

**IN THE INCOME TAX APPELLATE TRIBUNAL
“C” BENCH : BANGALORE**

**BEFORE SHRI N.V. VASUDEVAN, VICE PRESIDENT
AND
Ms. PADMAVATHY S, ACCOUNTANT MEMBER**

IT(TP)A No.198/Bang/2022
Assessment year : 2017-18

GCorp Services Private Limited, No.21/19, Craig Park Layout, Off M.G. Road, Bengaluru – 560 001. PAN: AAECG 6624M	Vs.	The Assistant Commissioner of Income Tax, Circle 3(1)(1), Bengaluru.
APPELLANT		RESPONDENT

Appellant by	:	Shri Nageswar Rao, Advocate
Respondent by	:	Shri Praveen Karanth, CIT(DR)(ITAT), Bengaluru.

Date of hearing	:	06.09.2022
Date of Pronouncement	:	13.09.2022

ORDER

Per Padmavathy S., Accountant Member

This appeal is against the final assessment order passed by National Faceless Assessment Centre u/s. 143(3) r.w.s. 144C(13) of the IT Act dated 28.1.2022 for the assessment year 2017-18.

2. The only issue arising out of the various grounds raised by the assessee relates to the transfer pricing adjustment done on account of interest paid on Non-convertible Debentures (NCDs) issued by the assessee to its Associated Enterprise (AE). Though the assessee

contented the adjustment raising various grounds, during the course of hearing, the Id. AR submitted that out of the grounds raised, if grounds pertaining to the TPO not considering the effective rate of interest taking into account the moratorium period are adjudicated, then the rest of the grounds can be left open. Accordingly, we will adjudicate the issue of TPO not applying the effective rate of interest without considering the moratorium period and the relevant grounds raised in this regard are extracted below –

(8) The Id AO/TPO pursuant to the directions of the Hon'ble DRP erred in law and in facts by not considering the moratorium period benefit availed by the appellant and by rejecting the effective rate of interest testing the arm's length nature of the international transaction of interest accrued on NCDs

(9) The Id DRP erred in law and in facts in arbitrarily holding that there is no requirement for adopting a different rate of interest on account of moratorium period since appellant could have paid interest during such period as well without appreciating that the appellant has been benefitted from the moratorium period granted by the associated enterprise which needs to be factored in while determining the arm's length interest rate

3. The assessee is a company engaged in the business of real estate development. The assessee has issued NCDs in three tranches to its AE. During the year under consideration, the assessee has accrued on these NCDs @ 15% p.a. for first two tranches and @ 14.25% p.a. for the third tranche as per details given below:-

International Transactions	Amount (INR)
Interest accrued on NCDs issued in Tranche I	10,02,00,000
Interest accrued on NCDs issued in Tranche II	6,67,50,000
Interest accrued on NCDs issued in Tranche III	6,34,12,501
Total	23,03,62,501

4. The assessee benchmarked the said transactions using CUP method. In the TP study, the assessee used Comparable Uncontrolled Price (CUP) method as the most appropriate method for determining the arm's length price (ALP) of the interest rate on NCDs issued to the AE. As per the comparables chosen by the assessee, the median rate of interest was worked out at 11.45%. As per the terms agreed with the AE the assessee is having a moratorium period of 60 months for Tranche-I, 58 months & 11 days for Tranche-II and 24 months for Tranche-III. The assessee in the TP study computed the effective rate of interest taking into account the moratorium period worked out at 11.5% for Tranche-I, 11.61% for Tranche-II and 13.52% for Tranche-III. The assessee therefore concluded that rate of interest is within arm's length price. The TPO did not accept the effective rate considered by the assessee and made the TP adjustment of Rs. 4,97,51,100 by applying the coupon rate of 15% as interest on Tranche I & II of NCDs. The DRP rejected the objections raised by the assessee on the ground that there is an option available to the assessee to pre-pay the interest and therefore the effective rate of interest cannot be compared for computing the ALP.

