. Without prejudice to the above, the Ld. Counsel for the assessee submits that the said expenditure is allowable as deduction u/s. 37(1) of the Act. Ld. Counsel for the assessee submits that for the A.Y. 2007-08 the Tribunal in ITA.No. 1575/MUM/2013 dated 19.10.2015 allowed the alternative claim of the assessee that the expenditure be allowed as deduction u/s. 37(1) of the Act. Copy of the order is placed on record.

56. Ld. DR vehemently supported the orders of the authorities below.

57. We have heard the rival submissions and perused the orders of the authorities below. On a perusal of the order of the Tribunal, we find that identical issue arouse for the A.Y. 2007-08 and the tribunal allowed the alternative claim of the assessee that expenditure incurred on clinical trials outside the in-house facility is eligible for deduction u/s. 37(1) of the Act observing as under: -

> *"5.5. We have considered the submissions made by both the sides and gone through the orders passed by the lower authorities and material placed before us for our consideration. Since, main claim of assessee with respect to deduction u/s 35(2AB) was not seriously pressed before us, therefore, same is dismissed. With respect to alternate claim made by the assessee u/s 37(1) of the Act, it is noted that the invoice of M/s. Reliance Clinical Research Services Pvt. Ltd. dated 31.03.2007 is enclosed at page no. 3 of the paper book, showing that payment has been made to the said company under the head "Clinical Trial Fees" – for the month of March, 2007 for time spent on 1st March to 31st March, 2007 for conducting clinical trials, in support of to all 'K projects', for a sum of Rs.57,65,564/-. It is further noted that on the back side of the invoice, complete details have been given with respect to time spent by 22 employees of RCRS, also giving particulars of the studies done by these employees. Names of these employees have been given along with*

their rates per hour. It is further noted that ld. Assessing Officer has shown no doubts about the genuineness of these expenses. It was held by Ld. CIT(A) that since claim of assessee with respect to deduction u/s.35(2AB) has been denied, therefore, these expenses are capital in nature. It was further observed by ld. CIT(A) that Assessing Officer, as well as assessee, have treated these expenses as capital in nature. In our view, the observations of Ld. CIT(A) are misplaced and without any basis. We have gone through details of these expenses. In our considered view, these expenses are apparently revenue in nature. Ld DR also could not point out as to which expenses are capital in nature. Thus, in our view, these expenses are of revenue nature.

5.6. The other argument of Ld DR was that assessee did not claim these expenses u/s 37 and did not treat them as revenue in nature, and therefore assessee should be precluded from claiming benefit of these expenses, now at this stage, irrespective of this fact that these expenses may have been held as allowable, if the assessee would have made its claim correctly as per law, at the time of filing of return. We have carefully considered this argument, but find that it is not sustainable in the eyes of law, in the given facts and circumstances of the case, and in view of well settled position of law. In our view, there are no estoppels against law. Even if, assessee agrees or consents for something contrary to law, the A.O. is obliged under the law, to discharge his duty of making fair assessment of income and to compute amount of tax payable as per law. As per Article 265 of the Constitution of India, "No tax can be collected except by authority of law". Hon'ble Supreme Court in the case of Ramlal vs Rewa Coalfield Ltd (AIR 1962 SC 361), held that the state authorities should not raise technical pleas if the citizens have a lawful right, which is being denied to them merely on technical grounds. The state authorities cannot adopt the attitude which private litigants might adopt. Further, we place our reliance on the judgment of Hon'ble Delhi High Court in the case of CIT vs Bharat General Reinsurance Co Ltd 81 ITR 303 (Del.) Relevant portion is reproduced below:

> *"It was true that the assessee itself had included that dividend income in its return for the year in question, but there was no estoppel in the Income-tax Act and the assessee having itself challenged the validity of taxing the dividend during the year of assessment in question, it must be taken that it had resiled from the position which it had wrongly taken while filing the return. Quite apart from it, it was incumbent on the income-tax department to find out whether a particular income was assessable in the particular year or not. Merely because the assessee wrongly included the income in its return for a particular year, it could not confer jurisdiction on the department to tax that income in that year even though legally such income did not pertain to that year. Therefore the income*

from dividend was not assessable during the assessment year 1958-59, but it was assessable in the assessment year 1953-54. It could not, therefore, be taxed in the assessment year 1958-59."

