IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "K", MUMBAI
BEFORE SHRI AMIT SHUKLA (JUDICIAL MEMBER)
AND
Ms. PADMAVATHY S. (ACCOUNTANT MEMBER)

I.T.A. No.3384/Mum/2014 - Assessment year: 2008-09
I.T.A. No.3385/Mum/2014 - Assessment year: 2009-10
I.T.A. No.3642/Mum/2016 - Assessment year: 2010-11
I.T.A. No.4562/Mum/2017 - Assessment year: 2011-12

Kansai Nerolac Paints Limited (Erstwhile known as Goodlas Nerolac Paints Limited), Nerolac House, G.K. Marg, Lower Power, Mumbai-400 013 **PAN : AAACG1376N**	vs	Addl CIT, Range 6(2), Mumbai Room No.669, 5th Floor, Aayakar Bhavan, M.K. Marg, Mumbai-400 020
ASSESSEE		**RESPONDENT**

I.T.A. No.4607/Mum/2017 - Assessment year: 2011-12

Addl CIT, Range 6(2), Mumbai Room No.669, 5th Floor, Aayakar Bhavan, M.K. Marg, Mumbai-400 020	vs	Kansai Nerolac Paints Limited (Erstwhile known as Goodlas Nerolac Paints Limited), Nerolac House, G.K. Marg, Lower Power, Mumbai-400 013 **PAN : AAACG1376N**

ASSESSEE	**RESPONDENT**
Present for the Assessee	Mrs.Aarti Vissanji
Present for the Department	Shri. Rajesh Pardeshi, JCIT

Date of hearing	17/11/2023
Date of pronouncement	04/12/2023

O R D E R

Per Padmavathy S, AM:

These appeal filed by the assessee for AY 2008-09 to AY 2011-12 and by the revenue for AY 2011-12 are against the order of the Commissioner of Income-tax (Appeals)-15, Mumbai [in short, 'the CIT(A)] dated 21/02/2014 for the AY 2008-09, dated 24.02.2014 for AY 2009-10, dated 20.02.2016 for AY 2010-11, dated 29.03.2017 for AY 2011-12. The issues contended are common for all the appeals and hence they were heard together and disposed off through this common order.

2. The common issues contended by the assessee through various grounds are tabulated below –

Issues contended	AY 2008-09	AY 2009-10	AY 2010-11	AY 2011-12
Expenditure on software to be allowed as revenue expense.	Ground No.1	Ground No.1	Ground No.1	Ground No.1
Disallowance under secl.14A read with Rule 8D	Ground No.2	-	Ground No.9	Ground No.8
Addition on account of unutilized MODVAT credit	Ground No.3	-		
Depreciation on UPS			Ground No.2	Ground No.2
Transfer Pricing Adjustment – (a) Notional interest for counter guarantee given to associate concern (b) Notional interest for delayed payment from AEs	Ground No.4	Ground No.2	Ground No.3	Ground No.3
Disallowance of the provision for warranty	Ground No.5	Ground No.3	Ground No.4	Ground No.4
Allowability of amalgamation expenses under sec.35DD	Ground No.6	Ground No.4	Ground No.5	Ground No.5
Disallowance of commission payable to the Managing	Ground No.7	Ground No.5	Ground No.6	Ground No.6

Director under sec.40(a)(ia).				
Disallowance for delayed payment of ESIC under sec.36(1)(va)	Ground No.8	Ground No.6	Ground No.7	Ground No.7
Disallowance for excess depreciation claim on assets eligible for 100% depreciation			Ground No.8	-
Treaty rate to be applied for dividend distributed instead of rate prescribed in sec.115-O	Additional Ground		Additional Ground	Additional Ground

3. The revenue raised the following grounds of appeal –

"1. On the facts and in the circumstances of the case, and in law, the Ld. CIT(A) erred in deleting the adjustment of Rs. 17,57,731/- to the total income of the assessee on account of lower sale price of goods to the assessee's AE."

2. "On the facts and in the circumstances of the case and in law, the Ld. CIT(A) erred in deleting the adjustment of Rs. 17,57,731/- by holding that sales to non-AE in India could not be considered as CUP for sales made to AE outside India even though the products were the same, while approving at the same time the contribution analysis of sales to non-AEs within India with the contribution analysis of sales to the AE outside India by adopting TNMM."

3. "On the facts and in the circumstances of the case and in law, the Ld. CIT(A) has erred in deleting the addition of Rs. 14,51,98,277/- u/s. 145A, on account of cenvat credit to the closing stock"

4. The Appellant prays that the order of the CIT (Appeals) on the above grounds be set aside and that of the AO be restored.

5. The Appellant craves leave to amend or alter any ground or to submit additional new ground, which may be necessary"

<u>I.T.A. No.3384/Mum/2014 - AY 2008-09</u>

4. The assessee is engaged in the business of manufacturing of paints and varnishes. The business consists of manufacturing two kinds of products -

decorative and industrial. The assessee filed its original Return of Income on September 09, 2008 declaring total income at Rs. 1,56,98,68,602/-. The case was selected for scrutiny assessment and accordingly notices u/s. 143(2) dated September 09, 2009 was issued and duly served on the assessee on September 24, 2009. A reference was made to the Transfer Pricing Officer (TPO) in order to determine the Arm's Length Price (ALP) of the international transactions the assessee is having with its Associated Enterprises (AEs). The TPO proposed an adjustment of Rs.1,18,18,886/-. The Assessing officer passed the order dated January 30, 2012 under section 143(3) r.w.s 144C(3) of the Act, wherein besides the TP adjustment the assessing officer made certain disallowances / additions which resulted in the assessed being computed at Rs.164,60,64,178. Aggrieved the assessee preferred an appeal before the CIT(A) who confirmed the additions/disallowances made by the assessing officer. The assessee is in appeal before the Tribunal against the order of CIT(A).

DISALLOWANCE OF SOFTWARE EXPENDITURE BY TREATING THE SAME AS CAPITAL EXPENDITURE – Ground No.1

5. The brief facts of the issue are that during the relevant previous year the assessee had incurred expenditure towards various application software's aggregating to Rs. 35,37,723/-, the break-up of which is tabulated hereunder

Sr.No.	Nature of payment	Amount (Rs.)
1	Software development charges for –MIS Reports	65,000/-
2	Software development charges for E-MIS Reports	59,262/-
3	License fee of software modification of SAP Input and output screens	3,87,463/-
4	Application software for window operating systems	1,26,720/-
5	Licence fee of software for modification of SAP Input and output screens	18,72,000

6	Licence fee for form tracking module for sales tax	7,20,445/-
7	Licence fee for form tracking module for sales tax	2,04,314/-
8	Upgradation of software for GLC Machine (Testing Machine)	1,02,519/-
	TOTAL	**35,37,723/-**

The AO has treated the above expenditure as capital and allowed depreciation of Rs.17,11,188 @ 60% [Para 3, pg.2]. The AO has also observed that the Assessee's representative agreed for this disallowance as per note sheet entry dated 16.09.2011. On appeal, the CIT(A) upheld the disallowance.