5. The Id. AR submitted that the assessee though has provided in the books of accounts interest @ 15% owing to the moratorium period agreed with the AE, the assessee has not paid out any amount in cash by way of interest during the year under consideration. The Id. AR also submitted that the assessee is in discussion with its AE for further extension of the moratorium period. Thus it was contended by the Id

AR that on account of savings in cash outflow, having regard to time value of money, the rate of interest effectively will be lower than the agreed coupon rate. The ld. AR also brought to our attention the detailed submission made before the TPO with regard to arriving at the effective rate of tax. The ld AR further submitted that it is not correct on the part of the DRP to confirm the adjustment by stating that there is a pre-payment clause in the agreement ignoring the fact that the assessee has not paid any interest till date. In this regard, the ld. AR drew our attention to the decision of Pune Bench of the Tribunal in the case of *Goodyear South Asia Tyres P. Ltd. V. ACIT (ITA No.1431/PUN/2010 dated 28.11.2014)* where the Tribunal has held that for the purpose of comparison while arriving at the ALP, effective rate of interest need to be calculated considering the moratorium period as agreed between the parties.

6. The ld. DR relied on the order of the lower authorities.

7. We have heard the rival submissions and perused the material on record. We notice that the Pune Bench of the Tribunal in *Goodyear South Asia Tyres P. Ltd. (supra)* has considered a similar issue and held that :-

“16. We have carefully considered the rival submissions. Before proceeding to adjudicate the rival stands, it would be appropriate to briefly touch-upon the manner in which the impugned liability towards interest on loans raised from associated enterprises has been incurred by the assessee. Pertinently, the loans in question, namely, Technical knowhow loan, Foreign currency cash loan and ECB loan have been availed by the assessee from Goodyear Tyre and Rubber Co. an associated enterprise based in USA.

Assessee has made a payment of interest of Rs.2,96,25,682/- in respect of the aforesaid three loans. Regarding the technical knowhow loan, the details are that the assessee company entered into a technical assistance and license agreement with its associated enterprise on 21.06.1994 for provision of technical assistance in manufacturing of Earthmover tyres, Radial tyres, Radial passenger tyres, etc.. In terms of the said agreement, assessee was required to pay a lump sum technical knowhow fee of USD one crore. The said agreement was subsequently amended vide a supplementary agreement dated 01.10.2003, whereby the agreed amount of technical knowhow fee payable to Goodyear USA was reduced to USD 67,50,000/-. On 11th July, 1996 assessee entered into an agreement with the associated enterprise in terms of which the technical knowhow fee payable was converted into a loan which was initially interest-free for the first seven years period and was thereafter re-payable in three branches carrying interest @ 12% per annum. Consequent to the modification of the technical assistance agreement done on 01.10.2003, the loan agreement was also modified by an agreement dated 02.10.2003 whereby the principal amount of loan was reduced from USD one crore to USD 67,50,000/-. The loan agreement dated 11.07.1996 was approved by the Reserve Bank of India vide letter dated 17.04.1996, which was subsequently amended vide RBI letter dated 10.06.2003 reducing the principal amount of loan from USD one crore to USD 67,50,000/-. Copies of such approvals have been placed in the Paper Book at pages 469 – 473. In terms of the RBI approvals, it transpires that the technical knowhow loan was interest free for initial period of seven years from the date on which technical knowhow fee was payable and at the end of the seven years the loan was repayable in five equal installments together with interest @ 12% per annum. Notably, such interest was payable for the period after the moratorium period of seven years. The RBI approval also permits that during the seven years moratorium period, the loan amount was to be increased by 5% of the principal amount to account for the foreign exchange risk coverage. The aforesaid increase on account of foreign exchange risk coverage was not applicable after the close of seven year's moratorium period. Subsequently, RBI also extended the period of moratorium for payment of interest by two years, but in this extended period of moratorium no further increase on account of

exchange rate fluctuation was allowed. All these features of the technical knowhow loan are emerging from the material on record and in-fact the same are not in dispute.

17. Now, with regard to the foreign currency cash loan, the details are as follows. On 16.08.1995 assessee entered into a foreign currency cash loan agreement with its associated enterprise, namely, Goodyear Tyre and Rubber Co., USA for USD 56,00,000 for the purpose of financing import of capital goods. The said agreement was also approved by the Reserve Bank of India vide communication dated 27.09.1995, a copy of which has been placed in the Paper Book at page 393. In terms of the said approval by the Reserve Bank of India, it is prescribed that the loan shall remain interest-free for a period of seven years from the date of grant of loan and at the end of the seven years it shall be repaid in five equal installments together with interest @ 12%. A perusal of the RBI approval reveals that other terms and conditions in respect of above foreign currency cash loan are similar to those prescribed for technical knowhow loan, which we have succinctly enumerated in the earlier paras.

