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

Before Sh. Amit Shukla, Judicial Member

Dr. B. R. R. Kumar, Accountant Member

ITA No. 113/Del/2021 : Asstt. Year: 2016-17

Pepsico India Holdings Pvt. Ltd., Level 3-6, Pioneer Square, Sector-62, Golf Course, Extension Road, Gurgaon, Haryana-122101	Vs	ACIT, Central Circle-07, New Delhi
(APPELLANTT		**(RESPONDENT)**
PAN No. AAACP1272G		

SA No. 22/Del/2021 : Asstt. Year: 2016-17

Pepsico India Holdings Pvt. Ltd., Level 3-6, Pioneer Square, Sector-62, Golf Course, Extension Road, Gurgaon, Haryana-122101	Vs	ACIT, Central Circle-07, New Delhi
(APPELLANTT		**(RESPONDENT)**
PAN No. AAACP1272G		

Assessee by : Sh. Deepak Chopra, Adv.
Revenue by : Ms. Meera Srivastava, CIT DR

Date of Hearing: 23.03.2021		**Date of Pronouncement: 04.05.2021**

ORDER

Per Dr. B. R. R. Kumar, Accountant Member:

The present appeal and Stay Application have been filed by the assessee against the order dated 22.01.2011 passed by the AO u/s 143(3) r.w.s. 144C(13) of the Income Tax Act, 1961.

2. Following grounds have been raised by the assessee:

"1. That on the facts and circumstance of the case, the order passed by the Ld. Assistant Commissioner of Income Tax, Central Circle - 7, New Delhi ("AO"),

to the extent is prejudicial to the Appellant, is bad in law.

2. That on the facts and circumstances of the case, the AO erred in computing the total income of the Appellant at INR 289,43,50,4721- as against the returned loss of INR 282,26,40,528/-.

Transfer Pricing Adjustment on account of Advertisement, Marketing and Promotion ("AMP") Expenses

3. That the Transfer Pricing Officer ("TPO")/ Dispute Resolution Panel ("DRP")/ AO have erred in computing and sustaining Transfer Pricing Adjustment on account of AMP Expenses to the tune of INR 571,69,91,000/-.

4. That the TPO/DRP/AO erred in not following the decision of this Hon'ble Tribunal in Appellant's own case for immediately preceding years, wherein this Hon'ble Tribunal deleted identical Transfer Pricing Adjustment on account of AMP Expenses.

5. That the TPO/DRP/AO, despite duly making a note of the decision of this Hon'ble Tribunal rendered in the identical facts in the Appellant's own case for the preceding years, erred in not giving effect to the same, thereby passing a patently untenable order.

6. Without prejudice, the TPO/DRP/AO erred in observing that the Appellant was a subsidiary of Holland based company and was carrying out distribution activities as well as development of marketing intangibles for its Associated Enterprise ("AE"), all of which is factually incorrect.

7. Without prejudice, the TPO/DRP/AO erred in ignoring that the Appellant was a full fledged licensed manufacturer in India.

8. Without prejudice, the TPO/DRP/AO erred in ignoring various decisions of the Hon'ble jurisdictional

High Court / Tribunal, which clearly state that no adjustment can be made on account of AMP Expenses in the case of a licensed manufacturer, until and unless the Department demonstrates the existence of an explicit agreement / arrangement between the assessee and its AE for the purposes of incurring AMP Expenses.

9. Without prejudice, the TPO/DRP/AO grossly erred in assuming jurisdiction under section 92CA of the Income-tax Act, 1961 ("Act"), in respect of transactions which did not partake the character of "international transactions" within the meaning of the term, as defined in section 92B of the Act read with section 92F(v) of the Act.

10. Without prejudice, the TPO/DRP/AO failed to discharge the preliminary onus placed upon them, viz. to establish the existence of any "arrangement", whereby the AE, being the owner of the intellectual property, had directed any level of AMP Expense to be incurred by the Appellant.

11. Without prejudice, the TPO/DRP/AO grossly erred in concluding that carrying out of AMP expenses was an "international transaction" for the purposes of section 92B of the Act based on assumptions, surmises and conjectures.

12. Without prejudice, the TPO/DRP/AO erred in concluding that AMP expenses incurred by the Appellant resulted in the enhanced brand value of the brands owned by the AE.

13. Without prejudice, the TPO/DRP/AO erred in concluding that the AE reaped the benefits of marketing activities carried out by the Appellant, without actually demonstrating or quantifying the same.

14. Without prejudice, the TPO/DRP/AO grossly erred on facts and in law in concluding that the AE, being the legal owner of the brands, should have

compensated the Appellant for AMP Expenses incurred by it towards such brands, as the AE derived brand enhancement benefits because of such expenses.

15 Without prejudice, the TPO/DRP/AO erred in ignoring that economic ownership of the brands in question was with the Appellant, as was also acknowledged by the AE owning the said brands.

16 Without prejudice, the TPO/DRP/AO erred in not appreciating that the AMP Expenses already formed part of the benchmarking analysis of the manufacturing segment, which was not disputed by the TPO and therefore, it was not open to benchmark AMP Expenses separately.

17. Without prejudice, the TPO/DRP/AO failed to appreciate that AMP Expenses incurred by the Appellant formed a part of the excisable value of goods and hence, partook the character of "manufacturing expenses", which could not have been re-characterized.