6. The Ld.AR of the assessee submitted that in fact the assessee did not agree for the disallowance. The assessee had only accepted that the concerned expenses were incurred for purchase of software. In this regard, the Ld.AR invited our attention to the affidavit file by one Mr. Santosh H Ghadigaonkar, Chief Accountant of the assessee company, who has confirmed the above facts by swearing that – "(a) I submitted the extract of ledger account of application and implementation charges for the period 20-07-08 during the assessment proceeding; (b) Assessing Officer asked me to put tick mark against the items of purchase of software appearing in the said extract of ledger and submitted to her, I submitted the same after putting the tick; (c) the AO in the order sheet wrongly mentioned that I have accepted the ticked item as capital expenditure." The ld AR submitted that the application software was for use in areas relating to financial accounting and taxation and that the expenditure on application software is allowable as revenue expenditure. Reliance in this regard is placed on the decision of the Hon'ble Delhi High Court reported in 346 ITR 341 CIT v Amway India Enterprise. The ld AR further submitted that out of the above total expenses of Rs.35,37,723,

the sum of Rs. 31,18,422 i.e. Sl.no.2,3, & 5 to 7 has been incurred on licences which are periodically renewable and allowable as revenue expense. Reliance is placed on 346 ITR 138, Raychem RPG Ltd. (Bom);[2022] 284 Taxman 475 (Mad) CIT v Danfoss P. Ltd. The ld AR also submitted that a similar expenditure in assessee's own case has been allowed by the coordinate bench of the Tribunal for AY 2007-08.

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

8. We heard the parties and perused the material on record. We notice with regard to treatment of application software the Hon"ble Delhi High Court in the case of CIT v. Amway India Enterprises (2012) 346 ITR 341(Delhi) and CIT v. Asahi India Safety Glass Ltd. (2012) 346 ITR 329 (Del) has held that -

> *"3.5 We have heard the rival submissions and perused the relevant materials on record. In Amway India Enterprises (supra), it has been held that the purchase of software is a revenue expenditure. I.T.A. No.6789/Mum/2013 I.T.A. No.7196/Mum/2013 10 | P a g e In Asahi India Safety Glass Ltd. (supra) it is held that the extent of expenditure cannot be a decisive factor in determining its nature and treatment in books of account not conclusive. The Hon'ble High Court held that the software expenses were not to create new asset or a new source of income but to upgrade the system and thus the software expenditure is revenue expenditure. Facts being identical, we follow the ratio laid down in the above decisions and hold that the expenditure incurred by the assessee towards the purchase of application software is revenue in nature. Thus the 2nd ground of appeal is allowed."*

9. We further notice that the above decision has been followed by the coordinate bench in assessee's own case for AY 2007-08. Therefore respectfully following the above we deleted the disallowance of expenditure incurred by the assessee towards the purchase of application software. Further with regard to

license fee we notice that the Special Bench of the Tribunal in the case of Amway India Enterprises vs Dy.CIT (111 ITD 112) which has been affirmed by the Hon'ble Delhi High Court, where the Hon'ble Special Bench has described the concept of benefit of enduring nature as under:-

> “*"Whether expenditure on computer software gives on enduring benefit to an assessee:*
> *For ascertaining as to whether expenditure on computer software gives an enduring benefit, to an assessee, the duration of time for which the assessee acquires right to use the software becomes relevant. Having regard to the fact that software becomes obsolete with technological innovation and advancement within a short span of time, it can be said that where the life of the computer software is shorter (say less than 2 years), it may be treated as revenue expenditure...... ... . An assessee may own a software outright or be a licensee but the same may operate to confer benefit only in the revenue field and therefore it may have to be regarded as revenue expenditure........ .... If the advantage consists merely in facilitating the assessee's trading operations or enabling the management and conduct of the assessee's business to be carried on more efficiently or more profitably while leaving the fixed capital untouched, the expenditure would be on revenue account, even though the advantage may endure for an indefinite future. In other words, the functional test would become material and if on application of the same it is found that the expenditure operates to confer benefit in the revenue field, then the same would be revenue, irrespective of the duration of time for which the assessee acquires rights in a software."*

10. In assessee's case out of the total software expenses, the assessee has incurred substantial portion of the expenditure towards license fee which are to be paid periodically. Therefore it cannot be said that the payment is resulting in a benefit of enduring nature. Accordingly following the above decision of the special bench which is affirmed by the Hon'ble Delhi High Court, we hold that the expenses incurred towards payment of software license fees is revenue in nature and should allowed as a deduction. This ground of the assessee is allowed.

DISALLOWANCE UNDER SECL.14A READ WITH RULE 8D – Ground No.2

11. During the year, the assessee has earned interest income amounting to Rs. 88.19 lacs on Tax Free Bonds and Dividend of Rs. 829 lacs exempt under the Act. The assessee has calculated a suo moto disallowance of Rs. 7,73,439/- u/s.14A of the Act. The assessing officer re-computed the disallowance by invoking rule 8D, wherein he has disallowed a sum of Rs.29,69,000 towards interest under rule 8D(2)(ii) and a sum of Rs.69,14,000 under rule 8D(2)(iii). The CIT(A) upheld the disallowances.

12. The ld AR submitted that the assessee's own funds to the tune of Rs.593.69 cr. far exceeded the total investments made Rs.232.14 cr. and the disallowance under Rule 8D(2)(ii) is not warranted in the light of the judgment of the Hon'ble Supreme Court in South Indian Bank 438 ITR 1 and Reliance Utilities & Power Ltd. 313 ITR 340 (Bom) and others. The ld AR further submitted that this contention has been accepted by the Hon'ble ITAT in the Assessee's case for Assessment Year 2007-08. With regard to the disallowance made under Rule 8D(2)(iii) the ld AR submitted that the investments that have yielded exempt income alone can be considered. The ld AR placed reliance on the decision of Hon'ble ITAT Special Bench in Vireet Investments reported in 165 ITD 27. The ld AR also prayed that the investments in Growth Funds to be excluded while calculating the disallowance under rule 8D(2)(iii) and in this regard relied on the decision of the coordinate bench in the case of Manugraph Industries ITA No.4761/M/2013 (Ann.A)[2023] 151 taxmann.com 250 (Mumbai). Accordingly the ld AR submitted that the disallowance under Rule 8D(2)(ii) be deleted and the

disallowance under Rule 8D2(iii) be reworked after excluding investments that have not yielded income during the year and investments in Growth Funds.

13. The ld DR on the other hand relied on the order of the assessing officer and CIT(A)

14. We heard the parties and perused the material on record. It is a settled position now that when own funds are more than the investments earning exempt income, no disallowance under rule 8D(2)(ii) towards interest is warranted. Similar is the position that for the purpose of disallowance under rule 8D(2)(iii), only the those investment that earn tax free income should be considered. On perusal of records we notice that the assessee is having sufficient own funds which is more than the tax free investments and therefore we hold that no disallowance under rule 8D(2)(ii) can be made and the disallowance made by the assessing officer is hereby deleted. With regard to the disallowance made under rule 8D(2)(iii) we direct the assessing officer to recomputed the disallowance by considering only those investment that earn tax free income and exclude investments in growth funds. The assessing officer is further directed to consider the *suo moto* disallowance made by the assessee while re-computing the disallowance under rule 8D(2)(iii). Needless to say that the assessee be given a proper opportunity of being heard. It is ordered accordingly.

