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

BEFORE SHRI PRASHANT MAHARISHI, AM
AND
SHRI SANDEEP SINGH KARHAIL, JM

ITA No. 1578/MUM/2022
(Assessment Year 2019-20)

ITA No. 1579/MUM/2022
(Assessment Year 2018-19)

MFE Formwork Technology SDN BHD Unit No. 504, Tower 1 Star Hub, Airport Road, Behind ITC Grand, Maratha Hotel , Andheri (East) Mumbai-400 099	Vs.	CIT(Intl Tax) Room No. 1601, 16th Floor, Air India Bldg. Nariman Point, Mumbai-400 021
(Appellant)		**(Respondent)**

PAN No. AAGCM4280M

Assessee by	:	Shri.P.J.Pardiwala/Harsh Kothari/Bhupa Rapelli
Revenue by	:	Ms. Surabhi Sharma-CIT DR

Date of hearing: 07.11.2022
Date of pronouncement : 24.01.2023

O R D E R

PER PRASHANT MAHARISHI, AM:

01. ITA No.1578/Mum/2022 for A.Y. 2019-20 and ITA No.1579/Mum/2022 for A.Y. 2018-19 is filed by the assessee against the order passed under Section 263 of the Income-tax Act, 1961 (the Act) by the CIT, International Taxation-3, Mumbai, dated 7th June, 2022 for A.Y. 2017-18 and A.Y. 2018-19.

02. The assessee has raised following grounds of appeal for A.Y. 2018-19:-

"1. On the facts and circumstances of the case and in law, the order passed by the CIT under section 263 of the Act enhancing and modifying the assessment framed under section 143(3) of the Act vide order dated 15 April 2021 as erroneous and prejudicial to the interest of the revenue is without jurisdiction, bad in law and void-ab-initio.

The Appellant prays that the order dated 7 June 2022 passed under section 263 of the Act, by the CIT be struck down as invalid, null and void ab initio addition the original assessment order of the Assessing Officer be restored.

2. On the facts and circumstances of the case and in law, the CIT erred in holding that the assessment order is erroneous and prejudicial to interest of revenue on the issue of profits attributable to Appellant's Permanent Establishment ('PE') in India even though the same had been discussed and scrutinized by the Assessing Officer in detail while framing the assessment under section 143(3) of the Act and passing order dated 15 April 2021.

The Appellant prays that the order dated 7 June 2022 passed under section 263 of the Act, by the CIT be struck down as invalid, null and void ab initio.

3. Without prejudice to Ground numbers 1 and 2, on the facts and circumstances of the case and in law, the CIT erred in holding that the method of computing profits of ₹ 4,79,33,403 attributable to PE as adopted by appellant is inappropriate whereas the

CIT has adopted the same method and arbitrarily changed allocation of weights of various activities between the Appellant and its PE to arrive at a higher attribution of profits at ₹ 19,21,56,878, being 35% of gross profits of the Appellant in respect of goods sold to Indian customer without granting deduction for full operating expenses incurred by the appellant.

The Appellant prays that the percentage of profits as attributable to Appellant's PE in India should be restored to 24% and that profits attributable to its PE in India should be determined on net basis after granting deduction for full operating expenses.

4. Without prejudice to Ground numbers 1, 2, and 3 above, on the facts and circumstances of the case and in law, the CIT erred in placing reliance on the decision of the Hon'ble Delhi High court in the case of Rolls Royce PLC 339 ITR 147 (Del), without appreciating that facts of the Appellant's case are different than the facts in the case of Rolls Royce.

5. Without prejudice to Ground numbers 1, 2, 3 and 4 above, on the facts and circumstances of the case and in law, while the CIT has relied on the decision of Rolls Royce PLC (supra) to justify his action to attribute higher amount of profits to Appellant's PE in India, the CIT erred in attributing gross profit to the Appellant's PE in India after reducing only the marketing fees paid to agent in India whereas in the case of Rolls Royce (supra) profits attributable to India as computed on net basis.

Appellant prays that profits attributable to its PE in India should be determined on net basis after granting deduction of full operating expenses incurred by the appellant from the gross profit to derive income attributable in India.

6. Without prejudice to Ground numbers 1, 2, 3, 4 and 5 above, on the facts and circumstances of the case and in law, the CIT erred in not applying the operating profit ratio of 1.67% for computing the profits attributable to Indian PE which would have been in line with the decision in the case of Rolls Royce PLC 339 ITR 147 (Del) as relied on by the CIT himself to compute the income of the Appellant.

The Appellant prays that the CIT to be directed apply 1.67% operating profit ration to arrive at net profit attributable to Indian operations.

