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

BEFORE SHRI PRAMOD KUMAR, VICE PRESIDENT AND
SHRI SAKTIJIT DEY, JUDICIAL MEMBER

ITA no.4210/Mum./2014
(Assessment Year : 2008–09)

Ciba India Ltd.
(Through their successors BASF India Ltd.)
Vibgyor Towers, Unit no.101, 1st Floor
Block–C–62, Bandra Kurla Complex
Bandra (E), Mumbai 400 051
PAN – AAACC4147P

……………. Appellant

v/s

Jt. Commissioner of Income Tax (OSD)
Range–8(1), Mumbai

……………. Respondent

Assessee by : Shri Madhur Agrawal a/w
Shri Milin Thakkar and
Ms. Nyrica Trikannad
Revenue by : Shri Anand Mohan

Date of Hearing – 03.12.2020	Date of Order – 16.02.2021

O R D E R

PER SAKTIJIT DEY. J.M.

Captioned appeal has been filed by the assessee challenging the order dated 30th December 2013, passed by the learned Commissioner of Income Tax (Appeals)–10, Mumbai, pertaining to the assessment year 2008–09.

2. In ground no.1, the assessee has challenged the addition of ₹ 3,72,46,953, on account of transfer pricing adjustment.

3. Brief facts are, as stated by the Transfer Pricing Officer, the assessee, a resident company, is engaged in the business of manufacturing and trading in a wide range of specialty chemicals which are sold both in domestic as well as export market. The assessee is a part of CIBA Group, a leading Global Specialty Chemical company, having its headquarters at Basel in Switzerland. During the year under consideration, the assessee had entered into various international transactions with its Associated Enterprises (AEs), one amongst them being payment of ₹ 3,72,43,953, towards cost allocation of ERP system implemented by the AE. While examining the arm's length nature of payment made towards integrated enterprise source planning software manufactured by SAP AG (in short *"SAP ERP"*), he found that the assessee had benchmarked the transaction by applying Transactional Net Margin Method (TNMM) and claimed it to be at arm's length. The Transfer Pricing Officer, however, was not convinced with assessee's claim. Accordingly, he issued a show cause notice to the assessee to explain why the arm's length price of such cost recharge should not be treated as nil, or, to the extent the assessee establishes the benefit received from such payment. Further, the Transfer Pricing Officer also called upon the assessee to furnish

documentary evidences for cost allocation towards ERP services. In response to the query raised, the assessee furnished its reply along with supporting documentary evidences including agreement with AE for ERP services termed as *"ERP systems cost sharing agreement"* executed on 7th November 2005. On a perusal of the said agreement, the Transfer Pricing Officer found that the agreement for SAP ERP implementation was for a period of four years and allocation key for cost is net sales. In the submissions made, it was submitted by the assessee that the SAP ERP licences were implemented in India on 31st March 2008. The Transfer Pricing Officer observed, as per assessee's claim the cost sharing for implementation of ERP system was between the entire group and it has been allocated to 51 group entities including the present assessee. Thus, the cost was allocated to all the group entities without any mark–up. Therefore, the assessee applied Comparable Uncontrolled Price (CUP) method as price charged to other group companies was available as internal CUP. The Transfer Pricing Officer, however, did not accept the claim of the assessee. He observed, the assessee has not furnished any evidence to establish that the services were actually received or even if such services were received, any tangible benefit was derived by the assessee. Having held so, the Transfer Pricing Officer proceeded to determine the arm's length price by using external CUP by way of comparables available in

a particular data base. Thus, ultimately, the Transfer Pricing Officer concluded that since the assessee has failed to establish the benefit derived by implementing the SAP ERP system the arm's length price of the transaction has to be determined at nil. Therefore, the entire payment made of ₹ 3,72,46,953, was proposed as adjustment and added back to the income of the assessee in the assessment order.

4. The assessee contested the aforesaid adjustment before the first appellate authority. However, learned Commissioner (Appeals) concurred with the view expressed by the Transfer Pricing Officer.