18. Thirdly, the ECB loan raised by the assessee from its associated enterprise, namely, Goodyear Tyre and Rubber Co., USA is of a sum of USD 90,00,000. The said loan has been raised vide an agreement dated 12.09.2003 and such financing is to meet the working capital requirements. In terms of the said agreement, a copy of which has been placed in the Paper Book at page 438, the borrowing is repayable in three installments by 15.03.2006, 31.12.2006 and 31.12.2007. The ECB loan was availed by the assessee at the interest rate of LIBOR plus 3% as notified by the RBI in its Circular No.36 dated 14.11.2003, which was prevailing when the assessee raised such ECB loan.

19. In the background of the aforesaid terms and conditions of the loans raised from the associated enterprise, assessee paid interest aggregating to Rs.2,96,25,683/- to its associated enterprises. The assessee benchmarked the aforesaid transaction of payment of interest by applying Comparable Uncontrolled Price (CUP) method as the most appropriate method and thus justified that the aforesaid payment of interest was at an arm's length price. The stand of the assessee was that interest charged on technical knowhow loan and foreign currency cash loan @ 12% was lower

than the Prime Lending Rate (PLR) of interest charged by the State Bank of India at the relevant point of time, i.e. 12.25% - 13.25%. Assessee also justified the rate of interest on the ground that technical knowhow and foreign currency loans were specifically approved by the RBI wherein the rate of interest payable was also prescribed. Even with regard to the ECB loan availed, it was contended that the same was in accordance with guidelines and the interest rate ceiling prescribed by the RBI at the time of obtaining such loan. The aforesaid submissions of the assessee have not found favour with the TPO. One of the points raised by the TPO is that the technical knowhow loan has been obtained by conversion of technical knowhow fee payable to Goodyear Tyre and Rubber Co.. As per the TPO, what is indeed payable by the assessee is a charge/fee for obtaining technical knowhow and that it is not a pure cash loan taken by the assessee. According to the TPO, such a transaction cannot be compared with the prevailing lending rates in the domestic market at the time of raising of loan. Instead, according to him, the arm's length price would have to be determined by benchmarking the interest rates prevailing on borrowings from abroad at the time of payment of interest. Therefore, the plea of the assessee for comparing the interest paid @ 12% with the Prime Lending Rate of SBI was not accepted. Another reason advanced by the TPO is that assessee was also required to account for exchange fluctuation burden during the currency of the loan. Under these circumstances, as per the TPO, such a loan cannot be treated to be at par with a domestic loan raised from an Indian bank. In our view, the TPO is justified in saying that the impugned transactions involve loan liabilities in foreign currency and therefore it is not a domestic borrowing so as to compare the transaction of payment of interest with the domestic Prime Lending Rate of the Indian banks.

20. So however, one pertinent point has been raised by the assessee before us to the effect that in order to benchmark the interest cost incurred by the assessee it would be appropriate to evaluate the effective rate of interest payable by the assessee on the technical knowhow loan and foreign currency cash loan raised from the associated enterprise. Notably, the said argument has been raised by the assessee not only before us but also before the TPO as is evident from para 5 of the order of the TPO

wherein the arguments of the assessee have been reproduced. The plea of the assessee is that the rate of interest of 12% for the current year cannot be considered in isolation by ignoring the interest-free moratorium period of initial nine years. The Ld. Representative for the assessee submitted in the course of hearing that although the rate of interest payable during the five year repayment schedule is 12%, but if the initial interest-free period of nine years is considered, the effective rate of interest would be even lower than the rate of 5.46% considered by the TPO as an arm's length rate. In this context, our attention has been drawn to a working furnished in the course of the hearing. With respect to the technical knowhow loan, it is explained that actual interest cost of Rs.1,15,58,522/- (inclusive of the increased cost of borrowings on account of exchange in fluctuation) is spread over the period of loan the effective rate of interest for the assessment year 2006-07 works out to 2.51% only. Similarly, with respect to the foreign currency cash loan on spreading the actual interest cost of 1,39,69,848/- over the period of loan and also taking into account the increased borrowings on account of exchange rate fluctuation, the effective rate of interest for assessment year 2006-07 comes to 2.67%. It is sought to be pointed out that the aforesaid effective rates of interest is less than the arm's length rate of interest considered by the TPO in respect of technical knowhow and foreign currency cash loans. Therefore, there was no necessity of making any adjustment in the transaction of payment of interest on account of technical knowhow and foreign currency cash loans in order to bring it to the level of arm's length price. The aforesaid workings are tabulated as under :-