7. Without prejudice to Ground numbers 1, 2, 3, 4, 5 and 6 above, on the facts and circumstances of the case and in law, the CIT erred by not considering that since the PE in India was remunerated at arm's length price no further attribution of income is warranted as per decision of Hon'ble Supreme Court in the case of Morgan Stanley & Co. 292 ITR 416 (SC) and thus the original assessment order of the Assessing Officer is not erroneous and prejudicial to interest of revenue.

The Appellant prays that the order dated 7 June 2022 passed under section 263 of the Act, by the CIT be struck down as invalid, null and void ab initio."

03. The assessee has also raised following grounds of appeal for A.Y. 2019-20:-

> *"1. On the facts and circumstances of the case and in law, the order passed by the CIT under section 263 of the Act enhancing and modifying the assessment framed under section 143(3) of the Act vide order dated 29 October 2021 as erroneous and prejudicial to the interest of the revenue is without jurisdiction, bad in law and void ab-initio.*
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> *The appellant prays that the order dated 7 June 2022 passed under section 263 of the Act, by the CIT be struck down as invalid, null and void ab initio and the original assessment order of the Assessing Officer be restored.*
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> *2. On the facts and circumstances of the case and in law, the CIT erred in holding that the assessment order is erroneous and prejudicial to interest of revenue on the issues of profits attributable to Appellant's Permanent Establishment ('PE') in India even though the same had been discussed and scrutinized by the Assessing Officer in detail while framing the assessment under section 143(3) of the Act and passing order dated 29 October.*
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> *The Appellant prays that the order dated 7 June 2022 passed under section 263 of the Act, by the CIT be struck down as invalid, null and void ab-initio*
>
> *3. Without prejudice to Ground Number 1 and 2 above, on the facts addition circumstances of the case and in law, the CIT erred in holding that the*

method of computing profits of ₹ 7,31,82,787 attributable to PE as adopted by appellant is inappropriate whereas the CIT has adopted the same method and arbitrarily changed allocation of weights of various activities between the Appellant and its PE to arrive at a higher attribution of profits at ₹ 28,87,84,334 being 35% of gross profits of the Appellant in respect of goods sold to Indian customers without granting deduction for full operating expenses incurred by the appellant.

The Appellant prays that the percentage of profits as attributable to Appellant's PE in India should be restored to 24% and that profits attributable to its PE in India should be determined on net basis after granting deduction for full operating expenses.

4. Without prejudice to Ground Number 1, 2 and 3 above, on the facts and circumstances of the case and in law, the CIT erred in placing reliance on the decision of the Hon'ble Delhi High Court in the case of Rolls Royce PLC 339 ITR 147 (Del), without appreciating that facts of the Appellant's case are different than the facts in the case of Rolls Royce.

5. Without prejudice to Ground number 1, 2, 3 and 4 above, on the facts and circumstances of the case in law, while the CIT has relied on the decision of Rolls Royce PLC (Supra) to justify his action to attribute higher amount of profits to Appellant/s PE in India, the CIT erred in attributing gross profits to the Appellant's PE in India after reducing only the marketing fees paid to agent in India whereas in the

case of Rolls Royce (supra) profits attributable to India was computed on net basis.

Appellant prays that profits attributable to its PE in India should be determined on net basis after granting deduction of full operating expenses incurred by the appellant from the gross profit to derive income attributable in India.

6. Without prejudice to Ground number 1, 2, 3, 4 and 5 above, on the facts addition circumstances of the case and in law, the CIT erred in not applying the operating profit ration of 6.70% for computing the profits attributable to India PE which would have been in line with the decision in the case of Rolls Royce PLC 339 ITR 147 (Del) as relied on by the CIT himself to compute the income of the Appellant.

The Appellant prays that the CIT to be directed to apply 6.70% operating profit ratio to arrive at net profit attributable to India operations.

7. Without prejudice to Ground numbers 1, 2, 3, 4, 5 and 6 above, on the facts and circumstances of the case and in law, the CIT erred by not considering that since the PE in India was remunerated at arm's length price no further attribution of income is warranted as per decision of Hon'ble Supreme Court in the case of Morgan Stanley & Co. 292 ITR 416 (SC) and thus the original assessment order of the Assessing Officer is not erroneous and prejudicial to interest of revenue.

The Appellant prays that the order dated 7 June 2022 passed under section 263 of the Act, by the CIT be struck down as invalid, null and void ab initio."