ADDITION TOWARDS UNUTILISED MODVAT CREDIT – Ground No.3

15. During the course of assessment proceedings, the assessee was asked to explain as to why the value of closing stock should not be determined by including

the element of CNVAT i.e. by adopting the "inclusive" method. In reply, the assessee submitted that the adjustment is shown in Column "C" of the P&L Account where the CENVAT credit of Rs.14331/- lacs is credited to the P&L Account. The assessee further submitted that this will have a balancing effect whereby he CENVAT credit available from opening stock and purchases is either consumed in the production process or lying in closing stock. The assessee also submitted that there cannot be a situation where the adjustments prescribed under section 145A will result in to increased in profit and therefore, no adjustments to the total income of the company is required on account of provisions of section 145A of the Act. The Assessing Officer did not accept the submissions of the assessee stating that 'non-inclusion' of CENVAT i.e. following exclusive method is totally absurd and gives a distorted and suppressed picture of actual profits of the business. The Assessing Officer thus proceeded to add the difference of the opening and closing balances of CENVAT and Sales Tax Set off, the difference being Rs. 3,28,76,516/-, to the total income of the assessee. Aggrieved, assessee filed appeal before the CIT(A). The CIT(A) upheld the action of the Assessing Officer. Further aggrieved, the assessee is in appeal before the Tribunal.

16. The Ld.AR for the assessee submitted that the Assessee follows 'exclusive' method of accounting for MODVAT / CENVAT credit with regard to inventory, purchases and consumption. As per the method of accounting regularly employed by the assessee, the purchases are accounted for net of excise duty paid thereon since such excise duty is available as CENVAT credit. The CENVAT credit is shown on the Asset side of the Balance Sheet. The opening and the closing inventories are valued at net of excise duty paid thereon. Further, the sales are

accounted inclusive of the excise duty paid. Excise duty on goods manufactured whether sold or not, is debited to P&L A/c. The inventory of finished goods is valued inclusive of excise duty thereon. As per 'Accounting Standard ("AS") - 2 Valuation of Inventories' issued by the Institute of Chartered Accountants of India ("ICAI"), purchases are to be accounted 'net' of excise duty paid thereon. The Assessee has recorded its inventory as on March 31, 2007 inclusive of taxes, duties etc. paid or incurred on the closing stock. The Assessee also accounted for purchase and sales exclusive of CENVAT. The adjustment as required u/s. 145A of the Act was reflected in the Tax Audit Report as Nil. The Ld.AR emphasized that the assessee has to mandatorily comply with the Accounting Standards issued by the ICAI. Therefore, or the purpose of its books of account, required to be statutorily maintained, the assessee has complied with AS-2, Valuation of Inventories, AS 2 makes it mandatory to follow exclusive method accounting. However, for the purpose of taxation of filing the return of income, the assessee has worked out the impact of grossing up of tax, duty, cess, etc. by restating the values of purchases, sales and inventories by including, inter-alia, the effect of CENVAT credit in the Tax Audit report.

17. The Ld.DR relied on the decision of the lower authorities.

18. We heard the parties and perused the material on record. We notice that the coordinate while considering the similar issue for AY 2007-08, discussed the amended provisions of section 145A (which is relevant for the year under consideration) and held that –

> *It is to be noted that Section 145A of the 1961 Act was inserted by Finance (No. 2) Act, 1998 w.e.f. 1.4.1999 and later there has been substitution of Section 145A of*

the 1961 Act by Finance(No. 2) Act, 2009, w.e.f. 01.04.2010, wherein new clause (b) is inserted in the provisions of Section 145A and new clause (a) in amended Section 145A concerns with valuation of inventory which is exactly similarly worded to Section 145A as was inserted by Finance (No. 2) Act, 1998, w.e.f. 01.04.1999 . The notes on clause explain the substitution of Section 145A of the 1961 by Finance Act(No.2), 2009 w.e.f. 01.04.2010 as under:

> *"Clause 56 of the Bill seeks to substitute section 145A of the Income-tax Act, which relates to method of accounting in certain cases.*
>
> *The existing provisions contained in said section 145A provides that while computing the value of the inventory as on the 1st and the last day of the previous year, the computation according to the method of accounting regularly employed by the assessee shall be adjusted to include the amount of any tax, duty, cess or fees paid or liability incurred for the same under any law in force.*
>
> *It is proposed to amend the said section so as to provide that the interest received by an assessee on compensation or on enhanced compensation, as the case may be, shall be deemed to be the income of the year in which it is received.*
>
> *This amendment will take effect from 1st April, 2010 and will, accordingly, apply in relation to the assessment year 2010-11 and subsequent years."*

The Memorandum to Finance Bill , 2009 also explain substitution of Section 145A as under which as we will see is concerned with insertion of new clause (b) to Section 145A of the 1961 Act, which is reproduced as under :

> ***"Rationalization of provisions for taxation of interest received on delayed compensation or enhanced compensation***
> *The existing provisions of Income-tax Act provide that income chargeable under the head "Profits and gains of business or profession" or "Income from other sources", shall be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee. Further, the Hon'ble Supreme Court, in the case of Rama Bai v. CIT (181 ITR 400) has held that arrears of interest computed on delayed or enhanced compensation shall be taxable on accrual basis. This has caused undue hardship to taxpayers.*
>
> *With a view to mitigating the hardship, it is proposed to amend section 145A to provide that the interest received by an assessee on compensation or enhanced*

compensation shall be deemed to be his income for the year in which it is received, irrespective of the method of accounting followed by the assessee.

Further, it is proposed to insert clause (viii) in sub-section (2) of section 56 to provide that income by way of interest received on compensation or on enhanced compensation referred to in sub-section (2) of section 145A shall be assessed as "income from other sources" in the year in which it is received.

This amendment will take effect from 1st April, 2010 and shall accordingly apply in relation to assessment year 1998-99 and subsequent assessment years."

Thus, the amendment to Section 145A of the 1961 Act by Finance Act, 2009 w.e.f. 01.04.2010 so far as valuation of inventories was similarly worded as the provision existed vide Finance Act, 1998 wef 01.04.1999. The assessee has heavily relied upon the decision of Hon"ble Bombay High Court in the case of CIT v. Diamond Dye Chem Limited(supra), wherein Hon"ble Bombay High Court held that the tax impact will be neutral under both inclusive and exclusive method and held that cenvat credit could not have been added to value of closing stock, by holding as under:

"5. We have considered the submissions. It is not disputed that the assessee was liable to excise duty. The assessee got credit in the excise duty already paid on the raw materials purchased by it and utilized in the manufacturing of excisable goods. The assessee was adopting the exclusive method i.e. valuing the raw-materials on the purchase price minus (-) the Modvat credit. The same would be permissible. The Apex Court in the case of Indo Nippon Chemicals Co. Ltd. (supra) while affirming the order of High Court, has observed that the income was not generated to the extent of Modvat credit or unconsumed raw-material. Merely because the Modvat credit was irreversible credit offered to manufacturers upon purchase of duty paid raw-materials, that would not amount to income which was liable to be taxed under the Act. It is also held that whichever method of accounting is adopted, the net result would be the same.

