IN THE INCOME TAX APPELLATE TRIBUNAL, 'K' BENCH MUMBAI

BEFORE: SHRI AMIT SHUKLA, JUDICIAL MEMBER
&
SHRI GAGAN GOYAL, ACCOUNTANT MEMBER

ITA No.6263/Mum/2014
(**Assessment Year :2004-05**)

M/s. CLSA India Private Limited (Formerly CLSA India Limited) 8/F, Dalamal House Nariman Point Mumbai – 400 021	Vs.	Deputy Commissioner of Income Tax, Range-4(1), 6th Floor, Room No.640/678, Aayakar Bhavan, M.K.Road Mumbai – 400 020
PAN/GIR No.AAACC2262K		
(Appellant)	..	**(Respondent)**

Assessee by	Shri Mukesh Butani a/w. Shri Harsh Shah
Revenue by	Ms. Samruddhi Hande a/w. Shri Akhtar Hussain Ansari
Date of Hearing	**25/01/2023**
Date of Pronouncement	**21/04/2023**

आदेश / O R D E R

PER AMIT SHUKLA (J.M):

The aforesaid appeal has been filed by the assessee against the order dated 24/03/2014 passed by ld. CIT(A)-10, Mumbai for the quantum of assessment passed u/s.143(3) for the A.Y.2004-05.

2. In various grounds of appeal, the assessee has mainly challenged following three additions / adjustments:-

(i)	Payment of royalty / branding fees	- Rs. 1,30,22,846/-
(ii)	Payment of referral fees	-Rs. 7,73,58,162/-
(iii)	Reimbursement of indirect Overhead expenses	- Rs. 4,22,23,050/-
	Total	**Rs.13,26,04,058/-**

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3. The facts in brief are that the assessee company operates in financial services industry and capital markets. The principal business activities of the assessee include equity research, equity brokerage and advisory services. The assessee is a member of the National Stock Exchange of India Limited and the Bombay Stock Exchange and works primarily as institutional brokerage services. For benchmarking the international transaction relating to; i) payment and royalty branding fees; ii) the payment of referral fees; and iii) reimbursement of indirect overhead expenses, assessee has applied TNMM as Most Appropriate Method, whereby assessee had shown its operating profit margin of 66.21% as against average of 6.43% of the comparable companies. In so far as the payment of royalty / branding fees are concerned, this issue has been raised vide ground Nos.3-9 and at the outset, it has been stated that same is squarely covered by the decision of the Tribunal in assessee's own case for A.Y.2002-03 and 2003-04.

4. Assessee has paid royalty and branding fees of Rs.1,30,22,846/- calculating @1% of gross receipts for the use of

brand 'CLSA' as per the terms of branding agreement entered into with its AE CLSA BV Netherlands w.e.f.19/02/2002. The ld. TPO has determined ALP at 'Nil' holding that for any such transactions, no brand fee is paid by any independent enterprise and assessee has used TNMM method for computing the arm's length price of the international transaction by comparing the net profit margin of the company at entity level with that of the other permanent entities and the payment of 'brand fee' has not been separately and independently benchmarked, which assessee was supposed to be benchmarked separately. We find that this issue has been dealt by the Tribunal in A.Y.2002-03 in ITA No.2362/Mum/2011, wherein the Tribunal has observed and held as under:-

"8. We have perused the records and considered the rival contentions carefully. The dispute raised in this ground is regarding transfer pricing adjustment made by AO in respect of royalty paid by the assessee to CLSA BV of which the assessee is a subsidiary. The royalty amounting to Rs.7,11,466/- @ 1% of net receipt has been paid by the assessee during the year from 19.2.2002 to 31.2.2002. The assessee had not paid any royalty earlier as the same was not permitted by the erstwhile Foreign Exchange Regulation Act (FERA). However, later when FERA was replaced by FEMA, government allowed payment of royalty and therefore assessee started making payment of royalty to the parent company which is incorporated in Netherlands, after taking approval from RBI. Since the assessee had entered into an international transaction with an associate enterprise, the matter was referred to TPO who has made transfer pricing adjustment using CUP method. The TPO noted that no other subsidiary of CLSA BV anywhere in the world had paid any royalty. Therefore, he had treated this as internal CUP of royalty

payment. Further, since the AY .02-03 assessee could not give any information regarding similar payment of royalty by any broking company, the TPO treated the same as external CUP of no payment of royalty. Accordingly, he has considered the entire payment as excessive and made adjustment on this account which was followed by the AO.