(i) Regarding technical knowhow loan :-

Year	Loan outstanding (A)	Interest spread (B)	Exchange fluctuation (C)	Interest +exchange fluctuation cost D=B+C	Interest rate % D/A
1995	49,795,823	963210	-	963,210	1.93
1996	52,285,614	963210	2489791	3,453,001	6.60
1997	117,880,405	963210	2489791	3,453,001	2.93
1998	198,180,446	963210	5645041	6,608,251	3.33
1999	207,558,238	963210	9377791	10,341,001	4.98
2000	215,208,767	963210	7650529	8,613,739	4.00
2001	220,853,808	963210	5645041	6,608,251	2.99
2002	223,691,325	963210	2837517	3,800,727	1.70
2003	223,691,325	963210	-	963,210	0.43
2004	223,691,325	963210	-	963,210	0.43
2005	223,691,325	963210	-	963,210	0.43
2006	210,246,455	963210	-	963,210	0.46
Total/average		11,558,522	36,135,489	48,694,001	2.51

(ii) Regarding foreign currency cash loan :-

Year	Loan outstanding (A)	Interest spread (B)	Exchange fluctuation (C)	Interest +exchange fluctuation cost D=B+C	Interest rate % D/A
1996	13,44,02,400	12,69,986	-	12,69,986	0.94
1997	19,97,52,520	12,69,986	67,20,120	79,90,106	4.00
1998	20,94,04,140	12,69,986	9651620	1,09,21,606	5.22
1999	21,90,55,760	12,69,986	9651620	1,09,21,606	4.99
2000	22,87,07,380	12,69,986	9651620	1,09,21,606	4.78
2001	23,83,59,000	12,69,986	9651620	1,09,21,606	4.58
2002	24,38,24,000	12,69,986	5465000	67,34,986	2.76
2003	24,38,24,000	12,69,986	-	12,68,986	0.52
2004	24,38,24,000	12,69,986	-	12,69,986	0.52
2005	24,38,24,000	12,69,986	-	12,69,986	0.52
2006	24,38,24,000	12,69,986	-	12,69,986	0.52
Total/average		1,39,69,848	5,07,91,600	6,47,61,448	2.67

21. The aforesaid workings have not been disputed in the course of hearing before us. Be that as it may, the moot point is as to whether it is relevant to consider the stated rate of interest of 12% or the effective rate of interest for the purpose of benchmarking the transaction with comparable cases. The terms and conditions of the agreement approved by the RBI in relation to technical knowhow and foreign currency cash loans, which have been succinctly noted

by us in the earlier part of this order, clearly establish that in the initial period of nine years there was a moratorium on interest payment and that assessee was not required to incur any interest costs. It is only subsequent to the moratorium period, assessee was to incur interest cost and that too, during the period of repayment of loans. Of course, during the moratorium period the liability towards principal amount of loan was liable to be increased by 5% on account of exchange rate fluctuation. Considering the entirety of terms and conditions, therefore, the cost of borrowings to the assessee (i.e. on technical knowhow and foreign currency cash loans) are to be computed after factoring the initial period of moratorium. **Therefore, it would be inappropriate to merely compare the stated rate of interest of 12% with the prevailing rates without taking into consideration the specific terms and conditions of the assessee's borrowings. Therefore, in-principle, we are agreement with the assessee for the proposition that it would be appropriate to compute effective rate of interest in respect of international transaction of loan entered into with the associated enterprise before carrying out the exercise of benchmarking such international transactions vis-à-vis the arm's length price/interest of the comparable uncontrolled transactions.** On this aspect, the Ld. Departmental Representative reiterated the stand of the TPO to the effect that the Transfer Pricing Regulation of India provide that for comparability of an uncontrolled transaction with an international transaction, data relating to the relevant financial year alone is to be used and that the data relating to other periods not being more than two years prior to such financial year can be considered only if such data revealed facts which have an influence on determination of the transfer pricing in relation to the transaction being compared. In other words, as per the Ld. Departmental Representative, the aforesaid approach of considering the data of other years would not be appropriate. In our considered opinion, the aforesaid argument is quite fallacious. While computing the yearly effective rate of interest in respect of impugned loans what is being sought is the factoring of the terms and conditions of the loan agreements. Moreover, the point being made out by the TPO is on account of sub-rule (4) of rule 10B of the Income Tax Rules, 1962, which is of no relevance in the present context. The aforesaid sub-rule provides that the data to be used in analyzing the comparability of an uncontrolled transaction with an international transaction shall be the data relating to the financial

year in which the international transaction has been entered into. The said provision has no relevance in the present context, wherein the issue relates to identifying and determining the correct international transaction which is required to be benchmarked under the Transfer Pricing Regulation. Therefore, the plea of the Revenue on this aspect is liable to be rejected. We hold so.