18. Without prejudice, the TPO/DRP/AO failed to appreciate that no benefit, incidental or otherwise, accrued or arose to the AE because of the AMP Expenses incurred by the Appellant since neither "royalty" nor any dividend / profit was repatriated to the said AE as a result of increased sales of the Appellant in India.

19. Without prejudice, the TPO/DRP/AO failed to appreciate that even the Appellant from its AE, for the purposes of its manufacturing products for which AMP Expenses were incurred, were insignificant/ minor as compared to the sales achieved by the Appellant and therefore, on that account as well no benefit could have been said to have arisen to the AE.

20. Without prejudice, the TPO/DRP/AO erred in observing that no royalty was paid by the Appellant to its AE as quid pro quo for the marketing activities carried out by it without compensation from AE.

21. Without prejudice, the TPO/DRP/AO erred in not allowing the benefit of imputed "royalty" taxed in the hands of Pepsi Co. Inc., USA, while computing adjustment on account of AMP Expenses.

22. Without prejudice, the TPO/DRP/AO erred in not appreciating that there was no shifting of profit outside India that warranted any Transfer Pricing Adjustment.

23 Without prejudice, the TPO/DRP/AO erred in adopting the "Other Method", as prescribed under Rule 10AB of the Income-tax Rules, 1962 ("Rules"), as the most appropriate method for the purposes of computing the arm's length price ("ALP") of the alleged "international transaction" of AMP Expenses, incurred by the Appellant.

24 Without prejudice, the TPO/DRP/AO erred in adopting the "Other Method", without justifying the non-applicability of all the other prescribed methods under the Rules, for the purposes of computing the ALP of the alleged "international transaction" of AMP Expenses incurred by the Appellant.

25 Without prejudice, the TPO/DRP/AO erred in applying the Bright Line Method ("BLT"), under the guise of "Other Method", for the purposes of computing the ALP of the alleged "international transaction" of AMP Expenses, incurred by the Appellant.

26. Without prejudice, the TPO/DRP/AO erred in applying BLT in complete ignorance of the precedents set by the Hon'ble jurisdictional High Court against the application of BLT for the purposes of computing the ALP of the alleged "international transaction" of AMP Expenses, incurred by the Appellant.

27. Without prejudice, the TPO/DRP/AO erred in comparing the ratio of AMP/ Sales of the assessee with that of the Pepsi Group globally, while applying BLT for the purposes of computing the ALP of the

alleged "international transaction" of AMP Expenses, incurred by the Appellant.

28. Without prejudice, the TPO/DRP/AO erred in not including the sales made by third party bottlers in the total sales while computing the ratio AMP/ Sales.

29. Without prejudice, the TPO/AO/DRP erred in not carrying out a separate benchmarking analysis, based on domestic comparables, for the purposes of applying BLT for computing the ALP of the alleged "international transaction" of AMP Expenses, incurred by the Appellant.

30. Without prejudice, the TPO/DRP/AO erred in arbitrarily construing the alleged "international transaction" of incurring AMP Expenses as a "service", without bringing any evidence on record to establish such "arrangement" between the Appellant and its AE.

31. Without prejudice, the TPO/DRP/AO grossly erred in arbitrarily imputing a profit margin that the Appellant ought to have earned for the alleged "service" offered by it to the AE by incurring AMP Expenses, based on the global net profitability of the Pepsi Group.

Consequential Grounds

32. That the AO erred in levying interest under section 234A of the Act.

33. That the AO erred in levying interest under section 234B of the Act.

34. That the AO erred in adding back the amount already refunded to the Appellant [including interest under section 244A(1) and 244A(1A) of the Act] to the tax liability of the Appellant

35. That the AO/DRP erred in initiating the penalty proceedings under section 271(1)(c) of the Act."

3. The solitary issue to be adjudicated in this appeal pertains to transfer pricing adjustment on account of AMP expenses.

4. At the outset, it was brought to our notice that the issue before us has been squarely covered in the assessee's own case for the assessment years 2006-07 to 2013-14 in ITAT No. 1334 /Chd/2010,1203/Chdi/2010,2511/Del/2013,1044/Del/2014 and 4516/Del/2016, for the assessment year 2014-15 in ITA No. 7933/Del/2018 and for the assessment year 2015-16 in ITA No. 9003/Del/2020.

5. From the record, we find that the ld. DRP has categorically stated that they were in know of the orders of the Tribunal for the earlier years but directed the AO to adhere to the addition made by the TPO as the department is contesting the decision of the Tribunal and the issue has not reached a finality. For the sake of ready reference, the relevant part of the order of the ld. DRP is reproduced as under:

> *3.2 Ground Nos. 2 to 2.21 relate to the adjustment on account of AMP expenses.*
>
> *3.2.1 The assessee, a subsidiary of PepsiCo Inc. USA, was engaged inter-alia in manufacturing soft drink/ juice based concentrates for aerated/ non-aerated drinks for is deemed associated enterprises ("AOs") in Bangladesh, Nepal, Bhutan and Sri Lanka, besides local sales thereof to its franchisee bottlers in India. For the purpose of carrying the above-mentioned activity in designated areas, it obtained a license for the technology to manufacture concentrates, use and exploitation of brands of AEs and use of trademarks in India. During the year under consideration, i.e., AY 2016-17, the assessee incurred AMP Expenses to the*

tune of INR 920,27,38,000/-. The Transfer pricing Officer vide an order dated 31.10.2019, held that since incurring of the said AMP expenses by the assessee had also benefitted the AEs thereby promoting their brands and trademark, the assessee had essentially incurred cost in connection with the services it provided to the AEs under a mutual arrangement, which although not reduced into writing, was ascertainable from the conduct of the assessee itself. Accordingly, the TPO stated that incurrence of AMP expenses qualified as an 'international transaction' under the terms of section 92B(1) read with section 92F(v) of the Income-tax Act, 1961 ("ITAT"). Pursuant thereto, the TPO computed adjustment to the tune of INR 571,69,91,000/- on account of AMP Expenses. It is submitted that the Hon'ble Income Tax Appellate Tribunal, New Delhi has, in the assessee's own case for AY 2006-07 to AY 2015-16, decided the issue of adjustment on account of AMP expenses in favour of the assessee. While doing so, the Hon'ble Tribunal has categorically held that AMP Expenses do not qualify as an 'international transaction' for the purposes of section 92B of the ITAT.

3.2.2 The Panel has considered the submission. The TPO and the AO are directed to verify from the record and if the aforesaid orders of the ITAT are not contested by the department before the High Court or the Supreme Court, the adjustment on account of AMP expenses would stand deleted. If these orders are contested before the High Court or the Supreme Court, as the case may be, the TPO/AO would retain this adjustment."

6. We have gone through the orders of the various Co-ordinate Benches of the Tribunal pertaining to the assessee for the earlier years. For the sake of ready reference, the relevant portion in ITA No.9003/Del/2019 for the assessment year 2015-16 is reproduced as under:

"8. On a reading of the order dated 19/11/2018 in ITA No. 1834/Chand/2010 and batch for the assessment years 2006-07 to 2013- 14 reported in (2018) 100 taxman.com 159 (Delhi) we find that the issue of AMP is dealt with by the Tribunal in extenso and a conclusion was reached to the effect that the AMP adjustment made by the Ld. TPO/learned Assessing Officer could be sustained.

9. We deem it just and necessary to refer to the observations of the Tribunal, which read as follows:-

58. Thus, form the plain reading of the aforesaid principles laid down by the Hon'ble Jurisdictional High Court, the key sequitur is that:

(i) International transaction cannot be identified or held to be existing simply because excess AMP expenditure has been incurred by the Indian entity.

(ii) International transactions cannot be found to exist after applying the BLT to decipher and compute value of international transaction.

(iii) There is no provision either in the Act or in the Rules to justify the application of BLT for computing the Arm's Length Price and there is nothing in the Act which indicate how in the absence of BLT one can 5 discern the existence of an international transaction as far as AMP expenditure is concerned.

(iv) Revenue cannot resort to a quantify the adjustment by determining the AMP expenses spent by the assessee after applying BLT to hold it to be excessive and thereby evidencing the existence of the international transaction involving the AE.

… … …
… … …

60. Another point which has been raised by the Revenue is that, huge spending of AMP expenses amounts to brand building and trade mark of the AE, and therefore, such a spending gives a benefit to the AE by enhancing its brand value which helps the AE in achieving sales in other territories or otherwise. This concept of brand building and whether such a brand building can be attributed to advertisement and sale promotions and thereby benefitting the AE, has been discussed in detail by the Hon'ble High Court in the case of Sony Ericsson Mobile Communication (supra) which for the sake of ready reference is reproduced hereunder:—

"Brand and brand building

102. We begin our discussion with reference to elucidation on the concept of brand and brand building in the minority decision in the case of L. G. Electronics India Pvt. Ltd. (supra). The term "brand", it holds, refers to name, term, design, symbol or any other feature that identifies one seller's goods or services as distinct from those of others. The word "brand" is derived from the word "brand" of Old Norse language and represented an identification mark on the products by burning a part. Brand has been described as a duster of functional and emotional 103 It is a matter of perception and reputation as it reflects customers' experience and faith. Brand value is not generated overnight but is created ever a period of time, when there is recognition that the logo or the name guarantees a consistent level of quality and expertise. Leslie de Chematony and McDonald have described "a successful brand is an identifiable

product, service, person or place, augmented in such a way that the buyer or user perceives relevant, unique, sustainable added values which match their needs most closely". The words of the Supreme Court in Civil Appeal No. 1201 of 1966 decided on February 12, 1970, in Khushal Khenger Shah v. KhorshedbannDabidaBoatwala, to describe "goodwill", can be adopted to describe a brand as an intangible asset being the whole advantage of the reputation and connections formed with the 6 customer together with circumstances which make the connection durable. The definition given by Lord MacNaghten in Commissioner of Inland Revenue v. Midler and Co. Margarine Ltd. [1901] AC 217 (223) can also be applied with marginal changes to understand the concept of brand. In the context of "goodwill" it was observed:

"It is very difficult, as it seems to me, to say that goodwill is not property. Goodwill is bought and sold every day. It may be acquired. I think, in any of the different ways in which property is usually acquired. When a man has got it he may keep it as his own. He may vindicate his exclusive right to it if necessary by process of law. He may dispose of it if he will—of course, under the conditions attaching to property of that nature ... What is goodwill? It is a thing very easy to describe very difficult to define. It is the benefit and advantage of the good name, reputation, and: connection of a business. It is the attractive force which brings in custom. It is the one thing which distinguishes an old established business from a new business at its first start. The goodwill of a business must emanate from a particular centre or source. However, widely extended or diffused its influence may be, goodwill is worth nothing unless it has power of attraction sufficient to bring customers

home to the source from which it emanates. Goodwill is composed of a variety of elements. It differs in its composition in different trades and in different businesses in the same trade. One element may preponderate here and another element there. To analyse goodwill and split it up into its component parts, to pare it down as the Commissioners desire to do until nothing is left but a dry residuum ingrained in the actual place where the business is carried on while everything else is in the all, seems to me to be as useful for practical purposes as it would be to resolve the human body into the various substances of which it is said to be composed. The goodwill of a business is one whole, and in a case like this it must be dealt with as such. For my part, I think that if there is one attribute common to all cases of goodwill it is the attribute of locality. For goodwill has no independent existence. It cannot subsist by itself. It must be attached to a business. Destroy the business, and the goodwill perishes with it, though elements remain which may perhaps be gathered up and be revived again ..."

104 "Brand" has reference to a name, trade mark or trade name. A brand like "goodwill", therefore, is a value of attraction to customers arising from name and a reputation for skill, integrity, efficient business management or efficient service. Brand creation and value, therefore, depends upon a great number of facts relevant for a particular business. It reflects the reputation which the proprietor of 7 the brand has gathered over a passage or period of time in the form of widespread popularity and universal approval and acceptance in the eyes of the customer. To use words from CTT v. Chunilal Prabhudas and Co.

[1970] 76 ITR 566 (Cal); AIR 1971 Cal 70, it would mean :

"It has been horticulturally and botanically viewed as 'a seed sprouting' or an 'acorn growing into the mighty oak of goodwill'. It has been geographically described by locality. It has been historically explained as growing and crystallizing traditions in the business. It has been described in terms of a magnet as the 'attracting force'. In terms of comparative dynamics, goodwill has been described as the 'differential return of profit'. Philosophically it has been held to be intangible. Though immaterial, it is materially valued. Physically and psychologically, it is a 'habit and sociologically it is a 'custom'. Biologically, it has been described by Lord Macnaghten inTrego v. Hunt [1896] AC 7 as the 'sap and life' of the business."

There is a line of demarcation between development and exploitation. Development of a trade mark or goodwill takes place over a passage of time and is a slow ongoing process. In cases of well recognised or known trademarks, the said trade mark is already recognised. Expenditures incurred for promoting product(s) with a trade mark is for exploitation of the trade mark rather than development of its value. A trade mark is a market place device by which the consumers identify the goods arid services and their source. In the context of trade mark, the said mark symbolises the goodwill or the likelihood that the consumers will make future purchases of the same goods or services. Value of the brand also would depend upon and is attributable to intangibles other than trade mark. It refers to infra-structure, know-how, ability to compete with the established market leaders. Brand value, therefore, does not

represent trade mark as a standalone asset and is difficult and complex to determine and segregate its value. Brand value depends upon the nature and quality of goods and services sold or dealt with'. Quality control being the most important element, which can mar or enhance the value.

Therefore, to assert and profess that brand building as equivalent or substantial attribute of advertisement and' sale promotion would be largely incorrect. It represents a coordinated synergetic impact created by assort-merit largely representing reputation and quality. There are a good number of examples where brands have been built without incurring substantial advertisement or promotion expenses and also cases where in spite of extensive and large scale advertisements, brand values have not been created. Therefore, it would be erroneous and fallacious to treat brand building as counterpart or to commensurate brand with advertisement expenses. Brand building or creation is a vexed and complexed issue, surely not just related to advertisement. Advertisements may be the quickest and effective way to tell a brand story to a large audience but just that is not enough to create or build a brand. Market value of a brand would depend upon how many customers you have, which has reference to brand goodwill, compared to a baseline of an unknown brand. It is in this manner that the value of the brand or brand equity is calculated. Such calculations would be relevant when there is an attempt to sell or transfer the brand name. Reputed brands do not go in for advertisement with the intention to increase the brand value but to increase the sales and thereby earn larger and greater profits. It is not the case of the Revenue that the foreign associated enterprises are in the business of sale/transfer of brands.

Accounting Standard 26 exemplifies distinction between expenditure HJ7 incurred to develop or acquire an intangible asset and internally generated goodwill. An intangible asset should be recognised as an asset, if and only if, it is probable that future economic benefits attributable to the said asset will flow to the enterprise and the cost of the asset can be measured reliably. The estimate would represent the set off of economic conditions that will exist over the useful life of the intangible asset. At the initial stage, intangible asset should be measured at cost. The above proposition would not apply to internally generated goodwill or brand. Paragraph 35 specifically elucidates that internally generated goodwill should not be recognised as an asset. In some cases expenditure is incurred to generate future economic benefits but it may not insult in creation of an intangible asset in the form of goodwill or brand, which meets the recognition criteria under AS26. Internally generated goodwill or brand is not treated as an asset in AS-26 because it is not an identifiable resource controlled by an enterprise, which can be reliably measured at cost. Its value can change due to a range of factors. Such uncertain and unpredictable differences, which would occur in future, are indeterminate. In subsequent paragraphs, AS-26 records that expenditure on materials and services used or consumed, salary, wages and employment related costs, overheads, etc., contribute in generating internal intangible asset. Thus, it is possible to compute good- will or brand equity/value at a point of time but its future valuation would be perilous and an iffy exercise.