8.1 In our view the approach adopted by TPO/AO is not correct. International transaction in case of the assessee has to be compared with uncontrolled transactions. There can be an internal CUP provided, the transaction is with an unrelated party. But comparing the transaction in case of the assessee with transactions of CLSA BV with another associate enterprise cannot be considered as internal CUP. Moreover, lack of transaction cannot be considered as a transaction. Regarding external CUP also, TPO has not placed any material on record to show that no payment of royalty has been made by any independent party for using brand name/trade name. Non availability of a comparable transaction can not be considered as transaction and cannot be the basis of selection of comparable transaction. Further, CUP method can not be applied if the relevant information is not available. This view is also supported by the decision of Mumbai Bench of the Tribunal in Cabot India Ltd. vs. DCIT on which the ld. Sr. Counsel has placed reliance. We, therefore agree with the finding of CIT(A) that CUP method on the facts of the case could not be applied. We are unable to accede to the request of the ld. CIT-DR, the AY .02-03 matter may be restored to AO/TPO to find out a comparable transaction for application of CUP method. No such comparable transaction has been brought on record even by AO or by DRP, though the assessee had clearly stated that no such information was available. No such comparable case has been placed by the ld. CIT-DR even before us. The issue, therefore, cannot be restored for making roving inquiries.

8.2 The ld. CIT-DR has placed reliance on the decision of the Tribunal in the case of M/s. Knorr Bremse (I) Pvt. Ltd. (supra), has argued that in case the assessee does not show that transaction by transaction approach was not possible and there has been no real or tangible benefit for carrying on international transactions with the AEs. CUP method can be adopted with preference to TNMM. It has been pointed out that in that case it was also held that TPO was justified in taking ALP at nil. We have perused the said judgment. There cannot be any dispute about applicability of CUP method when transaction by transaction approach was possible but the method can be applied only when information is available for application of CUP method. In the cited case, the Tribunal had upheld the order of TPO determining ALP at nil on the basis of CUP method as in that case there was material to show that no real or tangible benefit had been derived by the assessee from the transaction with the AEs and benefit if any was only incidental. The present case is different. In this case, though the AO observed that the trade name/brand name CLSA was AY .02-03 not protected in any country including India and the assessee could not give any document to prove ownership of the brand by CLSA BV, CIT(A) on detailed examination of the matter has given a finding that the CLSA brand was owned by CLSA BV and the same was also registered in India. CIT(A) has also given a finding that CLSA strongly strived to maintain as well as enhance its brand value which had earned recognition in India and Asian markets. There is no material produced before us to controvert the said finding. In the broking business, brand does promote the business and as rightly observed by CIT(A) it is one of the profit drivers within the industry. Thus it cannot be said that the assessee had not derived any benefit from use of brand. The decision of the Tribunal relied upon by the ld. CIT-DR, therefore, cannot be applied to the facts of the present case. 8.3 We also find that the AO without any detailed examination as to why other CLSA entities were not making any payment of royalty, rushed to apply the CUP method which as we have held could not be applied for the lack of proper information. CIT(A) has examined the matter