04. We first take the facts for A.Y. 2018-19. The assessee is a non-resident company incorporated in Malaysia. It supplies aluminium formwork that finds application in construction of buildings. It is a wholly owned subsidiary of MFC Formwork technology in India Pvt. Ltd. The assessee has entered into a marketing services agreement with Indian entity to promote and market the products within India and to educate the prospective customers the benefits of the product. A technical service agreement was so entered wherein entities require to providing support of formwork supplied by Malaysia to its customer in India. The Indian entity qualifies as a dependent agent of the assessee as per Article 5 of the Double Taxation Avoidance Agreement between India and Malaysia. Therefore, assessee had a permanent establishment in India. Thus, the assessee has filed the return of income of such Permanent Establishment. The assessee submitted that 24% of gross profit based on FAR analysis as taxable income of the assessee PE. The assessee has computed the profit attributable to the activity of Permanent Establishment (PE) in India from the sales based in India. Thus, the assessee computed sales made in India of ₹420 crores, reduced the cost of sales proportionate of ₹351 crores, computed gross profit at ₹68.64 crores. It applied 24% ratio being profit attributable to Indian operations amounting to ₹16.47 crores. From this, assessee reduced

the marketing fees paid to its agent's i.e. Indian entity in India of ₹11.66 crores and derived taxable profit of Rs. 4.79 crores. Interest on income tax refund was also added thereon and taxable income of the PE was computed at ₹4,91,38,893/-.

05. The learned Assessing Officer accepted the ratio of 24% gross profit ratio for attribution of profits. Accordingly, the total income of the assessee was assessed under Section 143(3) of the Act by learned DCIT, International Taxation, Circle 3(2) (1), Mumbai under Section 143(3) of the Act as per order dated 15th April, 2021 at the returned income.

06. The learned PCIT, on examination of the records, found that the reason for selection of case for scrutiny was the large claim of refund, which has arisen because of ratio of attribution of profit. The learned Assessing Officer has not applied his mind on the FAR analysis submitted by the assessee on the issue of attribution of income to the permanent establishment. The learned Assessing Officer has also not conducted proper enquiry. Further, marketing expenses accepted as borne exclusively by the assessee is again incorrect and without due application of mind. Therefore, the profit further reduced by the assessee by ₹11.68 crores is not correct. Accordingly, a notice under Section 263 of the Act was issued on 4th April, 2022 holding that the assessment order passed on 29th April, 2021, was erroneous and prejudicial to the interest of the Revenue.

07. The assessee submitted his reply stating that the learned Assessing Officer has conducted specific enquiry as per notice dated 24th February, 2021, which was replied by the assessee on 2nd March, 2021. Assessee further submitted that assessment proceedings from A.Y. 2013-14 to A.Y. 2019-20, attribution rate of 24% is consistently applied and accepted. Therefore, there is no error in the assessment order. It was further stated that the facts were known to the jurisdictional Assessing officer, where the certificate for lower deduction of tax was obtained. Assessee once again explained the business of Assessee Company in India, basis of attribution of income, methodology of allocation etc, and FAR analysis. However, the learned CIT held that the learned Assessing Officer did not make any enquiry. The learned Assessing Officer simply accepted the attribution at the rate of 24% of the gross profit. The CIT also held that there is no rational for further reducing the total marketing fees of ₹11.68 crores. Accordingly, he held that the attribution should have been on the basis of net expenses. Accordingly, he held that the ratio of attribution of 24% should be applied after reduction of 11.68 crores from the gross profit of ₹68.64 crores, whereas, the assessee has applied attribution rate to the gross profit and thereafter, took the deduction of 11.68 crores.Accordingly order u/s 263 was passed.

08. Identically revisionary order was also passed for AY 2019-20.

09. The learned Authorized Representative submitted that identical issue arose in the case of the assessee for A.Y. 2017-18, wherein on identical facts and circumstances the order under Section 263 of the Income-tax Act, 1961 (the Act) was passed by the learned CIT. The matter travelled before the co-ordinate Bench in ITA No.890/Mum/2022 dated 30th August, 2022, wherein the order passed by the learned PCIT under Section 263 of the Act for that assessment year was quashed. He also submitted copy of the above order and extensively narrated the facts of the findings of the co-ordinate Bench.

010. The ld CIT DR relied up on the orders of the ld PCIT.

011. We have carefully considered the rival contentions and perused the orders of the lower authorities. We have also carefully gone through the order passed under Section 263 of the Act by the learned PCIT. We also find that identically for A.Y. 2017-18 the learned PCIT invoked the provisions of Section 263 of the Act vide order dated 25th March, 2022, which travelled before the co-ordinate Bench in ITA No.890/Mum/2022, wherein the order dated 30th August, 2022 was passed setting aside the revision order for that year. There is no change in the facts and circumstances of the case.

