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

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

Ms. Astha Chandra, Judicial Member

ITA No. 4069/Del/2019 : Asstt. Year: 2009-10
ITA No. 4070/Del/2019 : Asstt. Year: 2010-11

Addl. CIT, Special Range-02, New Delhi-110002	Vs	Bacardi India Pvt. Ltd., S-405 (LGF), GK Part-II, New Delhi-110048
(APPELLANT)		**(RESPONDENT)**
PAN No. AAACB3944R		

ITA No. 4517/Del/2019 : Asstt. Year: 2009-10
ITA No. 4518/Del/2019 : Asstt. Year: 2010-11

Bacardi India Pvt. Ltd., 805-808, time Tower, M. G. Road, Gurgaon, Haryana-122002	Vs	Addl. CIT, Special Range-02, New Delhi-110002
(APPELLANT)		**(RESPONDENT)**
PAN No. AAACB3944R		

Assessee by : Sh. Nageswar Rao, Adv. &
Sh. S. Chakarborty, Adv.
Revenue by : Sh. Surender Pal, CIT DR

Date of Hearing: 28.02.2022		**Date of Pronouncement: 20.05.2022**

ORDER

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

The present appeals have been filed by the Revenue as well as the assessee against the orders of the ld. CIT(A)-42, New Delhi dated 28.02.2019.

2. Since, the issues involved in all these appeals are identical, they were heard together and being adjudicated by a common order.

3. In ITA No. 4069/Del/2019, following grounds have been raised by the Revenue:

> *"1. Whether on the facts and circumstances of the case, the ld. CIT(A) is legally justified in not treating AMP expenditure as International Transaction without appreciating the arguments of the TPO in para 3.1 to para 10 of order and when the Hon'ble ITAT has held AMP expenditure as an International Transaction in assessee's own case for A.Y. 2011-12 in ITA No. 1197/Del/2016 dated 27.03.2019.*
>
> *2. Whether on the facts and circumstances of the case, the ld. CIT(A) is justified in issuing direction to include the four comparables which were already rejected by the TPO by giving proper reasoning in his order."*

4. In ITA No. 4517/Del/2019, following grounds have been raised by the assessee:

> *"1.1 That, the Hon'ble Commissioner of Income Tax (Appeals) ["CIT(A)"] has grossly erred in directing to undertake a fresh benchmarking analysis for the transaction involving "export of finished goods" while adopting a perplexing approach of an intensity based comparability adjustment for alleged Advertising, Marketing and Promotion ("AMP") expenses.*
>
> *1.1.1 This despite clearly concluding that on the facts in the instant case, AMP expenditure is not an international transaction and that any adjustment in respect of such AMP expenditure is not justified.*
>
> *1.2 Without prejudice, on the facts and circumstances of the case and in law, the Hon'ble CIT(A) has grossly erred while directing to re-determine the arm's length price of the international transaction involving "export of finished goods" when no adverse inference in relation to the same was drawn by the Learned Transfer Pricing Officer ("TPO") during the course of assessment proceedings.*

1.3 Without prejudice, on the facts and circumstances of the case and in law, the Hon'ble CIT(A) has erred in rejecting the economic analysis carried on by the Appellant without providing any cogent reasons for doing so. The analysis was in accordance with the provisions of the Act read with the Rules, and the Hon'ble CIT(A) erred in directing to re-determine the arm's length price of the international transaction involving "export of finished goods".

1.4 Without prejudice, the Hon'ble CIT(A) has erred in not appreciating the fact that AMP expenses incurred by the Appellant are solely in relation to sales made by it in the domestic Indian market, whereas the Appellant does not incur a single penny of AMP expense in relation to goods (exported) sold to AEs.

1.5 Without prejudice, on the facts and circumstances of the case and in law, the Hon'ble CIT(A) has erred in selecting comparables which are inappropriate in relation to the final product segment of the Appellant.

1.6 Without prejudice, on the facts and circumstances of the case and in law, the Hon'ble CIT(A) has erred in misinterpreting the various decision of higher courts which clearly requires exclusion of all non-brand related expenses (i.e. point of sales expenses, which are in the nature of rebates and discounts, selling expenses, sales commission, etc.) for the purpose of computing AMP expenses.

1.7 Without prejudice, on the facts and circumstances of the case and in law, the Hon'ble CIT(A) has erred in applying an arbitrary mark-up to be determined, having regard to the average return earned by the entities engaged in providing marketing support services.