in detail as to why other CLSS entities were not paying royalty which was because of the fact that CLSA had different arrangement in different jurisdictions. CLSA was present in 13 markets out of which India, Korea and Taiwan had capital market regulation which required FIIs to contract directly with a domestic CLSA entity. In other jurisdictions, a single contract model was followed as per which client in particular country willing to buy AY .02-03 securities in other countries has to place order in CLSA entity in the home country which shares commission with CLSA unit of the other country. In Korea, there was commission sharing arrangement whereas CLSA Taiwan operated as a branch which books the commission and it is charged an allocation of certain head office expenses. In India there was no commission sharing arrangement and payment of royalty was therefore permitted. CIT(A) on examination of the arrangement/system followed by CLSA BV has also given a finding that in other jurisdictions, CLSA entities were making market contributions. Therefore only on the ground that other CLSA units did not pay any royalty, it could not be held that payment of royalty by the assessee was not justified. 8.4 CIT(A) has also examined the business development system followed by other comparable companies in India and has given a finding that these companies on average were incurring business development expenditure which was 6.4% of brokerage turnover whereas similar expenditure incurred by the assessee was only 1.28% including royalty of 1% paid by the assessee . Therefore expenditure incurred by the assessee on royalty and business development could not be considered as excessive compared to the comparable parties. CIT(A) has also applied the TNMM method for benchmarking international transactions. There are 29 comparables selected details of which have already been given earlier which gave an average margin of -5.5% and, in case, loss making AY .02-03 companies were excluded, the average margin came to 16.06% whereas in case of the assessee the margin declared was 57.58%. CIT(A) has therefore held that no TP adjustment is required to be made in case of the assessee with which, on the facts of case, we fully agree. We, therefore, see no

infirmity in the order of CIT(A) in deleting the addition made and the same is therefore, upheld."

5. Thus apart from that, similar observation and finding has been given in A.Y.2003-04. Thus, consistent with view taken in the earlier years, the royalty payment of 1% is accepted and adjustment made by the ld. TPO is deleted.

6. Coming to the issue of payment of referral fees as raised vide ground Nos.10-17, the brief facts are that assessee has entered into referral agreement dated 07/02/2003 with its AE CLSA Ltd Hongkong, pursuant to which assessee paid referral fees equivalent to 30% of the brokerage fees earned by it from the clients referred by the AE. During the year assessee has paid Rs.7,73,58,162/-.

7. Similarly, with regard to issue of reimbursement of indirect overhead expenses as raised vide ground Nos.18-23; assessee had entered into Indirect Overhead Reimbursement Agreement with CLSA Ltd Hongkong w.e.f. 1st April, 2003. The assessee has contributed towards its portion of overhead expenses incurred by CLSA group for the purpose of specified functions attributable to the operations in India. It has been stated that CLSA group is engaged India sales Specialists who were based in New York, London and Singapore and cater exclusively for generating great flow to the Indian market. The India Sales Specialists are responsible for interacting with the clients on day to day basis to sell CLSA India services and research products to the clients. Accordingly, assessee had reimbursed Rs.42,223,050/- towards

cost and in respect of India sales specialists. To justify the ALP of the payment, assessee has submitted independent 'Agreed upon Procedures Report' issued by PLIC certified public Accountants, Hongkong which provides nature of expenses and the computation of indirect overhead expenses attributable to the assessee. Pursuant to this, the indirect overhead expenses attributable to the assessee from CLSA Hongkong books of account were extracted and the total amount of each indirect overhead expenses reimbursed by the assessee was validated by independent experts. The assessee has benchmarked both the above transactions i.e. payment of referral fees and reimbursement of indirect overhead expenses by using TNMM as the Most Appropriate Method and concluded that they are at ALP. The assessee has justified that sale efforts, research activities and IT infrastructure are the main functions responsible for earning of brokerage income from clients. Accordingly, payment of referral fees and indirect overhead expenses reimbursement is closely inter linked to the assessee's business and therefore, was benchmarked using TNMM by considering assessee as a tested party.

8. However, the ld. TPO has determined the ALP of this transaction at Nil and entire payment of referral fees and indirect overhead reimbursement was adjusted holding that assessee could not prove or establish from the transfer pricing angled that it acted as an independent enterprise functioning in an uncontrolled environment while agreeing to pay the referral fees

to CLSA Hongkong for services which it had hitherto received free of charge.

9. The ld. CIT (A) has simply confirmed the action of the ld. TPO that assigning any reasons and considering the submissions made by the assessee in support of rendition of services.