In paragraph 44 of AS-26, it is stated that intangible asset arising from development will be

recognised only and only if amongst several factors, can demonstrate a technical feasibility of completing the intangible asset: that it will be available for use or sale and the intention is to complete the intangible asset for use or sale is shown or how the intangible asset generate probable future benefits, etc. The aforesaid position finds recognition and was accepted in CIT v. B. C. Srinivasa Setty [1981] 128 ITR 294 (SC), a relating transfer to goodwill. Goodwill, it was held, was a capital asset and denotes benefits arising from connection and reputation. A variety of elements go into its making and the composition varies in different trades, different businesses in the same trade, as one element may pre-dominate one business, another element may dominate in another business. It remains substantial in form and nebulous in character. In progressing business, brand value or goodwill will show progressive increase but in falling business, it may vain. Thus, its value fluctuates from one moment to another, depending upon reputation and everything else relating to business, personality, business rectitude of the owners, impact of contemporary market reputation, etc. Importantly, there can be no account in value of the factors producing it and it is impossible to predicate the moment of its birth for it comes silently into the world unheralded and unproclaimed. Its benefit and impact need not be visibly felt for some time. Imperceptible at birth, it exits unwrapped in a concept, growing or fluctuating with numerous imponderables pouring into and affecting the business. Thus, the date of acquisition or the date on which it comes into existence is not possible to determine and it is impossible to say what was the cost of acquisition. The aforesaid observations are relevant and are equally applicable to the present controversy. It

has been repeatedly held by the Delhi High Court that advertisement 110 expenditure generally is not and should not be treated as capital expenditure incurred or made for creating an intangible capital asset. Appropriate in this regard would be to reproduce the observations in CTT v. Monto Motors Ltd. [2012] 206 Taxman 43 (Delhi), which read:

"4. . . . Advertisement expenses when incurred to increase sales of products are usually treated as a revenue expenditure, since the memory of purchasers or customers is short. Advertisement are issued from time to time and the expenditure is incurred periodically, so that the customers remain attracted and do not forget the product and its qualities. The advertisements published/displayed may not be of relevance or significance after 10 lapse of time in a highly competitive market, wherein the products of different companies compete and are available in abundance. Advertisements and sales promotion are conducted to increase sale and their impact is limited and felt for a short duration. No permanent character or advantage is achieved and is palpable, unless special or specific factors are brought on record. Expenses for advertising consumer products generally are a part of the process of profit earning and not in the nature of capital outlay. The expenses in the present case were not incurred once and for all, but were a periodical expenses which had to be incurred continuously in view of the nature of the business. It was an on-going expense. Given the factual matrix, it is difficult to hold that the expenses were incurred for setting the profit earning machinery in motion or not for earning profits."

(Also see, CIT v. Spice Distribution Ltd., I. T. A. No. 597 of 2014, decided by the Delhi High Court on September 19, 2014 [2015] 374 ITR 30 (Delhi) and CTT v. Salora International Ltd. [2009] 308 ITR 199 (Delhi).

Accepting the parameters of the "bright line test" and if the said para meters and tests are applied to Indian companies with reputed brands and substantial AMP expenses would lead to difficulty and unforeseen tax implications and complications. Tata, Hero, Mahindra, TVS, Baja], Godrej, Videocon group and several others are both manufacturers and owners of intangible property in the form of brand names. They incur substantial AMP expenditure. If we apply the "bright line test" with reference to indicators mentioned in paragraph 17.4 as well as the ratio expounded by the majority judgment in L. G. Electronics India Pvt. Ltd.'s case (supra) in paragraph 17.6 to bifurcate and segregate the AMP expenses towards brand building and creation, the results would be startling and unacceptable. The same is the situation in case we apply the parameters and the "bright line test" in terms of paragraph 17.4 or as per the contention of the Revenue, i.e., AMP expenses incurred by a distributor who does not have any right in the intangible brand value and the product being marketed by him. This would be unrealistic and impracticable, if not delusive and misleading (aforesaid reputed Indian companies, it is patent, are not to be treated as comparables with the assessee, i.e., the tested parties in these appeals, for the latter are not the legal owners of the brand name/trade mark).

112. Branded products and brand image is a result of consumerism and a commercial reality, as

branded products "own" and have a reputation of intrinsic believability and acceptance which results in 11 higher price and margins. Trans-border brand reputation is recognised judicially and in the commercial world. Well known and renowned brands had extensive goodwill and image, even before they became freely and readily available in India through the subsidiary associated enterprises, who are assessees before us. It cannot be denied that the reputed and established brands had value and goodwill. But a new brand/trade mark/trade-name would be relatively unknown. We have referred to the said position not to make a comparison between different brands but to highlight that these are relevant factors and could affect the function undertaken which must be duly taken into consideration in selection of the comparables or when making subjective adjustment and, thus, for computing the arm's length price. The aforesaid discussion substantially negates and rejects the Revenue's case. But there are aspects and contentions in favour of the Revenue which requires elucidation."