5. The learned Counsel for the assessee, drawing our attention to the agreement entered with the AE for SAP ERP implementation submitted, the assessee had entered into the agreement for replacing the existing fragmented system of various CIBA Group entities by implementing a single new ERP system spanning over a period of four years. He submitted, similar agreement for implementing of SAP ERP was entered by all CIBA Group entities with the Head Office. He submitted, as per the terms of the agreement, the assessee has to pay cost for ERP on the basis of actual cost incurred by the Head Office without any mark–up. He submitted, surmising that the assessee has not derived any benefit from implementation of ERP system, the Transfer Pricing Officer has treated the arm's length price as nil. He

submitted, by implementing the ERP system the assessee has availed key benefits by way of reduced operating cost, better accessibility, maintaining the budget and variation with the budget, better inventory, management, etc. He submitted, the specific benefits derived by the assessee were submitted before the Transfer Pricing Officer vide letter dated 25th October 2011. He submitted, the AE has engaged external software and advisory firm and has delegated a number of highly qualified staff to implement the project on a full time basis for a four year development period to ensure that the ERP system meets the specific need of all the group entities including the assessee. He submitted, the Departmental Authorities failed to appreciate that the ERP system was implemented in a span of four years and every year the assessee had to pay for the modules implemented or upgraded. Therefore, the payment made for four years is for gradual implementation of various modules. He submitted, apart from furnishing the cost sharing agreement, the assessee has furnished various other documents including the certificate from independent auditors to establish that cost for implementation of ERP system was allocated to all the group entities without any mark–up. He submitted, the debit note issued by the AE was also furnished before the Transfer Pricing Officer. He submitted, without properly verifying the documentary evidences, the Transfer Pricing Officer has

determined the ALP at nil. He submitted, the reliance placed by the Transfer Pricing Officer on a particular database is wholly misconceived as the said database is a independent technology and service professional providing SAP end users training to the personnel to help them in building skills required for job profiles involving day–to–day activities like posting of invoices, creation of master records and generating of reports. It also provides services for end user jobs in entities that have implemented SAP ERP. He submitted, while the assessee has implemented an advance version of SAP ERP system, the Transfer Pricing Officer has considered comparables implementing older versions. Further, the data of comparables is not contemporaneous and ranges from 2001 to 2006. He submitted, while the assessee has provided the details of cost charged to CIL, which relates to cost of software, hardware and infrastructure including personnel cost, no such data relating to the comparables was provided by the Transfer Pricing Officer. In this context he drew our attention to various distinguishing features as furnished in the chart. He submitted, as per the transfer pricing provisions, the Transfer Pricing Officer is required only to determine the arm's length price of a particular transaction. It is not his duty to examine whether the transaction was actually required to be undertaken or the nature of benefit received from such transaction. He submitted, without following any specific

method to determine the arm's length price he has perfunctorily determined the arm's length price at nil by applying the benefit test. Thus, he submitted, the adjustment made has to be deleted. In support of such contention, the learned Authorised Representative relied upon the following decisions:–

1. *DCIT v Danisco (India) (P.) Ltd. (63 taxmann.com 174)(ITAT Delhi)*
2. *Akzo Nobel India Ltd. v DCIT (81 taxmann.com 366)(ITAT Kolkata)*
3. *DCIT v Diebold Software Services (P.) Ltd. (48 taxmann.com 26 (Mum.)*
4. *Festo Controls Private Ltd. v DCIT (30 taxmann.com 16)(Bang.)*
5. *Merck Ltd. v/s DCIT (37 taxmann.com 433)(ITAT Mumbai)*
6. *Trumpf India Private Limited Vs. DCIT (ITA No. 977/Mum./2014*
7. *CIT v EKL Appliances Ltd. (345_ ITR 241)(Delhi)*
8. *Safran Aerospace India Pvt. Ltd. v DCIT (ITA No.1261/Bang/2010)*
9. *Daikin Airconditioning India (P) Ltd v DCIT (92 taxmann.com112 (Del.)*
10. *Schneider Electric India (P.) Ltd. vDCIT (82 taxmann.com 364*
11. *CorningSAS-India Branch Office vDDIT(82 taxmann.com 444 (Del.)*
12. *Honda Motor India (P.) Ltd. vDCIT (88 taxmann.com 137)(ITAT Del.)*
13. *TNS India (P.) Ltd. v ACIT (48 taxmann.com 128)(ITAT Hyderabad)*
14. *Ingersoll Rand (India) Ltd. v DCIT (67 taxmann.com 328) ITAT*
15. *Dresser-Rand India Pvt. Ltd. v Addl.CIT (13 taxmann.com 82 (Mum.)*
16. *Castrol India Ltd. v ACIT (ITA No.3938–4413/M/2010)(Mum.)*
17. *CIT v Excel Industries Ltd. (358 ITR 295)(SC)*
18. *CIT v Arthur Andrson & Co. (318 ITR 229)(Bom)*
19. *Clariant Chemicals (India) Ltd. v JCIT (44 taxmann.com 421)Mum.*
20. *Thomas Cook (India) Ltd. v DCIT (70 taxmann.com 322)*
21. *Benetton India (P.) Ltd. v DCIT (87 taxmann.com 241) (Del.)*
22. *Qual Core Logic Ltd v DCIT (22 taxmann.com 4) (Hyd.)*
23. *ACIT v MSS India (P) Ltd (32 SOT 132) (Pune)*
24. *McCann Erickson India Pvt. Ltd. v ACIT (24 taxmann.com 21 (Del.)*