Further reliance is placed by us on another judgment of Hon'ble Gujarat High Court, in the case of, S.R. Koshti 276 ITR 165 (Guj) in which relief was granted to assessee with following observations:

"The authorities under the Act are under an obligation to act in accordance with law. Tax can be collected only as provided under the Act. If an assessee, under a mistake, misconception or on not being properly instructed, is over-assessed, the authorities under the Act are required to assist him and ensure that only legitimate taxes due are collected."

In the case of Snehlata 192 CTR 50, Hon'ble J&K High Court held that "when the substantive law confers a benefit on the assessee under a statute, it cannot be taken away by the adjudicatory authority on mere technicalities. It is settled proposition of law that no tax can be levied or recovered without authority of law. Article 265 of the Constitution of India and section 114 of the State (J&K) Constitution imposes an embargo on imposition and collection of tax if the same is without authority of law."

Lastly, we find it useful to refer to judgment of Hon'ble Bombay High Court in the case of Central Provinces Manganese Ore 112 ITR 734, holding that, the mere fact that a deduction was not claimed before the Income-tax Officer, was not of much importance, since if the liability arises then a claim can be made in a bonafide manner at any stage before the higher authority, who is competent to grant relief.

Thus, in view of aforesaid discussion, coupled with facts and circumstances of this case and clear position of law, as discussed above, in our opinion there was no reason to deny the claim assessee u/s 37 of the Act. Therefore, the AO is directed to allow these expenses u/s 37 of the Act. Accordingly, ground no.2 of the assessee's appeal is partly allowed."

58. Facts being identical following the order of the Tribunal we allow the claim of the assessee that the said expenditure should be allowed u/s. 37 of the Act. Thus, the Assessing Officer is directed to allow this expenditure u/s. 37 (1) of the Act. This Ground is allowed.

59. Ground No.3 is general in nature and no adjudication is required.

60. Ground No. 4 is in respect of Interest-free loans provided to AE, M/s. Reliance Life Science Inc., USA ('M/s. RLSI). In the grounds of appeal assessee contends as under: -

> *(i) The learned CIT(A) erred in determining the arm's length price (ALP) of interest chargeable in respect of interest free loan advanced to M/s. RLS Inc at INR 1,30,16,828.*
>
> *(ii) Further, the learned CIT(A) failed to appreciate that no interest was chargeable on the above referred loan, since the same loan was optionally convertible into share capital.*
>
> *(iii) Without prejudice to the above, the learned CIT(A) erred in determining the arm's length rate at LIBOR plus 300 basis points without providing any reasons for considering mark-up of 300 basis points over LIBOR instead of determining the arm's length rate of interest at LIBOR plus comparable mark-up rate furnished by the Appellant of 165 basis points*.

61. Ground No.4 is identical to Ground No. 3 for the A.Y. 2009-10. Facts' being identical to the case of assessee for the A.Y. 2009-10, the decision rendered therein applies mutatis mutandis to the appeal for the Assessment year under consideration i.e. A.Y. 2010-11. We order accordingly.

62. Ground Nos. 5 & 6 are in respect of subscription to share application money paid to RLSI & RLSBV treated as deemed loan and interest was charged thereon. In the grounds of appeal assessee contends as under:

> *(i) The learned CIT(A) erred in determining the arm's length price (ALP) of interest chargeable in respect of subscription to equity share capital of M/s. RLS Inc at INR 50,11,071/-.*

(ii) The learned CIT(A) erred in confirming the action of the learned AO in treating the subscription money as a deemed interest free loan on which interest is chargeable.