60.1 Thus, the Hon'ble High Court after describing the concept of the "brand" had made a clear cut demarcation between development and exploitation of brand which is either in the form of trademark or goodwill which takes place over a passage of time by which its value depends upon and is attributable to intangibles other than trademark like, infrastructure, knowhow, ability to compete in the established market, lease, etc. Brand value does not represent trademark as asset and it is quite difficult to determine and segregate its value. Brand value largely depends upon the nature of goods and services sold, after sales services, robust distributorship, quality control, customer satisfaction

and catena of other factors. The advertisement is more telling about the brand story, penetrating the mind of the customers and constantly reminding about the brand, but it is not enough to create brand, because market value of a brand would depend upon how many customers you have, which has reference to a brand goodwill. There are instances where reputed brand does not go for advertisement with the intention to increase the brand value but to only increase the sale and thereby earning greater profits. It is also not the case here that foreign AE is in the business of sale/transfer of brands. Their Lordships have also referred to Accounting Standard 26 which provides for computation of goodwill and brand equal value at a point of time but not its future valuation or how such an intangible asset will generate probable future benefit. Because, the value fluctuates from one moment to other depending upon reputation and other factors. Reputation of a brand only enhances the sale and profitability and here in this case is only benefitting the assessee company when marketing its products using the trade mark and the brand of AE. Even otherwise also, the value of the brand which has been created in India by the assessee company will only be relevant when at some point of time the foreign AE decides to sell the brand, then perhaps that would be the time when brand value will have some significance and relevance. But to make any transfer pricing adjustment simply on the ground that assessee has spent advertisement, marketing expenditure which is benefitting the brand/trademark of the AE would not be correct approach. Thus, this line of reasoning given by the TPO is rejected.

61. Further in the final report of Action 8-10 of Base Erosion and Profit Shifting Project (BEPS) of OECD titled as "Aligning Transfer Pricing Outcomes with Value Creation'. It has been suggested that no

adjustment is required on AMP expenditure incurred by full-fledged manufacturers. The report contains various examples pertaining to manufacturer. The following passage from the report is quite relevant which for the sake of ready reference is quoted herein below:

> *"6.40 The legal owner will be considered to be the owner of the intangible for transfer pricing purposes. If no legal owner of the intangible is identified under applicable law or governing contracts, then the member of the MNE group that, based on the facts and circumstances, controls decisions concerning the exploitation of the intangible and has the practical capacity to restrict others from using the intangible will be considered the legal owner of the intangible for transfer pricing purposes.*
>
> *6.41 In identifying the legal owner of intangibles, an intangible and any licence relating to that intangible are considered to be different intangibles for transfer pricing purposes, each having a different owner. See paragraph 6.26. For example, Company A, the legal owner of a trademark, may provide an exclusive licence to Company B to manufacture, market, and sell goods using the trademark. One intangible, the trademark, is legally owned by Company A. Another intangible, the licence to use the trademark in connection with manufacturing, marketing and distribution of trademarked products, is legally owned by Company B. Depending on the facts and circumstances, marketing activities undertaken by Company B pursuant to its licence may potentially affect the value of the underlying intangible legally owned by*

Company A, the value of Company B's licence, or both.

6.42 While determining legal ownership and contractual arrangements is an important first step in the analysis, these determinations are separate and distinct from the question of remuneration under the arm's length principle. For transfer pricing purposes, legal ownership of intangibles, by itself, does not confer any right ultimately to retain returns derived by the MNE group from exploiting the intangible, even though such returns may initially accrue to the legal owner as a result of its legal or contractual right to exploit the intangible. The return ultimately retained by or attributed to the legal owner depends upon the functions it performs, the assets it uses, and the risks it assumes, and upon the contributions made by other MNE group members through their functions performed, assets used, and risks assumed. For example, in the case of an internally developed intangible, if the legal owner performs no relevant functions, uses no relevant assets, and assumes no relevant risks, but acts solely as a title holding entity, the legal owner will not ultimately be entitled to any portion of the return derived by the MNE group from the exploitation of the intangible other than arm's length compensation, if any, for holding title."

From the above quoted passage, it can be seen that the guidelines clearly envisage that legal ownership of intangibles, by itself, does not confer any right ultimately to retain returns derived by MNE group from exploiting the intangibles, even though such returns is initially accruing to the legal owner as a result of its legal/contractual right to exploit the intangible. The return depends upon the functions

performed by the legal owner, assets it uses, and the risks assumed; and if the legal owner does not perform any relevant function, uses no relevant assets, and assumes no relevant risks, but acts solely as a title holding entity, then the legal owner of the intangible will not be entitled to any portion of the return derived by the MNE group from the exploitation of the intangible other than the Arm's Length compensation if any for holding the title. Here also the PepsiCo Inc which is legal owner of the trademark license to the assessee has not performed any relevant function or used any assets or assumed any risk albeit has acted only as a title holder. It is not even entitled to any return for holding such title and in such circumstances, there seems to be no reason as to why it should compensate its subsidiary in India for the marketing activities while operating in India as a full-fledged manufacturer who alone is reaping the profit from the operation in India. It has been clearly demonstrated by the assessee that the risk with respect to its manufacturing operation in India was undertaken wholly by the assessee and not by the US parent AE. This is even evident from the various clauses of the agreement also.