6. Considering the above, the amount of the un-utilized Cenvat credit could not have been directly added to the closing stock."

The assessment year under consideration before Hon"ble Bombay High Court in the case of Diamond Dye Chem Limited(supra) was AY 2008-09 which was post amendment by Finance Act, 1998 wherein Section 145A was inserted w.e.f.

01.04.1999. The Hon"ble Bombay High Court in the case of Diamond Dye Chem Limited(supra) while adjudicating appeal relied upon decision of Hon"ble Supreme Court in the case of CIT v. Indo Nippon Chemicals Company Limited (2003) 261 ITR 275(SC) , wherein Hon"ble Supreme Court in the case of Indo Nippon Chemicals Limited(supra) was seized of AY 1989-90 which was prior to introduction of Section 145A by Finance Act, 1998 w.e.f. 01.04.1999. Incidentally when earlier Hon"ble Bombay High Court was adjudicating appeal in the case of CIT v. Indo Nippon Chemicals Co. Limited reported in (2000) 245 ITR 384(Bom.) which related to AY 1989-00, it was brought to the notice of Hon"ble Bombay High Court that there was newly inserted Section 145A of the 1961 Act by Finance Act(No. 2) , 1998 w.e.f. 01.04.1999, where in Hon"ble Bombay High Court held in para 10 , as under:

> *"10. Before concluding, we may mention that, in rejoinder, the learned counsel for the department has brought to our attention section 145A of the Act. He has also invited our attention to the Subsequent Guidance Note issued by the Institute of Chartered Accountants of India on Tax Audit under section 44AB of the Act. It was contended that even the ICAI has subsequently declared that the net/exclusive method adopted by various assessees should be applied with adjustments on account of any tax, duty, cess or fee actually paid or incurred on inputs which should be added to the cost of the inputs if not so added in the books of account. He contended that in the Subsequent Guidance Note, the ICAI once again discussed the above two methods and, in the circumstances, it was urged that the net method followed by the assessee was wrong because the assessee has followed the net method without making any adjustments as required under section 145A. In this connection, we may point of that section 145A was introduced by the Finance (No. 2) Bill 1998. Originally, the Bill contemplated the proposed amendment to apply from 1-4-1986 in relation to the assessment year 1986-87 and subsequent years. However, later on, when the said Bill was enacted into law, the provision was made applicable from 1-4-1999, i.e., assessment year 1999-2000. In this appeal, we are concerned with the assessment year 1989-90. In the circumstances, we are not inclined to go into the provisions of section 145A. We are also not examining, therefore, the Subsequent Guidance Note issued by the ICAI which is based on section 145A. The Legislature clearly intended, therefore, that the computation made by the assessees prior to the assessment year 1999- 2000 should not be disturbed and, therefore, the Legislature has brought the said section 145A into force only from 1-4-1999."*

Hon"ble Bombay High Court while adjudicating appeal in the case of Diamond Dye Chem Limited(supra) did not consider the Co-ordinate Bench decision in the case of Catrini India Limited(supra) as well amended provisions of Section 145A of the 1961 Act. It relied upon decision of Hon"ble Supreme Court decision in case of Indo Nippon Chemical(supra) which is prior to insertion of Section 145A of the 1961 Act. Under these circumstances as discussed by us elaborately above, we are inclined to restore this matter back to the file of the AO for denovo determination of the issue in the light of our above discussions as well decision referred to above.The assessee will be allowed to raise its defence in denovo proceedings. The AO shall provide proper and adequate opportunity of being heard in the set aside proceedings. The grounds of appeal are allowed for statistical purposes We order accordingly.

19. Respectfully following the above decision of the coordinate bench we remit the issue back to the assessing officer with similar directions.

TRANSFER PRICING ADJUSTMENT – Ground No.4
(a) NOTIONAL INTEREST FOR COUNTER GUARANTEE GIVEN TO AE

20. The Assessee and Kansai Paint Co. Ltd., Japan (KPJ) an AE formed a joint venture, Kansai Coating Malaysia Sdn. Bdh. (KCM) to take over the business assets and liabilities of Sime Darby Malaysia Bhd., a Malaysian company. The Assessee subscribed to 55% and KPJ to 45% of the share capital of KCM. KPJ had provided guarantee to RBH Bank Berhard, a local Bank for the loan taken by KCM for its working capital requirements. The Assessee had by its letter dated 7th August 2008 to KCJ provided a counter guarantee to the extent of 55% (pg.88 of the PB-I). The assessee contended before the TPO that giving counter guarantee is a shareholder activity and hence cannot be subject to TP adjustment. The TPO did not accept the submissions of the assessee and benchmarked the ALP for the guarantee @ 6.36% being the difference between BBB (15.68%) and AAA

(9.32%) credit ratings as per CRISIL to arrive at a TP adjustment of Rs.1,06,23,299. On further appeal the CIT(A) upheld the TP adjustment.

21. The ld AR submitted that the issue of counter guarantee has been considered by the decision of the coordinate bench in assessee's own case for the assessment year 2007-08. The counter guarantee given by the Assessee has been held to be an international transaction and ALP determined @ 0.5% of the corporate guarantee. The ld AR further submitted that the ALP @ 6.36% based on local interest as per CRISIL credit rating is incorrect. A corporate guarantee and a bank guarantee are distinct and the rate applicable for a bank guarantee cannot be applied for a corporate guarantee. It is also submitted that in the case of JSW Ltd. (2023) 153 taxmann.com 457 para 5, the corporate guarantee fee has been fixed at 0.35% and the same be accepted in the present case.

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

23. We heard the parties and perused the material on record. We notice that the coordinate bench in assessee's own case for AY 2007-08 has considered the issue of ALP adjustment towards counter guarantee and held that –

> *"27. We have considered rival contentions and perused the material on record. We have observed that the assessee alongwith its AE namely Kansai Paints Company Ltd., Japan jointly promoted a company in Malaysia namely Kansai Coatings Sdn. Bhd. Malaysia which is also AE of the assessee wherein the assessee held 55% of share while the Japanese company held 45% share in the Malaysian JV Company. The said Malaysian company acquired business assets and liabilities of Sime Darby Malaysia Bhd. for which Malaysian company obtained loan mainly for working capital of RM 24 Million from RBH Bank*