6. The learned Departmental Representative, strongly relying upon the observations of the Transfer Pricing Officer and learned Commissioner (Appeals) submitted, the assessee has to prove through supporting evidence that any international transaction conducted with the AE is at arm's length. He submitted, in the present case, there are

concurrent findings of the Transfer Pricing Officer and learned Commissioner (Appeals) that the assessee has failed to furnish any supporting evidence to prove the benefit derived for implementation of SAP ERP. Therefore, the adjustment made is proper.

7. We have considered rival submissions in the light of the decisions relied upon and perused the material on record. On a perusal of the order passed by the Transfer Pricing Officer, we find that in the course of the proceedings, the assessee had furnished the agreement entered with the AE for implementation of SAP ERP system as well as various other documentary evidences including the debit note raised by the AE towards allocation of cost. It is also a fact that the AE has entered into similar agreement with 51 other group entities towards cost allocation for implementing SAP ERP system. Therefore, the cost charged to other AEs in the group is certainly available with the assessee as CUP for comparing the transaction with the AE. It is also a fact that ERP implementation has started from preceding years and spanned over a period of four years. The payment made by the assessee towards implementation of SAP ERP system in the preceding assessment years has been accepted by the Transfer Pricing Officer to be at arm's length. It is also evident from the order of the Transfer Pricing Officer, he has not disputed the fact that the AE has implemented SAP ERP system for assessee's business in India. That being the case, the cost

paid by the assessee for implementation of SAP ERP system without any mark–up cannot be treated as nil by applying the benefit test. It is for the assessee to decide whether a particular system or investment would be beneficial to him or not. The Transfer Pricing Officer certainly cannot step into the shoes of the assessee or the Assessing Officer to evaluate the business expediency of a cost incurred for business purpose and the benefit derived. His job is to determine the arm's length price by adopting any one of the prescribed methods. In the facts of the present case, though, the Transfer Pricing Officer has stated that he has adopted CUP method for determining the arm's length price, however, in reality, he has determined the arm's length price at nil on purely ad–hoc basis by stating that the assessee has not derived any benefit. Moreover, the allegations of the Transfer Pricing Officer and learned Commissioner (Appeals) that the assessee has failed to furnish supporting evidence to establish its claim is found to be baseless as the assessee has furnished sufficient documentary evidences not only to prove the implementation of SAP ERP system but also the benefit derived by it from such system. Moreover, when the Transfer Pricing Officer has accepted the payment made towards SAP ERP implementation in the earlier years, there is no reason to deny the same in the current year by determining the arm's length price at nil. In any case of the matter, it is a fact on record that the assessee has

implemented the SAP ERP system and is utilizing it for its business purpose. The Transfer Pricing Officer has also stated that SAP ERP system is a necessary tool for carrying out business works. That being the case, the determination of arm's length price at nil, that too, on ad–hoc basis is unsustainable. Accordingly, we have no hesitation in deleting the addition made on account of transfer pricing adjustment. This ground is allowed.

8. In ground no.2, the assessee has challenged the disallowance of ₹ 43,96,080, under section 14A of the Act.

9. Brief facts are, during the assessment proceedings the Assessing Officer noticed that in the year under consideration, the assessee has received exempt income by way of dividend amounting to ₹ 34,76,240. Whereas, it has not disallowed any expenditure for earning the exempt income. When called upon to explain, the assessee submitted that it has not incurred any expenditure for earning the exempt income. The Assessing Officer, however, was not convinced and proceeded to compute the disallowance at ₹ 68,21,468, by applying rule 8D.

10. Though, the assessee contested the aforesaid disallowance, however, it was unsuccessful.

11. The learned Counsel for the assessee submitted, since the assessee had sufficient surplus fund available with it, no disallowance of interest expenditure under rule 8D(2)(ii) can be made. To impress upon the fact that the assessee had sufficient interest free funds, the learned Counsel for the assessee drew our attention to Page–25 of learned Commissioner (Appeals)'s order. As regards the disallowance of administrative expenditure under rule 8D(2)(iii), the learned Counsel for the assessee submitted, only those investments which have yielded exempt income during the year should be considered for computing disallowance. In this regard, he drew our attention to a chart showing disallowance computed at ₹ 3,91,961.79.