62. Before us, learned CIT-DR submitted that the stand of the Revenue is that, the expenditure incurred by the Indian subsidiary of an MNE group on market function amounts to incurring of such expenses for and on behalf of the parent company outside India because;

- *Firstly, such kind of expenses promote the brand/trademarks that are legally owned by the foreign parent AE;*

- *Secondly, these expenditures create or develop marketing intangibles in the form of brands,*

trademarks, customer list dealer/distribution channels, etc. even though Indian company may not be the owner or have any right in these intangibles, but development of such intangibles deserves compensation for computing the value of compensation and the required adjustment. A comparison of the average of AMP spent by the comparables in a similar line of business has to be made to determine the routine amount spent on AMP for the product sale and any such expenditure over and above is purely for developing the brand value or other marketing intangibles for the benefit of the AE; and it is in the form of the service to the AE which requires adjustment along with the markup of the service charge on the same work out on the cost plus basis.

♦ *Lastly, the functions relating to DEMPE (Development, Enhancement, Maintenance, Protection and Exploitation) results into many direct and indirect benefits, which are by way of increase revenue from the territory on account of sale/royalty/FTS etc. and in some cases it may make revenue enhancement in the other parts of the world. The direct benefit is by way of obtaining an advantage in the terms of the development of market for themselves and also leads to enhancement of the exit value.*

63. Before examining as to whether any transfer pricing adjustment on AMP is required or not for the reason stated above, the first and foremost condition is that, existence of an international transaction in relation to any service of benefit has to be established before the transfer pricing provision can be triggered so as to place value on service of benefit for the purpose of determining the compensation. Mere fact of excessive AMP expenditure cannot establish the existence of such a transaction. It is

only when such a transaction is established then perhaps it may be possible to bench mark it separately. Under the Indian Transfer Pricing provisions, it has been well established over the period of time that detailed FAR analysis has to be carried out to identify all the functions of resident tax payer company and the non-resident AEs pertaining to all the international transactions like purchase of raw material, payment of royalty, purchase of finished goods, export of finished goods, support services or whether there is any direct sales by AE in India. Further it needs to be seen, whether marketing activities relating to DEMPE functions reflected in any such expenditure incurred by the resident tax payer company and the non-resident AE in India are in conformity with the functions and risk profiles and the benefit derived by the tax payer company and the AE. It is also very relevant to examine, whether the AE is assuming any kind of risk in the Indian market or is benefitting from India in one way or the other. Thus, FAR analysis is the key which needs to be seen what kind of functions is being carried out by the AE in India, the nature of assets which have been deployed and the risk which have been assumed. If there is no risk of such attributes which is being carried out by the non-resident AE in India then there is no question of AE compensating to its subsidiary in India for any marketing expenses. Here, we have already stated at several places that parent AE of the assessee-company has not carried out any function in India and had not assumed any risk in India and even for the license for use of trademark, no royalty has been paid. Hence, no benefit whatsoever has accrued to the parent AE. Accordingly, we are of the opinion that under these facts and circumstances of the case it is very difficult to attribute any kind of Arm's Length compensation which is supposed to be made by the AE to the assessee company.

64. Thus, in view of discussion made above, we hold that, firstly, there is no international transaction in the form of any agreement or arrangement on AMP expenditure incurred by the assessee company; and secondly, under FAR analysis also, no such benefit from the AMP expenditure having any kind of bearing on the profits, income, losses or assets as accrued to the AE or any kind of benefit has arisen to the AE.

65. As stated above, from the Assessment Years 2006-07 to Assessment Year 2008-09, the TPO has applied BLT not only for identifying the international transaction but also for making the adjustment. From the Assessment Years 2010-11 to 2012-13 TPO has changed his stand and adjustment has been made by applying 'Profit Split Method'. As per Rule 10B(1)(d) PSM has to be applied, vis-à-vis the international transaction involving unique intangibles in the following manner: —

"(i) the combined net profit of the associated enterprises ("AEs") arising from the international transaction in which they are engaged is to be determined first;

(ii) the relative contribution made by each of the AEs to the earning of such combined net profit is to be evaluated thereafter on the basis of functions performed, assets employed and risks assumed by each enterprise (FAR) and on the basis of reliable external market data visà-vis independent parties;

(iii) the combined net profit is to be then split amongst the AEs in proportion to their relative contributions;

(iv) the profit thus apportioned to the assessee is to be taken into account 16 to arrive at an arm's length price (ALP) in relation to the international transaction.

(v) Alternatively, the combined net profit may be initially partially allocated to each enterprise so as to provide it with a basic return appropriate for the type of international transaction, in which it was engaged, with reference to market returns achieved for similar types of transactions by independent enterprises, and thereafter, the residual profit remaining after such allocation may be split amongst the enterprises in proportion to their relative contribution as per (ii) and (iii) above, and in such a case the aggregate of the net profit allocated to the enterprise in the first instance together with the residual net profit apportioned to that enterprise is to be taken to be the net profit arising to that enterprise from the international transaction."