012. The co-ordinate Bench held as under:-

> *"1. By way of this appeal, the assessee appellant has called into question correctness of the order dated 25th March 2022, passed by the learned*

Commissioner of Income Tax, under section 263 r.w.s. 143(3) of the Income Tax Act, 1961, for the assessment year 2017-18. The first and core grievance of the assessee is as follows:

> *On the fact and in the circumstances of the case and in law, the order passed by the CIT under section 263 of the Act, enhancing and modifying the assessment framed under section 143(3) of the Act vide order dated 18 December 2019, as erroneous and prejudicial to the interest of the revenue is without jurisdiction, bad in law and void ab initio.*

2. To adjudicate on this appeal, only a few undisputed material facts need to be taken note of. The assessee before us is a company incorporated in, and tax resident of, Malaysia, and there is no dispute on the point that the assessee is entitled to the benefits of the India Malaysia Double Taxation Avoidance Agreement [Indo-Malaysian tax treaty, in short]. The assessee group has a wholly owned subsidiary in India, by the name of MFE Formwork Technology India Pvt. Ltd (MFE-India, in short). The assessee has entered into a Marketing Service Agreement (MSA) with MFE India, and in view of the arrangements under the said agreement; MFE India constitutes its dependent agent permanent establishment in India. These facts are also well captured in the assessment order dated 18th December 2019 passed by the Assessing Officer, as follows:

3. The Assessee Company is a Non-resident company incorporated under the laws of Malaysia. The Assessee Company supplies aluminium formwork which finds application in the construction of buildings. The Group has a wholly owned subsidiary in India in the name and style of MFE Formwork Technology India P Ltd ('MFE-India') having its registered office at Mumbai, Andheri. The assessee is a tax resident of Malaysia in terms of Article 4 of the Double Taxation Avoidance Agreement ('DTAA') entered into between India and Malaysia. The Assessee Company had executed a Marketing Service Agreement ('MSA') with MFE-India. As per the MSA, MFE-India is required to (1) Promote and market the products of the Assessee Company within India and (2) Educate the prospective customers about the benefits of the products offered by the Assessee Company. Further, as per technical support service agreement between MFE-Malaysia and MFE-India, the latter is required to provide support in terms of the formwork supplied by MFE Malaysia to its customers in India; such support being in the nature of supervisory support that would be required by the customer as regards the formwork supplied. The said company qualifies as a dependent agent of the assessee in terms of Para 5 of Article 5 of the DTAA between India and Malaysia. Thus, for the year under consideration, the assessee had a Permanent Establishment ('PE') in India in

terms of Article 5 of the DTAA between India and Malaysia. The assessee has filed the Return of Income for such PE.

3. The assessee has computed its profits, under the 'Dual Taxpayer Approach' or the 'Authorised OECD Approach (AOA)'- as it is technically termed, in the paragraph 4 and 5 of the assessment order, as follows:

4. During the course of assessment the AR was asked to submit the Computation of Income for the Return of Income filed by the assessee for the year under consideration. It was seen from the Computation of Income filed by the AR that the assessee has computed profit attributable to the activity of PE in India from the sales made in India. From the Computation of Income filed by the Assessee, it is seen that for the purpose of determining the profits attributable to tax in India, the Assessee Company had attributed 24% of Gross Profits based on FAR Analysis carried out. The AR explained the basis of Computation as under:

Step	Particulars	Basis	Amt (Rs)
1.	Sales made in India	Sales made to customers in India during the relevant financial year.	1,691,493,506
2.	Less: Cost of Sales	In ratio of overall cost of sales incurred by the Assessee Company for global operations, based on the Global Financial	1,305,157,104

		Statements of the Assessee Company.	
3.	Gross Profits from Sales made in India	Sales as reduced by proportionate cost of sales (Sr 1 - Sr 2)	386,336,402
4.	Profits attributable to Indian Operations	24% of Gross Profits. The rate of 24% has been determined on the basis of a detailed FAR analysis based on Function Performed, Asset Deployed & Risks Assumed by each party.	9,27,20,736
5.	Less: Marketing Fee paid to agent (MFE Formwork Technology India P Ltd) in India	As per the Marketing Service Agreement, the Assessee Company has paid a Marketing Fee to its agent in India (MFE Formwork Technology India P Ltd) being the cost incurred for performing its duties under the agreement along with a mark-up of 15%	9,05,21,260
6.	Taxable Profits	Profit Attributable to Indian Operations as reduced by Marketing Fee paid to agent in India (Sr 4-Sr 5)	21,99,476

5. From the Computation of Income filed by the assessee it is seen that for the purpose of determining profits attributable to tax in India, the assessee Company has attributed 24% of Gross Profits based on FAR Analysis carried out. On going through the FAR analysis it seen that the Assessee has broken up each activity into

several sub-activities and allotted weights to each sub-activity and then determined what is the weightage attributable to activity of the Permanent Establishment in India. The ratio of 24% adopted by the assessee for the purpose of determining profits attributable to tax in India is in consonance with the ratio adopted by my predecessors in the earlier years. In light of the above discussion and based on the facts of the case of the Assessee, the gross profits attributable to the activity of Marketing carried out by the PE in India are computed at 24% of the Total Gross Profits from sales made in India.