12. We have considered rival submissions and perused the material on record. As regards the disallowance of interest expenditure under rule 8D(2)(ii), the contention of the learned Counsel for the assessee is twofold. Firstly, no interest disallowance should be made when the assessee has surplus interest free fund available with it. Secondly, only those investments which have yielded exempt income during the year should be considered for disallowance under rule 8D(2)(iii). On a perusal of impugned order of learned Commissioner (Appeals), we find that the assessee had made a submission that as against the interest free surplus funds available of ₹ 281,90,44,000, investment stood at ₹ 150,85,55,000. Thus, from the aforesaid submission, it is evident that

the assessee had sufficient interest free fund available with it to take care of the investment. Therefore, as per the settled legal principles, no disallowance of interest expenditure can be made under rule 8D(2)(ii). Hence, the disallowance made under rule 8D(2)(ii) has to be deleted. As regards disallowance of administrative expenditure under rule 8D(2)(iii), we direct the Assessing Officer to compute such disallowance by taking into account only those investments which have yielded dividend income during the year. In this regard, the Assessing Officer is directed to verify the correctness of disallowance computed by the assessee at ₹ 3,91,961.79. This ground is disposed off accordingly.

13. In ground no.3, the assessee has challenged the disallowance of ₹ 14,94,029, under section 43B of the Act.

14. In course of assessment proceedings, the Assessing Officer noticed that the assessee had claimed deduction of ₹ 14,94,029, on account of leave encashment paid by Huntsman International India Pvt. Ltd. Relying upon the assessment order passed for assessment year 2007–08, wherein, similar claim made by the assessee was disallowed pursuant to the directions of the DRP, he disallowed the deduction claimed by the assessee.

15. Learned Commissioner (Appeals) also sustained the disallowance.

16. The learned Counsel for the assessee submitted, while deciding identical issue in assessment year 2007–08, the Tribunal has restored it back to the Assessing Officer. Therefore, he submitted, let it be restored in the impugned year as well.

17. The learned Departmental Representative also agreed for restoration of the issue.

18. Having considered rival submissions, we find that while deciding the issue in assessee's own case for the assessment year 2007–08, the Tribunal in ITA no.759/Mum./2012 has restored the issue to the Assessing Officer for fresh adjudication. Facts being identical, following the aforesaid decision of the Co–ordinate Bench, we restore the issue to the Assessing Officer for fresh adjudication. Ground is allowed for statistical purposes.

19. In ground no.4, the assessee has challenged the disallowance of depreciation claimed on the WDV of the royalty expenditure.

20. The learned Counsel for the assessee submitted, in the assessment year 2001–02, the assessee had claimed certain amount towards expenditure for payment of royalty which was disallowed by the Assessing Officer and the first appellate authority as capital expenditure. He submitted, while deciding the issue, the Tribunal,

though, was of the view that the expenditure claimed is capital in nature, however, depreciation was allowed on such expenditure. Thus, he submitted, by virtue of such decision of the Tribunal consequential benefit has to be given to the assessee.

21. The learned Departmental Representative submitted, if the Tribunal has allowed depreciation to the assessee in preceding assessment years, consequential benefit can be given to the assessee.

22. Having considered rival submissions, we find that the royalty expenditure incurred by the assessee in the assessment year 2001–02 was held to be of capital in nature. However, the Tribunal directed the Assessing Officer to allow depreciation on such expenditure. Therefore, when depreciation has been allowed to the assessee on the expenditure incurred on royalty in the preceding assessment years, consequential benefit of depreciation has to be allowed to the assessee in the impugned assessment year as well. The ground raised by the assessee is allowed.

23. In the result, appeal is partly allowed.
Order pronounced in the open court on 16.02.2021

Sd/-	**Sd/-**
PRAMOD KUMAR	**SAKTIJIT DEY**
VICE PRESIDENT	**JUDICIAL MEMBER**

MUMBAI, DATED: 16.02.2021

<u>Copy of the order forwarded to</u>:

(1) The Assessee;

(2) The Revenue;

(3) The CIT(A);

(4) The CIT, Mumbai City concerned;

(5) The DR, ITAT, Mumbai;

(6) Guard file.

True Copy
By Order

Pradeep J. Chowdhury
Sr. Private Secretary

Assistant Registrar
ITAT, Mumbai