Berhad , a Malaysian Bank. As a condition for grant of loan, the Japanese AE of the assessee who was co-promoter of the Malaysian Company stood guarantor to the Bank. The Japanese Company required assessee to give counter guarantee to it in the ratio of 55% which was in the ratio of shareholding of the assessee in Malaysian Company. The assessee gave counter guarantee to its Japanese AE to the tune of RM 13.2 Million (Rs. 17.72 crores) towards it share in the JV company. The assessee is contemplating that this is a non fund based liability as there is no outflow of funds. On being asked by the Bench, it was fairly admitted by learned counsel for the assessee that in case of default by Malaysian Company with their bankers in Malaysia , the guarantee issued by Japanese AE in favour of Malaysian Bank will devolve and then assessee may in that eventuality will be asked to contribute its share by way of outflow of funds to meet its obligation under counter guarantee and this non fund based liability will get converted into fund based liability. Once corporate guarantees are issued , then the capacity of the issuer to raise further loans from banks, financial institutions etc. will get reduced as the corporate guarantee will certainly lead to higher debt to equity ratio which will lead to reduction in the capacity of issuer to borrow money from Banks, FI etc which could also lead to higher rate of interests charged by the bankers in case borrower become over leveraged due to higher debts including guarantees issued . Thus, in our considered view, the issue of corporate guarantee by taxpayer in favour of its AE is certainly an international transaction covered by provisions of Section 92B and in our considered view provisions of un-amended provisions of Section 92B duly covered liability created by a taxpayer in favour of its AE which was even by way of non fund based liability such as corporate guarantee issued by taxpayer in favour of AE. Explanation inserted in Section 92B by Finance Act, 2012 w.e.f. 01.04.2002 also clarified the position that guarantees issued by taxpayer in favour of its AE shall also be covered as an international transaction. Section 92B was amended by Finance Act, 2012 w.e.f. 01.04.2012 wherein an Explanation was inserted to clarify the position that international transaction would included guarantee also. The provisions of Section 92B are reproduced hereunder:

> ***"Meaning of international transaction. 92B.***
> ***92B.*** *(1) For the purposes of this section and sections 92, 92C, 92D and 92E, "international transaction" means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such*

enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises.

(2) A transaction entered into by an enterprise with a person other than an associated enterprise shall, for the purposes of sub-section (1), be [deemed to be an international transaction] entered into between two associated enterprises, if there exists a prior agreement in relation to the relevant transaction between such other person and the associated enterprise, or the terms of the relevant transaction are determined in substance between such other person and the associated enterprise [where the enterprise or the associated enterprise or both of them are non-residents irrespective of whether such other person is a non-resident or not].

[Explanation.—For the removal of doubts, it is hereby clarified that—
(i) the expression "international transaction" shall include—

(a) the purchase, sale, transfer, lease or use of tangible property including building, transportation vehicle, machinery, equipment, tools, plant, furniture, commodity or any other article, product or thing;

(b) the purchase, sale, transfer, lease or use of intangible property, including the transfer of ownership or the provision of use of rights regarding land use, copyrights, patents, trademarks, licences, franchises, customer list, marketing channel, brand, commercial secret, know-how, industrial property right, exterior design or practical and new design or any other business or commercial rights of similar nature;

(c) capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;

(d) provision of services, including provision of market research, market development, marketing management, administration,

technical service, repairs, design, consultation, agency, scientific research, legal or accounting service;

(e) a transaction of business restructuring or reorganisation, entered into by an enterprise with an associated enterprise, irrespective of the fact that it has bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date;

(ii) the expression "intangible property" shall include—

(a) marketing related intangible assets, such as, trademarks, trade names, brand names, logos;

(b) technology related intangible assets, such as, process patents, patent applications, technical documentation such as laboratory notebooks, technical know-how;

(c) artistic related intangible assets, such as, literary works and copyrights, musical compositions, copyrights, maps, engravings;

(d) data processing related intangible assets, such as, proprietary computer software, software copyrights, automated databases, and integrated circuit masks and masters;

(e) engineering related intangible assets, such as, industrial design, product patents, trade secrets, engineering drawing and schema-tics, blueprints, proprietary documentation;

(f) customer related intangible assets, such as, customer lists, customer contracts, customer relationship, open purchase orders;

(g) contract related intangible assets, such as, favourable supplier, contracts, licence agreements, franchise agreements, non-compete agreements;

(h) human capital related intangible assets, such as, trained and organised work force, employment agreements, union contracts;
(i) location related intangible assets, such as, leasehold interest, mineral exploitation rights, easements, air rights, water rights;

(j) goodwill related intangible assets, such as, institutional goodwill, professional practice goodwill, personal goodwill of professional, celebrity goodwill, general business going concern value;

(k) methods, programmes, systems, procedures, campaigns, surveys, studies, forecasts, estimates, customer lists, or technical data;

(l) any other similar item that derives its value from its intellectual content rather than its physical attributes.]"

Notes on clauses to Finance Bill, 2012 also clarified that explanation is clarificatory in nature and shall be applicable from 01.04.2002, which is reproduced hereunder:

"Clause 34 of the Bill seeks to amend section 92B of the Income-tax Act relating to meaning of international transaction. The existing provisions of the aforesaid section 92B provide the definition of "international transaction" for the purposes of the said section and sections 92, 92C, 92D and 92E.

It is proposed to insert an Explanation to the aforesaid section so as to clarify the definition of the expressions "international transaction" and "intangible property".

This amendment will take effect retrospectively from 1st April, 2002 and will, accordingly, apply in relation to the assessment year 2002-2003 and subsequent assessment years."

We have also observed that Mumbai-tribunal has consistently held that issuance of corporate guarantee by a taxpayer in favour of its AE within meaning u/s 92A is an international transaction which is covered u/s 92B of the 1961 Act. Reference is drawn to decision of Mumbai-tribunal in the case of Piramal Glass Limited v. DCIT reported in (2017) 80 taxmann.com 68(Mum-trib,) and decision of Mumbai-tribunal in the case of Videocon Industries Limited v. DCIT reported in (2017) 79 taxmannn.com 216(Mum trib.) and there are several other decision of Mumbai-tribunal.

We have also noted that recently Hon"ble Bombay High Court in the case of CIT v. Glenmark Pharmaceuticals Limited reported in (2019) 101 taxmann. com 84(Bombay) had held that ALP of the corporate guarantee can not be determined on the basis of charges as were prevailing for issuance of Bank Guarantee. The Hon"ble Bombay High Court held that no substantial question arose in this appeal. The Assessment year before Hon"ble Bombay High Court was AY 2009-10 and it based its decision on its earlier order in taxpayer"s own case for AY 2008-09, dated 02.02.2017 in ITA no. 1302 of 2014. The order of Hon"ble Bombay High Court for AY 2009-10, dated 10.12.2018 in the case of Glenmark Pharmaceuticals Limited (2019) 101 taxmann.com 84(Bom.), is reproduced hereunder:

> *"3. Regarding Question No. (1):—*
>
> *(a) We note that the impugned order of the Tribunal allowed the appeal of the respondent - assessee holding that Arm's Length Price of corporate guarantee cannot be determined on the basis of the Bank Guarantee. This by following its order dated 13.11.2013 in respect of the same respondent - assessee for the assessment year 2008-09.*
>
> *(b) Mr. Tejveer Singh, the learned counsel for the Revenue, very fairly points out that being aggrieved by the above order dated 13.11.2013 of the Tribunal for the assessment year 2008-09, Revenue had filed an appeal to this Court being Income Tax Appeal No. 1302 of 2014. The appeal of the Revenue on this issue was dismissed by the order dated 2.2.2017 by this Court as it did not give rise to any substantial question of law.*
>
> *(c) No distinguishing feature in fact or in law in this appeal from that in Income Tax Appeal No. 1302 of 2014 is shown to us.*
>
> *(d) Therefore, for the reasons recorded in our order dated 2.2.2017, this question also does not give rise to any substantial question of law. Thus, not entertained."*