4. The Assessing Officer accepted the computation of profits attributable to the dependent agent permanent establishment, and, accordingly, proceeded to finalize the assessment. The matter, however, did not rest there. The assessment so finalized was subjected to revision proceedings mainly on the ground that "no enquiry has been conducted with regard to how attribution of 24 percent gross profit was arrived at" and that "the Assessing Officer has simply accepted the Function Asset Risk Analysis [FAR analysis] submitted by the assessee company disregarding several other factors, which demonstrate lower than Arm's Length Profit are attributed to Indian operations". The learned Commissioner then proceeded to reject the FAR analysis on the basis of which PE profits were computed, and proceeded to compute, under rule 10 of the Income Tax Rules,

1962, and with the guidance of Hon'ble Delhi High Court judgment in the case of Rolls Royce PLC Vs DIT [(2011) 339 ITR 147 (Del)], as to what will be the correct attribution of profits attributable to the DAPE in question. It was worked out at 35%, as exactly was the profit rate in Rolls Royce (supra) and that is what, according to the learned Commissioner, was supported by the DAPE's FAR analysis as well. The learned Commissioner observed that based on this decision, and the revised FAR analysis, the profit attribution comes to 35%. The matter was remitted to the file of the Assessing Officer for passing consequential order to give effect to the findings of the learned Commissioner. The assessee is aggrieved and is in appeal before us.

5. When this appeal came up for hearing, it was noticed that admittedly the form of permanent establishment is a dependent agent permanent establishment (DAPE), and there also does not seem to be any controversy about the position that the assessee has paid an arm's length remuneration for the services rendered by the agent constituting the DAPE, i.e. MFE-India, as there is no ALP adjustment in respect of the payment made by the assessee to the MFE. Yet, there is a dispute about the FAR analysis, but that is because the assessee has proceeded on the dual taxpayer approach, recognizing the distinction between the dependent agent and the dependent agency permanent establishment. While a similar approach was approved and adopted by a coordinate bench in the

case of DDIT Vs Set Satellite Pte Ltd [(2007) 106 ITD 175 (Mum)], wherein, speaking through one of us, the coordinate bench upheld the dual taxpayer approach, but then the said decision did not find favour with the Hon'ble High jurisdictional Court which has reversed the said decision of the coordinate bench. We are thus alive to the fact that in the light of Hon'ble jurisdictional High Court judgment in the case of Set Satellite Singapore Pte Ltd Vs DCIT [(2008) 307 ITR 205 (Bom)], so far as profit attribution of a DAPE is concerned, the prevailing legal position is that as long as an agent is paid an arm's length remuneration for the services rendered, nothing survives for taxation in the hands of the dependent agency permanent establishment. Viewed thus, the existence of a dependent agency permanent establishment is wholly tax neutral, and there are a large number of decisions of the coordinate benches, following Hon'ble jurisdictional High Court's judgment in the case of Set Satellite (supra), holding so. The question that we put to the parties was whether an order can be said to be prejudicial to the interest of the revenue even when the income is determined on the basis of the correct legal position of the single taxpayer approach, which has the approval of the Hon'ble jurisdictional High Court as also a series of subsequent decisions of the coordinate benches, is less than the income determined by the Assessing Officer in the order being subjected to the revision proceedings. When the above proposition was so put to the parties, learned counsel for the assessee submitted that when the very existence of DAPE, in

the light of the above legal position, is tax neutral, the attribution of profits in the dual taxpayer approach and the FAR analysis for that purpose is wholly academic, from the point of view of the revision proceedings, inasmuch as the profit computation under the dual taxpayer approach cannot be said to be prejudicial to the interest of the revenue when tax liability computed, in accordance with the law laid down by the Hon'ble jurisdictional High Court, is NIL. It is pointed out that there is no ALP adjustment in the arm's length price of the services rendered by the Indian dependent agent i.e. MFI-India, nor is it the case of the Commissioner that such an ALP adjustment was warranted on these facts. Learned counsel submits that for this short reason alone, the impugned revision proceedings must be quashed. Without prejudice to this line of argument, he, however, seeks to argue the matter on merits as well. Learned Departmental Representative, however, points out that once an assessee opts for the computation of profits on a certain basis, the Commissioner was fully justified in revising the assessment order in question to correct the obvious and glaring errors in the FAR analysis necessary for computation of profits on that basis. Learned Departmental Representative relies upon the stand of the authorities below, but he does not, however, dispute that the permanent establishment of the assessee is indeed a dependent agency permanent establishment.

6. We have heard the rival contentions, perused the material on record and duly considered the facts of the case and in the light of the applicable legal position.

