

**IN THE INCOME TAX APPELLATE TRIBUNAL,
DELHI BENCH: 'I-1' NEW DELHI**

**BEFORE SHRI AMIT SHUKLA, JUDICIAL MEMBER
AND
SHRI O.P. KANT, ACCOUNTANT MEMBER
[Through Video Conferencing]**

ITA Nos. 2682 & 2683/Del/2013
Assessment Years: 2008-09 & 2009-10

M/s. Shyam Telecom Ltd., A-60, Naraina Industrial Area-1, New Delhi	Vs.	ACIT, Central Circle-2, New Delhi
PAN :AAACS0297E		
(Appellant)		(Respondent)

Appellant by	Sh. Ajay Vohra, Sr. Adv. Sh. Abhishek Aggarwal, Adv.
Respondent by	Sh. Bhagwati Charan, CIT(DR)

Date of hearing	08.10.2021
Date of pronouncement	08.10.2021

ORDER

PER O.P. KANT, AM:

These two appeals by the assessee are directed against a common order dated 25/02/2013, passed by the Learned Commissioner of Income-tax(Appeals)-XX, New Delhi [in short 'the Ld. CIT(A)'] for assessment year 2008-09 and 2009-10 respectively. Since common issue in dispute is involved in both these appeals, same were heard together and disposed off by way of this consolidated order for convenience and avoid repetition of facts.

2. The grounds raised by the assessee in assessment year 2008-09 are reproduced as under:

1. *The Ld. CIT(A) has grossly erred in confirming the interest rate of 13% as arm's length interest rate, computed by the Ld. Assessing Officer on the sum lent to the associated enterprise, being its US subsidiary.*
2. *The Ld. CIT(A) has grossly erred in not appreciating that no enhancement in the interest rate of 8% duly charged by the Appellant to the associate enterprise was warranted having regard to the prevailing Libor rate, Reserve Bank of India guidance and judicial precedents.*
3. *The Ld. CIT(A) has grossly erred in accepting an ad-hoc mark-up of 700 basis points over the Libor rate without any justification as to how the same was computed.*
4. *Without prejudice to the aforesaid grounds of appeal, the Ld. CIT(A) has erred in overlooking that, even if the interest rate is computed as per the parameters taken by the TPO in the Assessment Order for the AY 2007-08, the interest rate cannot exceed 11.7% and applying a 13% rate by the Ld. Assessing Officer on the pretext of rounding-up was unwarranted. The Appellant craves leave to add, alter, amend and / or modify any of the grounds of appeal.*

2.1 Similarly, the grounds raised by the assessee for assessment year 2009-10 are reproduced as under:

1. *The Ld. CIT(A) has grossly erred in confirming the interest rate of 7.52% as arm's length interest rate, computed by the Ld. Assessing Officer on the sum lent to the associated enterprise, being its US subsidiary.*
2. *The Ld. CIT(A) has grossly erred in not appreciating that no enhancement in the interest rate of 3% duly charged by the Appellant to the associate enterprise was warranted having regard to the prevailing Libor rate. Reserve Bank of India guidance and judicial precedents.*
3. *The Ld. CIT(A) has grossly erred in accepting an ad-hoc mark-up of 500 basis points over the Libor rate without any justification as to how the same was computed. The Appellant craves leave to add, alter, amend and / or modify any of the grounds of appeal on or before at any time of hearing. The Appellant prays for appropriate relief based on the above grounds of appeal and the facts and circumstances of the case.*

3. Briefly stated facts of the case are that the assessee is a telecom equipment manufacturer, supplying indoor and outdoor wireless enhancement solutions such as RF repeaters, optical distributed antenna solutions, IP cellular backhaul systems, etc.

3.1 The assessee established a subsidiary, namely, Shyam Telecom Inc (In short 'STI' or AE) in United States of America (USA) in the year 2005 which deals in telecom equipment manufactured by the assessee and promotes its brand globally.

3.2 STI, being a relatively new entity in the USA, it required working capital and for this purpose it relied on parent company i.e. the assessee. Accordingly, the assessee during financial year 2006-07 (assessment year 2007-08), advanced a loan of ₹ 14,95,77,721/- to 'STI'. During the assessment year 2008-09, the assessee charged interest rate at the rate of 8% and for assessment year 2009-10, the assessee charged interest rate of 3% on the loan, though no interest was charged in assessment year 2007-08 corresponding to financial year 2006-07.