22. At the time of hearing, the Ld. Representative also relied upon the decision of the Ahmedabad Bench of the Tribunal in the case of DCIT vs. Hitachi Home & Life Solutions (India) Ltd. vide ITA No.182/Ahd/2011 & Others dated 12.08.2012 wherein the royalty paid by the assessee at 3.75% to the associated enterprise was sought to be benchmarked. The Revenue determined the arm's length rate of payment of royalty @ 3%, while assessee was charged 3.75% by the associated enterprise. The assessee had put up a defence on the ground that the effective rate of royalty payable was @ 2.30% on sales. It was contended that the royalty of 3.75% was payable after reducing various expenses from the sale value of the products but the effective rate worked out to 2.30%, which was comparable to arm's length rate being considered by the Revenue. On the basis of the assertion of the assessee to the effect that the effective rate of royalty was lower than the comparable transaction, the addition made by the TPO was deleted by the Tribunal. The Ld. Representative for the assessee submitted that the concept of the effective rate of royalty as against the stated rate of royalty was approved by the Tribunal for the purpose of benchmarking the international transaction of the assessee. In the present case also, in our view the ratio of the decision of the Ahmedabad Bench of Tribunal in the case of Hitachi Home & Life Solutions (India) Ltd. (supra) applies. Therefore, in conclusion, without opining on the other arguments raised by the assessee, we deem it fit and proper to delete the addition with respect to the interest paid on Technical knowhow and foreign currency cash loans on the ground that the effective rate of interest incurred by the assessee is lower than the arm's length rate of interest considered by the TPO. Thus, on this aspect assessee succeeds.

8. The Hon'ble Tribunal in the above decision has clearly laid out the ratio that it would be appropriate to compute effective rate of

interest in respect of international transaction of loan entered into with the associated enterprise before carrying out the exercise of benchmarking such international transactions vis-à-vis the arm's length price/interest of the comparable uncontrolled transactions. We notice that the assessee has brought to the notice of the lower authorities that decision of the Hon'ble Tribunal which has not been taken into consideration. In assessee's case, though the coupon rate agreed is at 15% and 14.25%, there is a moratorium clause whereby assessee is having a moratorium period of 60 months for Tranche-I, 58 months & 11 days for Tranche-II and 24 months for Tranche-III. The assessee in the TP study has also given a detailed working for arriving at effective rate of interest (**Annexure 3.1 to 3.3 of TP study**) after considering the said moratorium period. However, we notice that the lower authorities have not considered the said working and have rejected the same on the ground that assessee has debited the Profit & Loss account with interest accrued at 15% / 14.25% and also on the ground that there is a pre-payment of interest clause in the agreement. This, in our considered view, is not the correct approach since the time value of money needs to be considered and debit to the Profit & Loss account is not the relevant factor for determination of ALP. Further the assessee has not paid any amount towards interest to the AE till date and as per the submissions of the Id AR, the assessee is in talks with the AE for extension of the moratorium period. This factual position has not been considered by the TPO/DRP. In view of the above discussion and considering, the decision of the Hon'ble Pune Bench of the Tribunal in

the case of *Goodyear South Asia Tyres P. Ltd. (supra)*, we remit the issue back to the TPO to analyse the transfer pricing study done by the assessee afresh. While doing the fresh benchmarking of the interest on NCDs, the TPO is directed to consider the ratio laid down by decision of the Tribunal in the case of *Goodyear South Asia Tyres P. Ltd. (supra)* and the comparables chosen by the assessee. Needless to say that the assessee may be given an opportunity of being heard. Since the issue is remitted back to the TPO for fresh consideration of the TP study conducted by the assessee, the rest of the grounds raised by the assessee with regard to the TP adjustment are left open.

9. The assessee's appeal is allowed for statistical purposes.

Pronounced in the open court on this 13th day of September, 2022.

Sd/-
(N V VASUDEVAN)
VICE PRESIDENT

Sd/-
(PADMAVATHY S)
ACCOUNTANT MEMBER

Bangalore,
Dated, the 13th September, 2022.

/Desai S Murthy/

Copy to:

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

By order

Assistant Registrar
ITAT, Bangalore