7. We find that section 263 of the Income Tax Act, 1961 provides that "The Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner may call for and examine the record of any proceeding under this Act, and if he considers that any order passed therein by the Assessing Officer is erroneous in so far as it is prejudicial to the interests of the revenue, he may, after giving the assessee an opportunity of being heard and after making or causing to be made such inquiry as he deems necessary, pass such order thereon as the circumstances of the case justify, including an order enhancing or modifying the assessment, or cancelling the assessment and directing a fresh assessment" (Emphasis, by underlining, supplied by us). It is, therefore, a condition precedent for invoking the revisionary powers under section 263 that in order to invoke the revision powers of the Commissioner, the order sought to be revised must be "erroneous in so far as it is prejudicial to the interests of the revenue". In other words, even if an order is erroneous but is not prejudicial to the interest of the revenue, the provisions of Section 263(1) cannot be put into service. In the case of Malabar Industrial Co Ltd Vs CIT [(2000) 243 ITR 83 (SC)], the Hon'ble Supreme Court has elaborated upon this point and observed that "A bare reading of this provision makes it clear

that the pre-requisite to exercise of jurisdiction by the Commissioner suo motu under it, is that the order of the ITO is erroneous insofar as it is prejudicial to the interests of the revenue. The Commissioner has to be satisfied with twin conditions, namely, (i) the order of the Assessing Officer sought to be revised is erroneous; and (ii) it is prejudicial to the interests of the revenue. If one of them is absent - if the order of the ITO is erroneous but is not prejudicial to the revenue or if it is not erroneous but is prejudicial to the revenue - recourse cannot be had to section 263(1)". In the light of this legal position about the scope of revisionary powers of the Commissioner, the question that we need to put to ourselves is whether the taxability of an arm's length remuneration to the dependent agent, in the hands of the dependent agent, exhausts the tax liability of the dependent agent permanent establishment, because if it does, non-levy of tax on the hypothetical profits of the DAPE, independent of the taxability of profits of the dependent agent, cannot be said to be prejudicial to the interests of the revenue. In view of Hon'ble jurisdictional High Court's judgment in the case of Set Satellite (supra), the answer is in affirmative. That is the view the coordinate benches of the Tribunal are taking, such as in the case of ADIT Vs Asia Today Ltd [(2021) 129 taxmann.com 35 (Mum)]. Clearly, therefore, the non-levy of short levy of taxes on the hypothetical profits of the DAPE, independent of the taxability of the dependent agent, cannot be said to be prejudicial to the interest of the revenueas long as the dependent agent has been paid an arm's length

remuneration for the services performed. In the present case, it is not even the case of the Assessing Officer at any stage that the dependent agent has not been paid arm's length remuneration, even though there is repeated reference to the FAR analysis of the DAPE. Learned Commissioner has made reference to the Rolls Royce decision (supra) in this context of profit attribution to the PE, but then this is a decision in the context of a fixed place PE as evident from question number 2 before Hon'ble Delhi High Court, i.e. whether the office of Rolls Royce India Limited at New Delhi constituted a permanent establishment of the assessee under Article 5 of the Double Taxation Avoidance Agreement between India and the United Kingdom. The profit attribution to the DAPE and fixed place PE are, in the light of Hon'ble jurisdictional High Court judgment in the case of the Set Satellite (supra), on a materially different basis. On a conceptual note, PE, whether a fixed base PE, DAPE or any other type of PE, provides for threshold limits to trigger taxation in the source state, but then if as a result of a DAPE, no additional profits, other than agent's remuneration in the source country - which is taxable in the source state anyway dehors the existence of PE, become taxable in the source state, the very approach to the DAPE profit attribution may indeed seem clearly incongruous, but then as is the settled legal position as long as the dependent agent has been remunerated, on an arm's length basis, for the functions performed, assets employed and risks assumed, that is the end of taxability of profits so far as the profits attributable to the DAPE are concerned.

As a matter of fact, the very reference to the Rolls Royce decision (supra) shows that the aspect of the distinction between profit attribution to a fixed place PE and a DAPE has been lost sight of. While the learned Commissioner has disputed the FAR analysis, there is clearly mix-up of the FAR analysis of the agent with the FAR analysis of the DAPE. Learned Commissioner, in the impugned order, has proceeded on the basis that the profit attribution of a fixed place PE and the DAPE are in pari materia- a proposition which has been specifically rejected in the binding judicial precedents discussed above. We may, in this regard, refer to the following observations of Hon'ble jurisdictional High Court in the Set Satellite decision (supra):

> *…….At this stage we may note that on behalf of the assessee learned Counsel has produced an order passed by the Additional CIT (Transfer Pricing-II), Mumbai in the matter of determination of arm's length price with reference to all the transactions reported in Form No. 3CEB filed by the assessee. The assessee is SET India, the depending agent. The order records that the assessee is engaged in the business of providing audio-visual television content and also acts as an advertising agent of Set Satellite Singapore Pvt. Ltd. The assessee distributes these channels to the Indian cable operators and that the assessee has applied the TNM method to determine the arm's length price for its*

international transaction. It, however, clarified that the order is in respect of reference received for the assessment year 2002-03 and not for subsequent assessment years.