(iii) Without prejudice to the above, the learned CIT(A) erred in determining the arm's length rate at LIBOR plus 300 basis points without providing any reasons for considering mark-up of 300 basis points over LIBOR instead of determining the arm's length rate of interest at LIBOR plus comparable mark-up rate furnished by the Appellant of 165 basis points.

Ground NO.6: Subscription to share application money paid to M/s. Reliance Life Science BV, Netherlands ('M/s RLS BV) treated as a deemed loan and interest charged thereon

(i) The learned CIT(A) erred in determining the arm's length price (ALP) of interest chargeable in respect of subscription to preference share capital of M/s. RLS Inc at INR 1 ,55,20,711/-.

(ii) The learned CIT(A) erred in confirming the action of the learned AO in treating the subscription money as a deemed interest free loan on which interest is chargeable;

(iii) Without prejudice to the above, the learned CIT(A) erred in determining the length rate at LIBOR plus 300 basis points without providing any reasons for considering mark-up of 300 basis points over LIBOR instead of determining the arm's length rate of interest at LIBOR plus comparable mark-up rate furnished by the Appellant of 165 basis points.

63. Ground Nos. 5 & 6 are identical to Ground No. 4 for the A.Y. 2009-10. Facts' being identical to the case of assessee for the A.Y. 2009-10, the decision rendered therein applies mutatis mutandis to the appeal for the Assessment year under consideration i.e. A.Y. 2010-11. We order accordingly.

64. Coming to the last Ground of appeal i.e. Ground No. 7, assessee challenged the order of the Ld.CIT(A) in determining the arm's length price

of net interest chargeable in respect of outstanding balances of the AE M/s. Reliance Genemedix [RGMX] and the ground reads as under: -

> *"Ground no 7:*
>
> *(i) Learned CIT(A) erred in determining the arm's length price (ALP) of net interest chargeable in respect of outstanding balance of the AE, M/s Reliance GeneMedix at INR 3,80,129/-.*
>
> *(ii) Further, the learned CIT(A) failed to appreciate that no interest was chargeable on the above referred outstanding balance, since the balances are in respect of debtors and creditors which are a part of routine day to day business activities and cannot be equated with loan;*
>
> *(iii) Without prejudice to the above, the learned CIT(A) erred w determining the arm's length rate at LIBOR plus 300 basis points without providing any reasons for considering mark-up of 300 basis points over LIBOR instead of determining the arm's length rate of interest at LIBOR plus comparable mark-up rate furnished by the Appellant of 165 basis points"*

65. Briefly stated the facts are that, during the F.Y. 2009-10 relevant to assessment year 2010-11 a sum of ₹.2,47,28,860/- was shown as due from RGMX as sundry debtor and a sum of ₹.96,52,341/- was shown as due to the said party as sundry creditor as on 31.03.2010 in the books of accounts by the assessee. Assessing Officer noticed that said amount due from RGMX was received and paid during various dates in the subsequent financial year. Assessee also furnished those details before the assessing officer. The TPO treated the outstanding balances of AE RGMX both in respect of sundry debtors and creditors as loan and determined the arm's length price of interest at 12% per annum by applying the PLR instead of adopting rate applicable in respect of the short

term borrowing, since balance in respect of sundry debtors and creditors according to him were part of routine day to day business activities and cannot be equated with loan. Assessee contended that as per its consistent policy it has not charged/paid any interest on its receivables/payable from non-AE's i.e. 3rd party business transactions. It was also contended that during the year under proceedings the assessee neither charged interest on its receivable nor it has paid any interest on its payables to its AE RGMX. Thus, it is contended that on application of the arm's length price taking assessee as a tested party and CUP as the most appropriate method, no interest adjustment can be made. However not convinced with the submissions of the assessee Ld. TPO made adjustment for receivable by calculating the net interest on net balances outstanding debtors and creditors with AE RGMX. Ld.CIT(A) sustained the adjustment.