The Hon'ble Bombay High Court has consistently held that comparison cannot be done while computing ALP of international transaction by way of corporate guarantee with bank guarantee. The similar stand was taken in CIT v. Everest Kento Cylinders Limited reported in (2015) 378 ITR 57(Bom.) , wherein Hon"ble Bombay High Court held as under:

> *"10. Having considered submissions of Mr. Malhotra for the revenue and Mr. Pardiwalla for the assessee, we are of the view that the order of the Tribunal as regards disallowance under section 14A and restricting the same to Rs. 1 lac was justified in view of the material before the Tribunal. Furthermore, having considered the fact that a sum of Rs. 4,47,649/- was not conceded in the return but was adhoc acceptance during the course of assessment, the assessee could not be bound by it. The Tribunal as the second fact finding authority had gone into factual aspects in great detail and therefore having interpreted the law as it stood on the relevant date the order passed cannot be faulted. In the matter of guarantee commission, the adjustment made by the TPO were based on instances restricted to the commercial banks providing guarantees and did not contemplate the issue of a Corporate Guarantee. No doubt these are contracts of guarantee, however, when they are Commercial banks that issue bank guarantees which are treated as the blood of commerce being easily encashable in the event of default, and if the bank guarantee had to be obtained from Commercial Banks, the higher commission could have been justified. In the present case, it is assessee company that is issuing Corporate Guarantee to the effect that if the subsidiary AE does not repay loan availed of it from ICICI, then in such event, the assessee would make good the amount and repay the loan. The considerations which applied for issuance of a Corporate guarantee are distinct and separate from that of bank guarantee and accordingly we are of the view that commission charged cannot be called in question, in the manner TPO has done. In our view the comparison is not as between like transactions but the comparisons are between guarantees issued by the commercial banks as against a Corporate Guarantee issued by holding company for the benefit of its AE, a subsidiary company. In view of the above discussion we are of the view that the appeal does not raise any substant"*

We have further noted that Hon"ble Supreme Court admitted SLP (Refer (2017) 85 taxmann.com 359(SC))against order of Hon"ble Bombay High Court in the case of CIT v. Glenmark Pharmaceuticals Limited reported in (2017) 85 taxmann.com 349(Bom.) for AY 2008-09 which is now decided by Hon"ble Supreme Court vide orders dated 11.12.2008 in CIT(LTU) v. Glenmark Pharmaceuticals Limited reported in (2018) 103 CCH 0314(SC) for AY 2008-09, wherein Hon"ble Supreme Court held as under:

"1. The following two questions arise for determination in this appeal filed by the Revenue.

(i) With respect to addition of Rs.11,51,24,333/- to the income of the assessee (respondent herein) made by the Assessing Officer (A.O.) on account of guarantee commission chargeable to its Associate Enterprises, whether the benchmark fixed by the Transfer Pricing Officer (TPO) for the international transaction by considering arm's length rate of the bank guarantee at 3% under Section 92CA(3) of the Income Tax Act, 1961 was correct?

(ii) Whether interest was not payable by the assessee/respondent under Section 234B of the Income Tax Act, 1961 on failure to deposit the advance tax in respect of tax payable under Section 115JB of the Income Tax Act, 1961?

2. Insofar as question No.(i) is concerned we have perused the order of the learned Tribunal and the order of the High Court affirming the view taken by the learned Tribunal.

3. On such consideration we find that question No.1 has been rightly decided by the High Court in favour of the Assessee and against the Revenue. The same would, therefore, not require reopening in this appeal. Insofar as question No.(ii) i.e. interest payable under Section 234B of the Income Tax Act, 1961 is concerned, the matter will require an in-depth hearing."

The Hon"ble Bombay High Court had earlier held in the case of Glenmark Pharmaceuticals Limited (2017) 85 taxmann.com 349(BOM) for AY 2008-09 that no comparison can be made while determining ALP of commission on corporate guarantee with bank guarantee. The Hon"ble Bombay High Court held as under:

"3. Regarding question no.(i):—

(a) We note that the impugned order of the Tribunal while allowing the assessee's appeal holding that the Arms Length Price of Corporate Guarantee cannot be determined on the basis of comparison with Bank Guarantee and relied upon the decision of its Co-ordinate bench in the case of Everest Kento Cylinder Ltd. v. Dy. CIT [2013] 34 taxmann.com

> *19 (Mum. - Trib.). Mr. Suresh Kumar, the learned counsel appearing for the Revenue very fairly states that being aggrieved with the above order in M/s. Everest Kento Cylinders Ltd., the Revenue had filed an appeal to this Court raising an identical issue viz. CIT v. Everest Kento Cylinders Ltd. [2015] 378 ITR 57/232 Taxman 307/58 taxmann.com 254 (Bom.). By an the above appeal was not entertained.*
>
> *(b) As no distinction in facts and/or law has been shown to us in this appeal which would warrant taking a different view on this very issue from that taken by this Court in Everest Kento Cylinders Ltd. (supra), we follow the same.*
>
> *(c) Accordingly, question no.(i) as proposed does not give rise to any substantial question of law for the reasons indicated in our order dated 8th May, 2015 in Everest Kento Cylinders Ltd. (supra). Therefore not entertained."*

The rate of guarantee commission varies depending upon several factors depending upon risk factor, period involved, amount involved, state of financial health of borrower, prevailing cost of funds in domestic and international market , state of economy where borrowers are located so on and so forth. The TPO applied CUP method to benchmark international transactions to compute ALP. It is observed vide TPO benchmarking that tax court of Canada while giving decision in the case General Electric Capital Canada Inc. v. The Queens (2009 TCC 563) based on facts and circumstances upheld ALP of guarantee commission @1% p.a. . On the other hand the TPO has also referred to guarantee commission charged by banks which is to the tune of 3%p.a. on bank guarantee issued by bankers. While it is also benchmarked that in a case of the Dutch State, FMO had charged guarantee commission of 2.5% in the case of Rabo India Finance Pvt. Limited wherein both were related parties. Thus, what emerges is that providing of corporate guarantee by a taxpayer to its AE within meaning of Section 92A is an international transaction u/s 92B which need to be benchmarked using CUP method to compute ALP of the said transaction of furnishing of corporate guarantee. The ALP to be computed will vary depending upon e several internal as well external factors. In our considered view, end of justice will be met if the ALP be determined @ 0.5% p.a. of corporate guarantee issued by assessee in favour of Kansai Paint Company Limited, Japan. The Mumbai-tribunal has computed ALP@ 0.5% in the case of Piramal Glass Limited v. DCIT reported in (2017) 80 taxmann.com 68(Mumbai) , in the case of Videocon Industries Limited v. DCIT reported in (2017) 79 taxmann.com 216(Mum-trib.) , in the case of Zee Entertainment

Enterprises Limited v. ACIT reported in (2018)100 taxmann.com 479(mum trib) and in the case of DCIT v. Rolta India Limited reported in (2019) 101 taxmann.com 40(mum-trib.).In view of our aforesaid discussions in detail, we are not inclined to accept the plea of the assessee that providing of corporate guarantee by tax-payer to its AE within meaning of Section 92A can be taken as international transaction u/s 92B only with effect from AY 2013-14 as the insertion of explanation to Section 92B By Finance Act, 2012 is w.e.f. 01.04.2002 . The said explanation was declared to be clarificatory in nature. This ground number 5 (a) and (b) are partly allowed. We order accordingly."