12. We may now consider the judgment in Morgan Stanley & Co. Inc's case (supra). The Appeals dealt with the Double Tax Avoidance Agreement (DTAA) between India and United States. That treaty advocated application of the arm's length principle or provided a mechanism for avoiding double taxation on income. The issue involved, Morgan Stanley and Company (for short, "MSCo.") and one of the group companies of Morgan Stanley, Morgan Stanley Advantages Services Pvt. Ltd. (for short "MSAS"). An agreement was entered into for providing certain support services to MSCo. MSCo. outsourced some of its activities to MSAS. MSAS was set up to support the main office functions in equity and fixed income research, account reconciliation and providing IT enabled services such as back office operations, data processing and support centre to MSCo. On 5-5-2005 MSCo. filed its advance ruling application . The basic question related to the transaction between the MSCo and MSAS. The advance ruling was sought on two counts (i) whether the applicant was having PE in India under Article 5(1) of the DTAA on account of the services rendered by MSAS under the services agreement dated 14-4-2005 and if so

(ii) the amount of income attributable to such PE. It was ruled that MSAS should be regarded as constituting a service PE under Article 5(2)(1). On the second question the AAR ruled that the transactional net margin method (TNMM) was the most appropriate method for the determination of the Arm's Length Price (ALP) in respect of the service agreement dated 14-4- 2005 and it meets the test of arm's length as prescribed under section 92C of the 1961 Act and no further income was attributable in the hands of MSAS in India. The said ruling of AAR on the question of income attributable to the PE was the subject-matter of challenge by the Department. Insofar as the issue of PE is concerned the Supreme Court was pleased to hold that it agreed with the Ruling of the AAR that stewardship activities would fall under Article 5(2)(1). Dealing with the question of deputation, the Court held that on the facts that there is a service PE under Article 5(2)(1) and as such held that the Department was right in its contention that there exists a PE in India. Considering Article 7 of that treaty the Court observed that what is to be taxed under Article 7 is income of the MNE attributable to the PE in India and what is taxable under Article 7 is profits earned by the MNE. Under the Income-tax Act the taxable unit is the foreign company, though the quantum of income taxable is income attributable to the PE of the said foreign company in India. The Court observed that the

important question which arises for determination is whether the AAR is right in its ruling when it says that once the transfer pricing analysis is undertaken there is no further need to attribute profits to a PE. The Court further noted that the computation of income arising from international transactions has to be done keeping in mind the principle of arm's length price. The Court further reiterated that the main point for determination is whether the AAR was right in ruling that as long as MSAS was remunerated for its services at arm's length, there should be no additional profits attributable to the applicant or to MSAS in India. After considering the various methods by which arm's length price can be determined the Court observed as under:—

> *"As regards determination of profits attributable to a PE in India (MSAS) is concerned on the basis of arm's length principle we have quoted Article 7(2) of the DTAA. According to the AAR where there is an international transaction under which a nonresident compensates a PE at arm's length price, no further profits would be attributable in India. In this connection, the AAR has relied upon Circular No. 23 of 1969 issued by the Central Board of Direct Taxes. This is the key question which arises for determination in these civil appeals."*

After discussing the various issues the Court in its conclusion held as under:—

> *"As regards attribution of further profits to the PE of MSCo. where the transaction between the two are held to be at arm's length, we hold that the ruling is correct in principle provided that an associated enterprise (that also constitutes a PE) is remunerated on arm's length basis taking into account all the risk-taking functions of the multinational enterprise. In such a case nothing further would be left to attribute to the PE. The situation would be different if the transfer of pricing analysis does not adequately reflect the functions performed and the risks assumed by the enterprise. In such a case, there would be need to attribute profits to the PE for those functions/risks that have not been considered. The entire exercise ultimately is to ascertain whether the service charges payable or paid to the service provider (MSAS in this case) fully represent the value of the profit attributable to his service. In this connection, the Department has also to examine whether the PE has obtained services from the multinational enterprise at lower than the arm's length cost."*

In our opinion, considering the judgment, if the correct arm's length price is applied and paid then nothing further would be left to be taxed in the hands of the Foreign Enterprise.