1.8 Without prejudice, the Hon'ble CIT(A) has erred by not appreciating the basic concepts, mechanism and

the methodology and guidance for applying the intensity based comparability adjustment and thereby not passing a speaking order.

1.9 That, the Hon'ble CIT(A) and the Learned Assessing Officer ("AO") / Learned TPO has erred in law and on facts while arbitrarily isolating outstanding trade receivables arising from the international transaction involving sale of goods to AEs and thus re-characterizing such outstanding receivables as a loan extended to AEs.

1.10 Without prejudice, the Hon'ble CIT(A) and the Learned AO / TPO has erred in not appreciating that any interest due on account of outstanding payments is already embedded in the sale price of goods/ services sold to AEs.

1.11 Without prejudice, the Hon'ble CIT(A) and the Learned AO / Learned TPO has erred on facts and in law while concluding that outstanding trade receivables constitute separate international transaction and proceeding to benchmark the same by incorrect application of Comparable Uncontrolled Price ("CUP") method using..the six months London Inter-bank Offered Rate ("LIBOR") plus 400 basis points.

1.12 Without prejudice, the Hon'ble CIT(A) and the Learned AO / TPO is not justified in ignoring that the trade practice of the Appellant of not charging / recovering interest on outstanding balances with AEs is also consistent with its practice of not charging / recovering interest on outstanding balance with unrelated / third parties.

1.13 Without prejudice, the Hon'ble CIT(A) is not justified in arbitrarily making a comparison of outstanding debtor days in relation to transactions undertaken by BIPL with its AEs vis-a-vis the transactions undertaken with third parties.

1.14 Without prejudice, the Hon'ble CIT(A) has erred in adopting an ad-hoc approach to benchmark the monthly balances of outstanding receivables after netting off outstanding balances payable by BIPL to

respective AE(s), while proposing an addition to income of the Appellant on account of imputed interest on outstanding receivables.
1.15 That, the Learned AO / TPO has erred in initiating penalty proceedings under Section 271(l)(c) and 271AA of the Act."

5. Bacardi India Private Limited, a 74:26 JV between Bacardi International Limited and Gemini Distilleries, is engaged in the business of manufacturing and sale of alcoholic beverages in the licensed territory. The Appellant predominantly operates as the 'exclusive' licensed manufacturer of alcoholic beverages (under the brand name / trade name BACARDI) earning around 90% (approx.) of its operating revenue from manufacturing activity. In addition, the Appellant also imports certain alcoholic beverages (which are in ready-to-sell condition) from its AEs in the miniscule quantity for resale it the local market.

6. For the Assessment Year 2009-10, the Appellant had filed its return of income on 30 September 2009 declaring a total loss of INR 19,40,16,060/-, resulting in a refund of INR 1,94,779/-. The return of Appellant was selected by the AO for scrutiny u/s 143 of the Act wherein the AO requested appellant to file certain information / explanation from time to time. Based the information furnished, the AO concluded the assessment proceedings by issuing the order under section 143(3) of the Act on 09 April 2013, thereby making an addition of INR 36,14,92,303/- to the income of the Appellant against which brought forward losses of INR 16,74,76,243/- was set off resulting in Nil income. The additions made were on account of the following:

Particulars		Amount (in INR)
	Total income/(loss) declared by the Appellant in return of income	(194,016,060)
Add:	Transfer Pricing adjustment 1. AMP Expenses Mark-up- Rs.36,12,24,752/- 2. Interest on Receivables– Rs.2,67,551/-	361,492,303
	Total	167,476,243
	Set off brought forward losses	167,476,243
	Total Assessed income/(loss) as per assessment order	**NIL**

7. The appellant has challenged the action of AO/TPO in

a) treating AMP as a separate international transaction,

b) using bright line test from benchmarking,

c) incurring expenditure on account of advertisement, marketing and promotion, under influence or control of the AE.