10. Before us, the ld. Counsel submitted that in so far as payment of referral fees is concerned, the same issue is covered in favour of the assessee by the decision of this Tribunal in assessee's own case for A.Y.2003-04. The relevant observation and finding of the Tribunal after considering the catena of evidences which has been discussed in detail in para 16, the Tribunal has given following finding of fact and the reasons for deletion of said addition:-

"17. We find that the aforesaid documents filed by the assessee as "additional evidence" U/rule 46A were in all fairness admitted by the CIT(A). In our considered view, the assessee by drawing support from the voluminous documentary evidence that was filed before the CIT(A) as 'additional evidence' U/rule 46A had therein substantiated the factum of receipt of referral services from its AE, viz. CLSA Ltd., Hong Kong, along with the tangible benefits derived therefrom. Although the aforesaid documents were filed by the assessee as "additional evidence" in two parts before the CIT(A), however, we are of a strong conviction that the same clearly dispels the doubts raised by the A.O/TPO as regards the rendition of the referral services by the AE, viz. CLSA Ltd., Hong Kong to the assessee during the year under consideration. As is discemible from the records, we find, that the TPO on being confronted with the aforesaid "additional evidence", had however, in neither of his three remand reports been able to place on record any such material which would

dislodge the factum of rendition of referral services by the AE, viz CLSA Ltd., Hong to the assessee during the year under consideration and therein prove to the contrary that no such referral services were therein factually rendered. Except for claiming that the documents filed by the assessee did not demonstrate that any actual referrals were made by the AE, viz. CLSA Ltd., Hong Kong, to the assessee, we find, that the said hollow claim of the TPO is not backed by any concrete material which would support the same. On the basis of the aforesaid observations, we are unable to concur with the view taken by the lower authorities that the assessee had failed to substantiate receipt of referral services from its the AE, viz. CLSA Ltd., Hong Kong during the year under consideration on the basis of any supporting documentary evidence."

11. Thus, following the earlier year judicial precedence, we hold that the ld. TPO cannot benchmark the 'referral fee' at Nil and accordingly, adjustment made by the ld. TPO is deleted on similar reasoning. Accordingly, grounds Nos.10-17 are allowed.

12. In so far as Indirect overhead expenditure, again this issue is covered by the assessee's own case for A.Y.2003-04, wherein it has been held that ad-hoc TP addition without following any one of the prescribed method is not sustainable which has been discussed in detail in para 19 of the ITAT order cited supra. Apart from that, we find that the assessee has benchmarked the transaction using TNMM, which is one of the prescribed methods as per Section 92C. Further, the assessee has also provided a supplementary and detailed analysis by way of the AUP report which certifies that only costs attributable to the assessee have

been reimbursed to the AE. The exact language of the AUP report is as under:-

> *"The total indirect overhead expense reimbursement relates to the cost of specialist India sales staff employed by affiliates of CLSA Limited in Singapore, New York and London and engaged (pursuant to agreements between CLSA Limited and the relevant affiliates) to provide services for the benefit of CLSA India. These include staff expenses office premises cost, travel and entertainment, telecommunications, research expenses, professional fee, depreciation, market data services, IT services, courier, postage and stationery, clearing and stock exchange fee, other expenditure and other allocated cost from other CLSA offices (the "relevant indirect overhead expenses")."*

13. Against the scientific approach adopted by the assessee, the ld. TPO has merely resorted to ad-hoc approach and without following any one of the prescribed methods determined ALP of reimbursement of indirect expense overheads as Nil. Thus, the addition of this adjustment made on account of reimbursement of indirect overhead expense is also directed to be deleted.

14. In the result, appeal of the assessee is allowed.

Order pronounced on 21st April, 2023

Sd/-	**Sd/-**
(GAGAN GOYAL)	**(AMIT SHUKLA)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Mumbai; Dated 21/04/2023

KARUNA, *sr.ps*

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent.
3. CIT
4. DR, ITAT, Mumbai
5. Guard file.

//True Copy//

BY ORDER,

(Asstt. Registrar)
ITAT, Mumbai