8. In the present case, there does not appear to be any dispute with respect to the ascertainment of the arm's length price of the services rendered by the dependent agent to the assessee, as no ALP adjustment is made in the remuneration paid by the assessee to the MFE India, i.e. the dependent agent. There are also several indications to suggest that DA and DAPE are being treated as distinct taxpayers, inasmuch as while the arm's length payment to the agent is not being questioned, the FAR analysis for the PE has been called into question. The two taxpayer approach adopted by the assessee has been accepted, and, taking it further, the profit attribution on the basis of the two taxpayer approach is enhanced. Even if that computation of profit attribution, on the basis of the two taxpayer approach, is erroneous, in view of Hon'ble jurisdictional High Court decision, it cannot be said to be prejudicial to the interest of the revenue unless there is a categorical finding that the payment to the dependent agent is not an arm's length price vis-à-vis functions performed, assets employed and risks assumed by the dependent agent. While doing so, one also has to bear in mind that DAPE is not anything distinct from the DA, in the light of the binding judicial precedents holding the field as of now, and the taxability of the dependent agent's

remuneration in the hands of the DA brings an end to the taxability of the DAPE also. There is no such finding about the payment to the dependent agent being less than the arm's length price of services rendered by the dependent agent, in the present case, even though there is a finding about questioning the DAPE's FAR analysis. The Commissioner ought to have examined the arm's length price determination in respect of the services rendered by the dependent agent, in this context. That exercise has also not been done.

9. In view of the above discussions, as also bearing in the entirety of the matter, we are of the considered view that unless the order sought to be revised cannot be said to be prejudicial to the interest of the revenue, its being erroneous, even if that be so, cannot be said to reason enough to invoke section 263 of the Act, and the order cannot be said to be prejudicial to the interests of the revenue unless there is a categorical finding that the dependent agent has not been paid arm's length remuneration for the functions performed, assets employed and risks assumed by the dependent agent. The order being prejudicial to the interest of the revenue, inasmuch as the payment to the dependent agent not being at an arm's length, is a sine qua non for holding that the order is prejudicial to the interest of the revenue. This exercise has clearly not been done on the facts of this case. For this short reason alone, we must set aside the impugned revision order.

10. As we part with the matter, we may add that once the assessee has accepted the dual taxpayer approach in its computation of income, it cannot be open to the assessee to deny the tax liability that it has already accepted under the said computation. We may, in this regard, refer to a materially similar situation dealt with by the Hon'ble Supreme Court in the case of Carborundum Co Vs CIT [(1977) 108 ITR 335 (SC)], wherein, even while Their Lordships held that the assessee had no tax withholding obligation in respect of technical know-how paid by the assessee, and, as such, revision order under section 263, holding the assessee liable to tax withholding treating 75% of such technical know-how is taxable in India, is unsustainable in law, Their Lordships also made clear that the 5% tax withholding liability accepted by the assessee cannot be negated as a result of the revision order being quashed. The same will be the position here. The impugned revision order being quashed would not affect the tax liability accepted by the assessee, under dual taxpayer approach, in the original assessment proceedings. As a matter of such adjustments being made in the course of normal assessment proceedings would have been, on jurisdictional point, perhaps in order, and the question, in that case, would have remained confined to the merits and the quantum of the adjustments. That, however, is not the situation before us. Learned counsel has also pointed out that there is a glaring error in the computation of profits inasmuch as the Commissioner has computed 35% of the gross figures of profit, whereas the computation of profit allocable

to the permanent establishment can at best be for 35% of net profits. That aspect of the matter, as of now, is purely academic, and we leave it at that. Similarly, we see no need to deal with the other aspects of the matter raised by the assessee-appellant. All those issues are academic as of now.

11. In the result, the appeal is allowed. Pronounced in the open court today on the 30th day of August 2022."

013. We find that the order of the Co-ordinate Bench squarely covered the issue before us. Therefore, respectfully following the decision of the co-ordinate Bench, we also set aside the impugned order passed by the learned PCIT under Section 263 of the Act for A.Y. 2018-19 and 2019-20. Accordingly, both the appeals filed by the assessee are allowed.

014. In the result, both the appeals of the assessee are allowed.

Order pronounced in the open court on 24.01.2023.

Sd/-	Sd/-
(SANDEEP SINGH KARHAIL)	(PRASHANT MAHARISHI)
(JUDICIAL MEMBER)	(ACCOUNTANT MEMBER)

Mumbai, Dated: 24.01.2023
Sudip Sarkar, Sr.PS
Copy of the Order forwarded to:

1. The Appellant
2. The Respondent.
3. The CIT(A)
4. CIT

5. DR, ITAT, Mumbai
6. Guard file.

BY ORDER,

True Copy//

Sr. Private Secretary/ Asst. Registrar
Income Tax Appellate Tribunal, Mumbai