8. The international transactions as disclosed by the assessee in Form 3CEB were as follows:

S.No.	Type of transaction	Value (in INR)	Method used
1.	Export of finished goods to AEs	2,90,95,650	TNMM
2.	Import of liquor for resale	7,67,70,608	RPM
3.	Provision of marketing support services	71,78,495	TNMM
4.	Payment of interest on ECB	44,00,715	CUP
5.	Payment of interest on FCD	56,26,056	CUP
6.	Reimbursement of expenses by AEs	9,23,74,118	No benchmarking required
7.	Reimbursement of expenses by AEs	76,13,465	
8.	Interest free loan	-	

9. The TPO after noting the international transactions mentioned proceeded to benchmark the transaction of AMP expenses.

10. The TPO held that the AMP expenditure as separate international transaction mainly on the following grounds:

- Brands under which the Appellant manufactured and sold liquor were owned by the associated enterprises ("AEs") of the Appellant and on that basis held that the AMP expenditure of the Appellant had a direct bearing on the promotion of the brands of its AE.

- The TPO contended that the Appellant had incurred substantial expenditure on the promotion of the concerned brands owned by its AEs, which was not reimbursed by the AEs to the Appellant.

- The TPO based on the Transfer Pricing Study ("TP Study") also contended that, since the marketing and ultimate sale of products was spearheaded by the AE having 74% share in JV, it indicated that the marketing effort undertaken by the Appellant was at the behest and under the control of its AEs.

- The TPO, thereafter contended that such efforts created a marketing intangible in favour of the AE and in that sense was an "international transaction" that needed to be benchmarked.

- The TPO observed that the liquor companies resort to surrogate advertising by brand building through the launch

of mineral water & soda. Further, TPO added that some companies also launch cassettes and CDs while others offer coasters, bottle openers and whiskey glasses. Thus, TPO concluded that such advertising, which is not product specific, develops the marketing intangible in the form of strong brand.

- As per TPO, the fact of carrying out high intensity of AMP activities was itself a proof that there existed an arrangement between the assessee and the AE, that compelled the assessee to carry out this level of expenditure, which in terms of section 92B(1) read with section 92F(v) of the Income-tax Act, 1961 ("Act") was an "international transaction" that needed to be benchmarked.

- TPO also observed that the ratio of AMP expenditure to sales is quite high.

11. Before the revenue authorities, the appellant contended that the aforesaid view of the TPO is based on the wrong application of prevailing jurisprudence and therefore, is untenable in law for the following reasons:

- That under no circumstances does expenditure incurred on independent local Indian vendors or service providers (of advertising and marketing and other expenses incurred) by the Appellant for assistance in the sales promotion and marketing activities, be considered as an "international transaction" between two associated enterprise ('AE') under Section 92B(1) or 92B(2) of the Act.

- Therefore, in order to be characterized as an "international transaction', it would have to be demonstrated that the same arises pursuant to an arrangement, understanding or action in concert. A "transaction", per se involves a bilateral arrangement or contract between the parties. Unilateral action by one of the parties, without any binding obligation, in absence of a mutual understanding or contract, could not be termed as a "transaction". A unilateral action, therefore, cannot be characterized as an "international transaction" capable of invoking the provisions of Section 92 of the Act.

- In the instant case, the Appellant has incurred expenditure on AMP to cater to the needs of the customers in the local market. Such AMP expenditure was neither incurred at the instance/ behest of overseas AEs, nor was there any mutual agreement or understanding or arrangement as to allocation or contribution by the AE towards reimbursement of any part of AMP expenditure incurred by the Applicant for the purpose of its business. In absence of any understanding, arrangement, etc., no "transaction" or "international transaction" could be said to be involved with respect to such AMP expenditure incurred by the domestic enterprise, which may be covered within the provisions of Indian Transfer Pricing regulations. Further, in the present case, payment for advertisement, marketing and sales promotion is made by the Appellant (which is a tax resident of India) to other Indian third parties. Therefore, the twin requirements of section 92B of the Act do not exist in the present case, i.e.

a. The transaction involved is between Indian parties and no foreign party is involved;
b. The transaction of AMP expenses does not take place between two AEs.

- The AMP expenses incurred by the Appellant represent a domestic transaction and are undertaken with the third parties which are not covered under the definition of "international transaction" within the purview of Section 92 of the Act. Analysis of such domestic transactions undertaken with third parties, in respect of which, no reference has been made by the AO to the TPO is beyond the powers vested with the TPO under Section 92CA of the Act. Accordingly, the aforesaid addition made by the TPO is invalid and liable to be quashed.