3.3 In assessment year 2007-08 the Learned transfer pricing officer (TPO) determined the arm's-length rate of interest on the loan at 13% on the basis of following methodology:

<i>CUP rate is thus arrived at as under:</i>	
<i>Basic interest rate for the credit rating of the AE</i>	<i>LIBOR + 400 basis points</i>
<i>Add: Transaction Cost</i>	<i>300 basis points</i>
<i>CUP Rate</i>	<i>LIBOR + 700 basis points</i>
<i>Add: Adjustment for security</i>	<i>Not Computed</i>
<i>Final CUP Rate</i>	<i>LIBOR + 700 basis points</i>

3.4 Thus, in assessment year 2007-08 the learned TPO for determining arm's-length interest rate, increased the London

Inter Bank Offered Rates (LIBOR) rate of interest with 400 basis points on account of credit rating of AE and further 300 basis point on account of transaction cost.

3.5 In assessment year 2008-09, the Assessing Officer himself benchmarked the transaction of interest and determined the arm's-length price following the approach of the learned TPO in assessment year 2007-08. The Assessing Officer worked out arm's-length interest rate at six-month LIBOR i.e. 4.7% + 700 basis points i.e. 11.7% per annum, however finally rounded to 13% per annum and made an adjustment of ₹ 42,00,000/-.

3.6 In assessment year 2009-10, the Learned Assessing Officer worked out the arm's-length interest rate at six-month LIBOR i.e. 2.52 % + 500 basis points i.e. 7.52 % and made an adjustment of ₹ 80,56,000/-.

3.7 The Ld. CIT(A) upheld the benchmarking of interest at LIBOR + 700 points in assessment year 2008-09 holding that assessee is not a banker and in view of credit rating and transaction cost, the LIBOR needs to be marked up by 700 basis points. Similarly assessment year 2009-10, benchmarking of interest rate at LIBOR+ 500 basis point was upheld. The relevant finding of the Ld. CIT(A) is reproduced as under:

“7.4. This matter can be viewed from another angle as well. Assessee has borrowed funds from banks in India. The opportunity cost of lending money to its AE is using the same money for its own business in India (reducing the borrowing costs at home). On verification from the appellant during the course of the hearing, it is noticed that on an average, the assessee is paying interest at the rate of 14.75% to SBI on cash credits and at the rate of 12% to Syndicate Bank for term loans. It must be remembered that the credit rating of the assessee in India is not the same as the credit rating of its AE in foreign market. From this angle also, the interest

rates of LIBOR + 700 & LIBOR + 500 basis points for AY 2008-09 & 2009-10 respectively seems very reasonable.

It is also necessary to note that assessee itself has charged interest during these two years. Therefore, only relevant question is that at what rate interest should be charged? The question is not whether interest should be charged at all, as the appellant accepts that interest is chargeable.

As the CUP method results into a single rate of interest, no further reduction on account of proviso to Section 92C(2) on such rate is applicable. Perot Systems (supra) is relied in this regard. The calculation of 3 years LIBOR rate is not applicable since a single year data needs to be applied in this case as per the rules.

Credit Risk and credit rating is the basis to arrive at the LIBOR plus. It includes all risks including country risks, and such quantification leads to LIBOR + 700 and 500 basis points. Therefore, no further accounting of country risk is necessary.

In view of the above discussion, I hold that the AO was justified in charging interests on the sum lent to the AE in the orders for AY 2008-09 and 2009-10 There is no need to interfere in the orders of the AO. Therefore, these grounds of appeal for both years are rejected.”

4. Before us, the assessee is aggrieved with the basis point marked up by the Assessing Officer on LIBOR rate. The contention of the assessee is that, in case of transaction with AE no markup for credit rating and transaction cost should be applied. In support of the contention, the learned Consul of the assessee relied on the decision of the Hon’ble Delhi High Court in the case of CIT Vs Cotton Naturals (I) P ltd (ITA 233/2014) and decision of Hon’ble Bombay High Court in the case of CIT Vs Everest Kanto Cylinder Limited (ITA No. 435/2015).

5. On the other hand, the Learned Departmental Representative relied on the orders of the lower authorities.

6. We have heard rival submission of the parties on the issue in dispute and perused the relevant material on record. The only dispute between the parties, is regarding the markup of 700 basis point in assessment year 2008-09 and markup of 500 points in

assessment year 2009-10 over the LIBOR rate applied by the Assessing Officer for determination of arm's-length price of international transaction of interest. The Assessing Officer has followed finding of his predecessor in AY 2007-08, but in AY 2007-08, the assessee has opted for scheme under Vivad -Se-Vishvas Act, 2020 and withdrawn his appeal. In the year under consideration, the assessee is not disputing the LIBOR rate application for determining the arm's-length price of the transaction and only disputing markup of 400 points on the basis of credit rating of the AE and 300 points on the basis of transaction cost. The finding of the Hon'ble Delhi High Court in the case of Cotton Natural (I) Pvt. Ltd (supra), which is relied upon by the assessee, on the issue of markup for transaction cost is reproduced as under:

“31. On the question of adjustment, the TPO referred to the FCNR loan advanced by the Power Finance Corporation to the Indian company i.e. Jindal Thermal Power Company Ltd. of US\$ 44.50 million. Interest charged in the said case was US LIBOR plus 350 basis points for a company which had been given BB+ credit rating. However, full facts like the nature of transaction; risk factors etc. are not elucidated. He has also referred to the Bank of Baroda website that the rate of interest on FCNR loan were between 350-650 basis points over LIBOR for the FY 2006-07. TPO held that in view of the financial health of the subsidiary AE, interest rate could be taken as the average of six months LIBOR plus 400 basis points. On the question of transaction cost, it was stated that it was mandatory for the bank to insist that the borrower must book forward contracts to hedge their position. The TPO referred to the premium payable for undertaking the said hedging transactions and added a cost of 3% per annum as premium, which should have been paid. At the same time, the TPO acknowledged that the taxpayer was not in the business of lending or borrowing money and observed that the taxpayer's risk was higher in advancing loan to a single customer, vis a bank which spreads its risk among various customers. Banks spread their risk when loans are/were advanced to various

consumers, but this does not happen when a loan is given to a single customer.

32. On the question of adjustment made on account of the transaction cost, we do not appreciate the reasoning given by the TPO and find it difficult to accept. The transaction or hedging cost is borne and paid by the borrower. These are undertaken when they take loans in US Dollars or other foreign currencies because the borrower wants to cover any loss on account of the depreciation of the Indian Rupee vis- a- vis the foreign currency. The assessee in the present case is not the borrower, but the lender. Transaction cost is not, therefore, applicable in the case in question, as the loan had to be repaid in US Dollars. Markup towards the transaction cost is exorbitant and even comparison with banks is unsound and unintelligible. Risk factor adjustment is also stretched, for it ignores the close relationship between the two AEs and the funds were the shareholder funds, and not borrowed money.”

6.1 The finding of Hon’ble Bombay High Court in the case of Everst Kanto cylinder Limited (supra) is reproduced as under:

“.....In light of the above decisions, the rate to be used for undertaking an adjustment should be LIBOR and not the average yield rates considered by the learned TPO. The LIBOR rate for March 2008 was 2.6798%. However the assessee has charged 7% from its AE as per the internal CUP available. Thus, the assessee has charged interest to EKC Dubai and EKC china at the rate higher than existing LIBOR rates. Accordingly, the said transaction of providing loan to EKC Dubai and EKC China is at arm's length. Additions made by the AO are accordingly set aside. ”

6.2 The Hon’ble Delhi High Court in the case of Cotton Naturals I Pvt. Ltd. (supra) has thus held that transaction cost or hedging cost is to be born and paid by the borrower and not by the lender and thus no adjustment for markup of transaction cost, is required to be charged. In the case of Everest Kanto cylinder Limited (Supra) LIBOR rate has been held at arm’s length in the facts of that case, and said ratio cannot be applied over facts of the case before us.

6.3 In the instant case, the AE was a relatively new entity in the year under consideration and credit rating of the same being not good, the assessee has advanced loan to the AE, so if in comparable situation, a bank in India sanction a loan to any entity in USA in uncontrolled manner transaction, then credit rating of the loan recipient entity should be taken into account. The AO has followed earlier AY 2007-08 and has not taken into consideration credit rating of the AE in the year under consideration, which has to be based on specific information and not on the basis of assumption. Before the Ld. CIT(A), the assessee has cited the RBI Master Circular and submitted that interest rate on foreign currency working capital loan for a period in excess of 180 days should be as under:

<i>S. No.</i>	<i>Relevant Year</i>	<i>Interest Rate (per annum)</i>
1.	2006	LIBOR + 3% p.a.
2.	2008	LIBOR + 3% p.a.
3.	2009	LIBOR + 505% p.a.
	<i>Average</i>	<i>LIBOR + 3.83% p.a.</i>

6.4 In view of the above, we are of the opinion that no markup for transaction cost should be applied on LIBOR rate for benchmarking of the international transaction; however, appropriate markup for credit rating should be applied depending on credit rating of AE. The Assessing Officer in assessment year 2008-09 and 2009-10 has not given any justification for applying markup of 400 points for credit rating and, therefore, in the interest of justice, the issue in dispute is restored to the file of the Learned Assessing Officer for deciding limited issue of markup for credit rating over LIBOR rate of interest after taking into

consideration criteria for credit rating during relevant period. The grounds of the appeal of the assessee for both the assessment years are accordingly allowed for statistical purposes.

7. In the result, the appeals of the assessee for assessment year 2008-09 and 2009-10 are allowed for statistical purposes.

Order pronounced in the open court on 8th October, 2021

Sd/-
(AMIT SHUKLA)
JUDICIAL MEMBER

Sd/-
(O.P. KANT)
ACCOUNTANT MEMBER

Dated: 8th October, 2021.

RK/-(DTDC)

Copy forwarded to:

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

Asst. Registrar, ITAT, New Delhi