The OECD Transfer Pricing Guidelines, 2010 provides that PSM first requires the identification of the profits which is to be split among the AEs, from the controlled transactions in which the AEs were engaged (the combined profit). Thereafter, the combined profit between the AEs is required to be split on an economically valid basis that approximates the division of profits that would have been anticipated and reflected in an agreement made at arm's length. The combined profit to be split should only be those arising from the controlled transaction. In determining those profits, it is essential to first identify the relevant transaction to be covered under PSM. Where a taxpayer has controlled transactions with more than one AE, it is also necessary to identify the parties in relation to that transaction. Comparable data is relevant in the profit split analysis to support

the division of profits that would have been achieved between independent parties in comparable circumstances. However, where comparable data is not available, the allocation of profits may be based on division of functions (taking account of the assets used and risks assumed) between the AEs. Further, the TP Guidelines also suggest two approaches in the effective application of PSM, which are: —

> *(i) Contribution analysis: Under the contribution analysis, the combined profits, which are the total profits from the controlled transactions under examination, would be divided between the associated enterprises based upon a reasonable approximation of the division of profits that independent enterprises would have expected to realize from engaging in comparable transactions.*
>
> *(ii) Residual analysis: Under the residual analysis, the combined profits 17 from the controlled transactions under examination is done in two stages; in the first stage, each participant is allocated an arm's length remuneration for its non-unique contributions in relation to the controlled transactions in which it is engaged; and in the second stage, any residual profit (or loss) remaining after the first stage division would be allocated among the parties based on an analysis of the facts and circumstances.*

As per the aforesaid guidelines which has also been referred by the TPO in his order and the relevant rules, we are of the opinion that, first of all, TPO is required to determine the combined profit arisen from international transaction of incurring AMP expenses and then he is required to split the combined profit in proportionate to the relative contribution of the assessee and the AE. Here, the TPO has neither

applied PSM correctly nor has he analysed the contribution made by both entities on the relative value of FAR of each of the entity. He has also not provided any reliable external data based on which the relative contribution of the entities involved in the transaction could have been evaluated either. He has applied PSM by taking the finance of the US part AE and has determined the rate of 35% allocable towards marketing activities by relying upon judgment of the Tribunal in Roll Royce PLC vs. DDIT (supra) and has applied the same to the global net profit of the US parent AE to arrive at the global profit of US parent AE from marketing activities. Thereafter, he has compared the AMP spent by the AE with that of the assessee company and multiplied that ratio with the global net profit of the US parent AE arising from marketing activities to compute the Transfer Pricing Adjustment on account of AMP expenses. Such an approach of the learned TPO at the threshold is wholly erroneous, because PSM is applicable mainly in international transaction involving transfer of unique intangibles or in multiple international transactions which are interrelated and interconnected that they cannot be evaluated separately for the purpose of determining the Arm's Length Price of any one transaction. Here in this case this is not in dispute that no transfer of any unique intangibles has been made accept for license to use trademark which too was royalty free. According to the Rule, under the PSM, combined net profit of the AEs arising from the international transaction has to be determined and thereafter, if incurrence of AMP expenses is to be considered from the value of such international transaction then the combined profit has to be determined from the value of such international transaction. No FAR analysis of AE has been carried out or even demonstrated that any kind of profit has been derived by the AE from the AMP expenses

incurred in India. Otherwise also, the profit earned on account of AMP expenses 18 incurred by the assessee by way of economic exploitation of the trademark/brand in India already stands captured in the profit and loss account for the assessee company and the same has duly offered to tax and hence there was no logic to compute or make any Transfer Pricing Adjustment on this score.

66. The TPO has followed the same reasoning in the Assessment Year 2013-14 also, but the DRP did not find any substance in the TPO's approach and directed the application of 'Other Method' as prescribed under Rules as against the application of PSM. By applying 'Other Method', adjustment had been made by comparing the AMP/sales ratio of the US parent AE with that of the assessee company and thereafter the DRP has considered the excessive AMP spent by the assessee company as a Transfer Pricing Adjustment. The only difference between the earlier approach of the TPO and the approach adopted by the DRP is that, earlier TPO compared the AMP/sales of the party, i.e., the assessee with that of the third party and now the DRP compares the AMP/sales of the assessee company with that of the parent AE. In our opinion, even the 'Other Method' has been incorrectly implied for the sake of ready reference Rule 10AB reads as under: —

> *"Other method of determination of arm's length price.*
>
> *10AB. For the purposes of clause (f) of sub-section (1) of section 92C, the other method for determination of the arm's length price in relation to an international transaction [or a specified domestic transaction] shall be any method which takes into account the price which has been*

charged or paid, or would have been charged or paid, for the same or similar uncontrolled transaction, with or between non-associated enterprises, under similar circumstances, considering all the relevant facts."

The aforesaid Rule provides that that "Other Method" shall be any method which takes into account the price which had been charged or paid for the same or similar uncontrolled transaction with or between non-associated enterprises under similar circumstances. Comparison of the AMP over sales ratio of the assessee with the AMP ratio of Pepsi Co Group on a worldwide basis was nothing but a distorted version of the BLT.

10. For the year 2014-15 also, on the same reasoning and following the view taken by the Tribunal for the assessment years 2006-07 to 2013- 14 the issue was held in favour of the assessee."

7. Since, the matter stands covered in favour of the assessee and in the absence of any material change in the facts of the case brought to our notice, we hereby direct that the addition be deleted.

8. Since, the addition made by the revenue authorities is directed to be deleted, the Stay Application No.22/Del/2021 filed by the assesse is dismissed as infructuous.

9. As a result, the appeal of the assessee is allowed and the Stay Application of the assessee is dismissed.

Order Pronounced in the Open Court on 04/05/2021.

Sd/-	Sd/-
(Amit Shukla)	**(Dr. B. R. R. Kumar)**
Judicial Member	**Accountant Member**

Dated: 04/05/2021

Subodh

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

ASSISTANT REGISTRAR