- The distribution agreement between the Appellant and its AE confirms that 100 percent of the advertisement, marketing and promotion expenses will be borne by the AE (itself), and therefore in line with the distribution agreement, the Appellant has received reimbursement of advertisement expenses from its AE which has been duly reported in the form 3CEB as well as benchmarked in the transfer pricing report.

12. During the proceedings before the ld. CIT(A), the TPO was specifically asked to list out the FAR analysis to showcase the carrying out of DEMPE functions. In this regard, the TPO, in its report dated 30th August 2017, has made the following observations:

- The extremely high level of advertising and market promotion expenditure CAMP') by the Appellant is for promotion of brand of the AE in India and development of marketing intangibles for the products of the AEs.

- The Appellant had developed marketing intangibles for its Associated Enterprise ('AE') in India at its own cost and risk by investing huge sums in marketing and other selling activities. The AE of the Appellant has made nil contribution to total expenditure incurred by the Appellant on development of brand and marketing intangibles for the AEs in India. This is evident from the fact that the Appellant has launched and promoted 'Bacardi' brand in India and had incurred huge expenditure under AMP in earlier years and in the year under consideration.

- The Appellant has incurred a cost in connection with the benefit and services provided to the AE through the marketing expenditure. Since the benefit of entire expenditure incurred on AMP is flowing to the AE, the AMP expenditure was an international transaction under section 92B(1) read with clause (v) of section 92F of the Income Tax Act, 1961 ('Act').

- The brand received by the Appellant has no intrinsic value. The AMP expenses that the Appellant has incurred is adding value to the brand. It is the Appellant's marketing efforts that have increased the sales of the products of the Appellant. The increased sale will come about only when the Appellant is able to so position the brand in the market that it will have such powerful recall value that the

customer will choose it over its competitors. This is the benefit that is accruing to the brand which is the end result of the increased level of AMP expenses incurred by the Appellant.

- The Appellant is not the economic or legal owner of the brand. The legal ownership of the brand vests with the AE.

- The Appellant has characterized itself as a normal risk distributor but, it is strictly under the control of foreign entity. All important decisions are taken by the foreign entity, even the ownership of the trademark is retained by the AE. The penetration strategy adopted by the Appellant is such as to benefit the AE. Even the pricing is decided with the mutual discussions with the AEs.

- The expenditure being incurred by the Appellant involves promotion of AE's brand and thus, the Appellant's marketing efforts results in creating marketing intangibles in India and therefore, the Appellant must receive an appropriate return for such marketing efforts. The Appellant has through its efforts developed local marketing intangibles by

  i. Promoting AE's brand and creating awareness among Indian customers
  ii. Developing and maintaining network of sub-directors, dealers, retailers and other business partners.
  iii. Creating customer awareness and loyalty by advertisement, organizing events, exhibitions, trade shows, and conferences etc.

13. The aforesaid observations of the TPO were confronted to the appellant by the ld. CIT(A). The submission of the appellant is that,

- The alleged AMP expenditure are incurred by the Appellant for pushing sales of its products; Quantum or intensity of an expenditure per-se cannot be presumed to be expenditure incurred for the promotion or development of brand.

- "Bacardi" - one of the world most recognizable and valuable brands. The Appellant is not undertaking any brand building efforts for the AE's Brands, rather the Appellant is deriving the benefits of global "Bacardi" brand.

- Due to all of the above and many other strategized brand building efforts by the AE or Bacardi Limited, the Bacardi brand is one of the most respected and valuable global brands, and has been amongst the undisputed leaders of brand valuation for decades.

- AMP is necessary business expenditure and Appellant is direct beneficiary of such expenses. Any indirect benefit to third party (read AEs) is purely incidental.

- Seeking compensation for AMP expenditure is inconsistent with the characterization/business model of the Appellant; the Appellant is entitled to the economic benefits related to the ownership of brand 'Bacardi' in India.

- Incurrence of domestic AMP expenses does not constitute 'international transaction' under either of sub-sections (1) or (2) of section 92B of the Act.