24. Respectfully following the above decision of the coordinate bench we hold that providing counter guarantee to AE is an international transaction within the meaning of section 92B of the Act and that ALP on the shall be calculated at 0.5%. The TPO is directed to recompute the ALP accordingly.

(b) NOTIONAL INTEREST FOR DELAYED PAYMENT FROM AEs.

25. During the year, the assessee has made exports of goods amounting to Rs.4,43,60,382/- to its Associated Enterprises (AEs) as well as its Non Associated Enterprises (non AEs). There has been delay in receiving the export proceeds from the sales made to AEs and non AEs. The TPO, by applying CUP method, has proceeded to determine what interest the assessee would have earned had it been advanced such loans to unrelated parties in similar situation as that of the subsidiaries. And since the assessee was the tested party, the TPO adopted the interest rate which the assessee would have earned by advancing such loan to an unrelated party in India. The TPO has considered various types of ratings which are given by CRISIL to corporate bonds. The TPO held that as unsecured loan is like an unrated bond and the risk is very high in such circumstances. Hence, the TPO considered the least rating and determined at a rate of 15,68% and calculated

notional interest on delay in receipt of service fees and export proceeds which has led to proposing disallowance of Rs.6,99,060/- and Rs.4,96,527/- aggregating to Rs.11,95,587/-.On appeal, CIT(A) upheld the addition. Aggrieved, the assessee is in appeal before the Tribunal.

26. The ld AR submitted that the assessee does not have any borrowings and that no interest on delayed payments is charged for the non-AE transactions. Given this it was submitted that there should not be any interest charged for relayed payments on AE transactions. Without prejudice the ld AR submitted that the rate applied by the revenue is the domestic rate which is not correct and that the LIBOR rate should be applied. Reliance in this regard is placed on The Bombay High Court in the case of Tecnimont (2018) 96 taxmann.com 223. The ld AR further prayed that the TPO has considered a credit period of 30 days and prayed that a credit period of 90 days be considered.

27. The ld DR relied on the order of the CIT(A) and the assessing officer.

28. We heard the parties and perused the material on record. It is settled positions that delay in receipt of receivables from AE is an international transaction. The Hon'ble Bombay High Court in the case of Tecnimont (P.) Ltd (supra) has held that the delay in receivables is in substance amounts to granting of loan to an AE so as to enjoy the funds, which the AE would otherwise have to repay and that interest needs to be charged based LIBOR rates as the rate prevailing in country where the loan is received/consumed by the AE. We therefore direct the assessing officer to charge interest at the rate of LIBOT +100

basis points after considering a credit period of 60 days. This ground of the assessee is partly allowed.

DISALLOWANCE OF THE PROVISION FOR WARRANTY – Ground No.5

29. The assessee, in its P&L Account, has debited Rs.25,00,000/- towards provision for warranty. The business of the assessee consists of two kinds of products, viz. decorative and industrial. The said claim was made in respect of expected future claims on performance warranty up to 7 years, given by the assessee on its exterior decorative paints and expected claims from industrial customers on account of quality issues. The provision for warranty is calculated @0.035% of the sales value of products on which warranty is offered by the assessee and amount of Rs.25 lakhs was debited as provision for warranty. The assessing officer has disallowed the provision made for the relevant year on the ground that it is a contingent liability and the Assessee has not met the following 3 conditions laid down by the Apex Court in Rotork Controls India Ltd. 314 ITR 62 viz.

a. An enterprise has a present obligation as a result of past event.
b. It is probable that an outflow of resources will be required to settle the obligation and
c. A reliable estimate can be made of the amount of obligation.

30. The assessing officer further held that there was no scientific or actuarial basis for the provision by relying upon the judgment of the Hon'ble Supreme Court in Bharat Earth Movers' case 245 ITR 428.The CIT(A) has confirmed the disallowance.

31. The Ld.AR submitted that the assessee had started giving warranty on its decorative paints and industrial products from FY 2006-07. Therefore, in absence of past experience, the Assessee had to rely on the available data of the past experience of the industry leaders of the paint industry. Asian Paints Limited was the market leader in the decorative paints market comprising of around 40 percent of the market share. The Assessee calculated the provision for warranty at the rate of 0.035% of the sales value of the products. While making the provision for warranty, the past experience of the actual claims of the industry has been taken into account. This percentage of 0.035% was worked out by the Assessee based on the consolidated financial information of M/s Asian Paints Limited. (Please see pg no. 241 to 244 of the paper book), in the following manner:

Sr No.				**(Rs in Millions)**
1	Total Turnover of Asian Paints Limited	42,598.59	39,099.65	
2	Turnover of Exterior Paints (Estimated at 20%)	8,519.72	7,019.93	
3	Provision for warranty	3.43	1.91	
	% of provision to turnover of Exterior paints	0.040	0.027	**0.035**
			Rounded to	0.035

The Ld.AR submitted that the liability to carry out repairs / replacement or make good for short supplies accrues on the date when the sales is effected and hence it is an in-built liability accrued in respect of warranty services and such liability is a definite ascertainable one and cannot be in the nature of a contingent liability. The ld AR further submitted that the conditions as mentioned by the assessing officer have been satisfied and that the assessee has also partly discharged its obligation in

the accounting year 2008-09. Accordingly, the ld AR submitted that the provision for warranty is not a contingent liability and should therefore, be allowed.

32. The ld. DR on the other hand vehemently argued that the provision is made only on an estimation basis and not based on any scientific method. Therefore the ld DR submitted that the provision based on estimate is a contingent liability and cannot be allowed.

33. We heard the parties and perused the material on record. We notice that the assessee has started providing warranties to the products sold from 2016-17 and that the basis of making the provision is the warranties provided by Asian Paints. The Hon'ble Supreme Court in the case CIT v/s. Rotork Controls India Ltd. (314 ITR 62) held that for a provision to qualify for recognition, there must be a present obligation arising from past events, settlement of which is expected to result in an outflow of resources and in respect of which a reliable estimate of amount of obligation is possible. In assessee's case there is no doubt that there is an obligation of guarantee that arises on sale of products by the assessee and that certain warranty towards which provisions are made is settled by the assessee in subsequent years. The contention of the revenue is that the basis on which the guarantee is provided for is not scientific. In our considered view, the method adopted by the assessee based on Asian Paint's provision for guarantee cannot be rejected without analyzing the provision vis a vis subsequent expenditure towards guarentee and whether the amount provided is commensurate with the actual spending. We in this regard notice that the assessee during the course of

assessment proceeding had submitted the following details with regard to provision towards warranty and the actual expenditure incurred.