66. Before us, the Ld. Counsel for the assessee submits that as per its consistent policy, it has not charged/paid any interest on its receivables/payables from Non-AEs i.e. third-party business transactions. Further, during the year under proceedings, the assessee has neither charged any interest on its receivables nor it has paid any interest on its payables to its AE RGMX. Hence, on application of the ALP, taking the Assessee as a tested party and CUP as the most appropriate method, the

adjustment for interest made by the TPO cannot be sustained. In support of his contention assessee placed reliance on the following decisions wherein the Hon'ble High Court and Tribunal has held that if there is complete uniformity in the act of the Assessee in not charging interest from both the AEs and Non AEs for the outstanding receivables, no adjustment of notional interest is called for –

(i) CIT vs Indo American Jewellery Ltd (ITA No. 1053 of 2012) (Bombay HC)
(ii) CIT v/s Livingstones (ITA No 887 OF 2014) (Bombay HC)
(iii) ACIT v/s Gitanjali Exports Corporation Limited (ITA No. 7662/Mum/2013) (Mumbai Tribunal)

67. Ld. Counsel for the assessee further submits that the CIT(A) has not given any finding on the merits of the issue and merely proceeded to determine ALP interest rate on the basis of alternative plea of the Assessee. Therefore, the adjustment confirmed by the CIT(A) cannot be sustained.

68. Ld. Counsel for the assessee further without prejudice to the above, submits that if at all any interest should be charged, the following should be considered:

(i) Hon'ble Bombay HC in the case of Pr CIT v/s Tecnimont Pvt Ltd in ITA No 56 of 2016 dated 03.07.2018 has upheld LIBOR as ALP for interest bearing loans given to the AE in foreign currency. Therefore, in the case of the Assessee, Libor should be adopted as ALP.

(ii) Alternatively, the Assessee's AE Reliance Pharmaceuticals Pvt Ltd had taken a loan from the third party Axis Bank Ltd @ LIBOR plus 1.65% p.a. which has been accepted as a valid CUP for interest bearing loans given to the AE. The same may be adopted.

69. Ld. DR vehemently supported the orders of the authorities below. Ld. DR further submits that the geography in which the AE and the Non AE operate are different and therefore the assessee not charging interest to the non AE under similar circumstances cannot be taken as CUP. In reply Ld. Counsel for the assessee submitted that different geography filter shall be a factor of consideration while determining the arm's length rate of interest to be charged for the amount advanced/outstanding to/from the AE and non AE. When the consistent policy of the assessee is not to charge interest from AE as well as non-AE and there is outrightly, no charge of interest on outstanding balances from the AE as well as non AEs, geography filter does not come into picture. In light of the aforesaid submissions, the assessee prays, that no interest ought to have been charged on amounts due from the AE, RGMX and consequently, the adjustment to the income be deleted.

70. We have heard both the parties perused the orders of lower authorities and the case law relied on. We find that in the case of

CIT *v.* Indo American Jewellery Ltd. in ITA.No. 1053 of 2012 dated 08.01.2013 the Hon'ble Bombay High Court held as under:

> *"3 As regards the second question is concerned, the Transfer Pricing Officer while determining the Arms Length Price of the international transactions, noticed that the outstanding balance from Associated Enterprises was amounting to Rs.8.76 crores. As that amount was outstanding for more than year, taking the rate of interest at 10%, the Transfer Pricing Officer determined the interest receivable at Rs.87.66 lacs and added the same to the international transaction cost.*
>
> *4 On appeal, the CIT(A) held that the total outstanding amount was Rs.8.73 Crores and out of which the amount outstanding from the Associated Enterprises was to the extent of Rs.5.11 Crores and the balance amount of Rs.3.62 Crores was outstanding from non Associated Enterprises. Relying on the Board Circular no. 12 of 2001, the CIT(A) further held that in the present case, the profit of one Associated Enterprise is negligible and the other Associated Enterprise has incurred losses and therefore it cannot be said that the assessee had transfered any profit to the Associated Enterprises outside India by not charging interest on the outstanding payment which has been realised after the due date and accordingly deleted the interest charged on late realisation of the export proceeds.*
>
> *5. On appeal filed by the Revenue, the ITAT upheld the order of CIT (A). While, upholding the order of CIT (A), the ITAT held that interest income is associated only with the lending or borrowing of money and not in case of sale. We express no opinion on the above reasoning of the ITAT and keep that reasoning open for debate in an appropriate case. However, in the facts of the present case, the specific finding of the ITAT is that there is complete uniformity in the act of the assessee in not charging interest from both the Associated Enterprises and Non Associated Enterprises- debtors and the delay in realization of the export proceeds in both the cases is same. In these circumstances, the decision of the Tribunal in deleting the notional interest on outstanding amount of export proceeds realized belatedly cannot be faulted."*

71. Similarly, in the case of CIT *v.* M/s. Lingingstones in ITA.No. 887 of 2014 dated 28.11.2016 the Hon'ble Jurisdictional High Court held as under: -

"3. The grievance of the revenue is that the respondent-assessee granted longer period of credit to its Associated Enterprises on sale of goods as compared to the period of credit granted to Non Associated Enterprises. Consequently the notional interest on delayed collection of consideration on sale of goods to Associated Enterprises needs to be added to the declared consideration to arrive at an arms length price

4. The Tribunal by the impugned order rendered a finding of fact that the respondent-assessee has not charged any interest from third parties i.e. Non Associated Enterprises on delayed payments exceeding more than 300 to 400 days from the sale of goods. Consequently, it holds that once such delayed payment in respect of sale of goods made to third parties carries no interest, then adding of notional interest to delayed payments made by the Associated Enterprises is not called for

5. Further, the impugned order places reliance upon the order of this Court in Income Tax Appeal (L) No. 1053 of 2012 (Commissioner of Income Tax-9 vs. M/s.Indo Amercian Jewellery Ltd.) rendered on 8th January, 2013. In the above case a similar question was not entertained by this Court on the ground that there is complete uniformity in the act of the assessee therein in not charging interest from Associated Enterprises and Non Associated Enterprises for delay in recovery of its sale proceeds.

6. In the present case also the Tribunal has rendered a finding of fact that the interest is not being charged in case of sales made to Non-Associated Enterprises for delayed payment just as in the case of Associated Enterprises. These finding of fact rendered by the Tribunal is not shown to be perverse in any manner."

72. In the case before us also as a consistent policy, assessee has not charged any interest on its receivables from non-AE's i.e. third party business transactions. Assessee has not paid any interest on payables to non-AE's. Further, we observe during the year under consideration assessee has neither charged interest on its receivable nor has paid any interest on its payables to its AE RGMX. Therefore, we observe that there is complete uniformity in the act of the assessee in not charging interest

from both AE's and non-AE'S for the outstanding receivables. In such circumstances the ratios of the above decisions relied on by the assessee are squarely applicable to the facts of assessee. Thus, respectfully following the said decisions we hold that no interest can be charged on amounts due from AE RGMX and consequently the adjustment made by the TPO is directed to be deleted. This ground of appeal is allowed.

73. In the result, appeal of the assessee is partly allowed as indicated above.

Order pronounced in the open court on the 30th September, 2019

Sd/-	Sd/-
(N.K. PRADHAN)	**(C.N. PRASAD)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Mumbai / Dated 30/09/2019
Giridhar, Sr.PS

Copy of the Order forwarded to:

1. The Appellant
2. The Respondent.
3. The CIT(A), Mumbai.
4. CIT
5. DR, ITAT, Mumbai
6. Guard file.

//True Copy//

BY ORDER

(Asstt. Registrar)
ITAT, Mum