14. On going through the entire issue, the ld. CIT(A) held as under:

- ✓ that under Sections 92B to 92F, the pre-requisite for commencing the TP exercise is to show the existence of an international transaction.
- ✓ The next step is to determine the price of such transaction.
- ✓ The third step would be to determine the ALP by applying one of the five price discovery methods specified in Section 92C.
- ✓ The fourth step would be to compare the price of the transaction that is shown to exist with that of the ALP and make the TP adjustment by substituting the ALP for the contract price. Under Section 92B (1) an 'international transaction' means-

  a) A transaction between two or more AEs, either or both of whom are non-resident;
  b) the transaction is in the nature of purchase, sale or lease of tangible or intangible property or provision of service or lending or borrowing money or any other transaction having a bearing on the profits, incomes or losses of such enterprises, and;
  c) Shall include a mutual agreement or arrangement between two or more AEs for allocation or apportionment or contribution to the any cost or

expenses incurred or to be incurred in connection with the benefit, service or facility provided or to be provided to one or more of such enterprises.

- ✓ The transactions listed in the Explanation under clauses (i) (a) to (e) to Section 92B are described as an 'international transaction'. This might be only an illustrative list, but significantly it does not list AMP spending as one such specific transaction.

- ✓ The settled position emerging out of various decisions of judicial authorities including jurisdictional Delhi High Court is that for a 'transaction' there has to be involvement of two associated entities and the Revenue has to show that there exists an 'agreement' or 'arrangement' or 'understanding' between two entities whereby one is obliged to spend excessively on AMP in order to promote the brand of other entity. The courts have held that it is important to demonstrate that the parties were "acting in concert". Further, there can be no "persons acting in concert" unless there is a shared common objective or purpose between two or more persons. The relationship can come into being only by design, by meeting of minds between two or more persons leading to the shared common objective or purpose. It is another matter that the common objective or purpose may be in pursuance of an agreement or an understanding, formal or informal.

- ✓ The ld. CIT(A) held that the TPO mainly relied on the TP study report that the appellant is engaged in brand

building exercise and hence, the benefit has been drawn by the foreign AE owning such brands.

- ✓ The ld. CIT(A) disagreed with the proposition of the TPO that this act of brand promotion on the part of appellant company as "action in concert" with its parent entity based on transfer pricing report. TPO worked out the excess AMP expenditure by applying bright line limit of 7.52% as ALP of AMP expenditure. Further, mark up of 15% was also applied to arrive at the amount of TP adjustment equivalent to the amount of compensation to be provided by AE for incurring AMP expenses for brand building.

- ✓ The ld. CIT(A) relied on the decision of Hon'ble Delhi High Court in CIT vs. EKL Appliances Ltd., wherein the court held that the very existence of international transaction cannot be a matter for inference or surmise.

- ✓ The ld. CIT(A) held that the TPO is not correct in treating AMP expenditure as international transaction in the absence of sufficient evidence towards understanding, arrangement or action in concert in the case of manufacturing segment. The high scale of AMP expenditure year on year basis per se cannot be the yardstick to hold it as international transaction. The ld. CIT(A) held that, at the best it can be the starting point to investigate but it cannot be taken as the evidence in itself.

- ✓ The ld. CIT(A) held that the appellant company is using the brand logo of the foreign AE as economic owner in a commercial sense for the purpose of exploiting it for the

business purpose. In the process, the foreign AE, the owner of the brand, would have also got benefitted incidentally due to Brand building as a result of appellant company's spending on AMP in India. The ld. CIT(A) held that there is no dispute that such AMP expenditure was very much required by the appellant company for carrying out and growth of its business in India. There is no basis in the finding of TPO that the AMP expenditure is excessive vis-a-vis the requirement of the appellant company in running the business in India.

- ✓ Holding thus, the ld. CIT(A) held that the TP adjustment in respect of such AMP expenditure to foreign AE(brand legal owner) without any basis is not justified.

15. Having said so, the ld. CIT(A) held that there is a rationale to factor in AMP intensity adjustment while equating the functional profit into the comparables in TNMM benchmarking. The "bright line test" which is the mirror image of intensity approach has no statutory mandate. Hence, cannot be upheld.

16. With regard to the receivables, we hold that the netting of interest paid or receivables as sought by the assessee may be accorded and the benefit of brought forward losses be allowed as per the provisions of Income Tax Act.

17. In the result, the appeals of the Revenue are dismissed and the appeals of the assessee are allowed.

Order Pronounced in the Open Court on 20/05/2022.

Sd/-	**Sd/-**
(Astha Chandra)	**(Dr. B. R. R. Kumar)**
Judicial Member	**Accountant Member**

Dated: 20/05/2022

Subodh Kumar, Sr. PS
Copy forwarded to:
1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

ASSISTANT REGISTRAR