Description	**F.Y.2006-07**	**F.Y. 2007-08**	**F.Y. 2008-09**
Opening Balance	--	20	45
Add: Amount claimed on provisional basis	20	25	80
Less: Incurred during the year (Utilisation/settlement)	--	--	65
Closing Balance	**20**	**45**	**60**

From the above it is clear that the assessee has incurred actual expenditure of Rs.65 lakhs during FY 2008-09 and therefore there is merit in the submission that the provision is resulting in actual expenditure in subsequent years. However it is noticed that the assessing officer has not taken cognizance of the actual expenditure incurred in the later years and also it is not clear how the expenditure is allowed in subsequent year i.e. whether actual amount incurred is allowed as a deduction. In case the amount is allowed in the year in which actually incurred then allowing the provision in the current year would amount to double deduction. We therefore remit the issue back to the assessing officer with a direction to examine the basis of provision, the actual expenditure incurred and allow the claim in accordance law with after giving a reasonable opportunity of being heard to the assessee.

ALLOWABILITY OF AMALGAMATION EXPENSES – Ground No.6

34. The Assessee had incurred Rs.19,26,722 during the assessment year 2006-07 as amalgamation expenses of which 1/5th had been claimed under sec.35DD. In the following year the Assessee incurred further expenses of Rs.93,10,466/- and

claimed the same under sec.35DD in 4 installments along with the balance of previous unclaimed amalgamation expenses. The AO rejected the claim holding that there was no provision to change the quantum of deduction from 1/5th to 1/4th nor to extend the period of allowability beyond 5 years. Accordingly the assessing officer allowed only 1/5th of RS.93,10,466 and disallowed the excess claim of Rs.4,65,524/- . The CIT(A) has confirmed the disallowance.

35. The Ld.AR submitted that from the plain reading of the section 35DD, it can be inferred that if the assessee incurs any expenditure wholly and exclusively for the purpose of amalgamation of the undertaking, irrespective of the year in which such expenses have been incurred i.e. whether prior to or subsequent to the year in which such amalgamation of undertaking takes place, such would be allowed as deduction in 5 equal installments cumulatively, starting from the year in which such amalgamation actually took place. Since Assessee had incurred expenditure amounting to Rs. 93,10,647/- wholly for the purpose of amalgamation in F.Y. 2007-08 i.e. year subsequent to which amalgamation actually took place, hence assessee had to amortize the expenditure in remaining 4 years, as deduction of the said expenditure is only allowable in 5 subsequent assessment years from the date of amalgamation i.e. in the present case financial year 2006-07. The Ld.AR, therefore, prayed that the Assessing Officer be directed to allow deduction of Rs. 4,65,524/- u/s 35DD of the Act.

36. The ld DR on the other hand submitted that as per the provisions contained in Sec. 35DD only 1/5 deduction in each of 5 successive previous years can be claimed beginning with the year in which amalgamation took place. The ld DR further submitted that there is no such provision to change the quantum of

deduction from 1/5th to 1/4th as claimed by the assessee. Therefore the ld DR prayed that the decision of the CIT(A) be upheld.

37. We heard the parties and perused the material on record. Before proceeding further we will look at the provisions of section 35DD which reads as under -

> ***Amortisation of expenditure in case of amalgamation or demerger.***
> ***35DD.*** *(1) Where an assessee, being an Indian company, incurs any expenditure, on or after the 1st day of April, 1999, wholly and exclusively for the purposes of amalgamation or demerger of an undertaking, the assessee shall be allowed a deduction of an amount equal to one-fifth of such expenditure for each of the five successive previous years beginning with the previous year in which the amalgamation or demerger takes place.*
>
> *(2) No deduction shall be allowed in respect of the expenditure mentioned in sub-section (1) under any other provision of this Act.*

38. The language of section 35DD is unambiguous wherein it is provided that the expenses incurred wholly and exclusively for the purpose of amalgamation is to be allowed as a deduction in 5 equal installments beginning from the year in which the amalgamation takes place. In assessee's case it is an undisputed fact that the amalgamation took place in the previous year 2006-07 and therefore 1/5th of the expenses incurred towards amalgamation has to be claimed from the said year for 5 years. The claim of the assessee is that the expenses incurred in the subsequent year i.e. 2007-08 need to be allowed in 4 installments since the assessee cannot claim the expenditure beyond 5 years from the year of amalgamation. However we are unable to appreciate this contention of the assessee for the reason that there is no provision under section 35DD to claim 1/4th of the expenditure incurred towards amalgamation and that the assessee could claim only 1/5th of the expenditure from

AY 2007-08 for 5 years. Therefore we see no reason to interfere with the decision of the CIT(A). This ground of the assessee is rejected.

DISALLOWANCE OF COMMISSION PAYABLE TO THE MANAGING DIRECTOR UNDER SEC.40(a)(ia) – Ground No.7

39. During the previous year, the assessee made provision of Rs. 75 lacs for commission payable to the Managing Director ("MD"). The MD, being an employee, the commission payable to the MD was considered to a part of his salary as per section 17(1) of the Act and the tax on the same was deducted under section 192 of the Act when the said commission was paid to him in the month of June 2008. For the year under consideration the assessing officer, made an addition of Rs. 75,00,000/- u/s 40(a)(ia) of the Act for the provision made against the commission payable to the MD on the ground that:

> a) commission has the same meaning assigned to that in section 194H wherein the term 'commission' has been defined in an inclusive manner;
>
> b) principal-agent relationship is not required, mere provision of services to another person is enough; and
>
> c) section 40(a)(ia) begins with the word "any interest, ..." and the section is applicable to tax deductible under Chapter XVII-B. section 40(a)(ia) is a legal fiction and has to be strictly construed.

40. On appeal, the CIT(A) upheld the disallowance. The Ld AR submitted that that the MD is an employee of the assessee company. The MD is responsible for the day to day management of the assessee Company subject to the superintendence, control and direction of the Board of Directors. Apart from looking after the day to day management, the MD had also attended several Board

and Audit Committee Meetings of the assessee in the capacity of an MD. The tax is deducted at source u/s 192 of the Act for the payments made to the MD in the capacity of an employee. As per the accrual method followed by the Companies Act, the Assessee had made a provision of Rs.75 lakhs as commission payable to the MD on 31.03.2008. The said provision was reversed on 1st April 2008 and credited to the P & L Account. As commission was part of the salary, tax of Rs.29,39,500 was deducted under sec.192 in June 2008 when the commission was actually paid and the same was deposited in July 2008. The same has been allowed in the following assessment year. Since the provision of Rs.75 lakhs has been reversed on 01.04.2008, credited to the P & L A/c. and assessed, the disallowance of the provision under sec.40(a)(ia) in the relevant year would effectively amount to double taxation. The ld AR further submitted that the provisions of sec.40(a)(ia) are not applicable to commission which forms part of salary in the light of the judgment of the Bombay High Court in the case of Pr.CIT v Indofil Industries Ltd. (2022) 135 taxmann.com 289.

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

42. We heard the parties and perused the materials. The case of the revenue is that the assessee has not deducted tax at source against the provision made towards commission payable to MD and that the commission payable is liable for tax deduction under section 194H of the Act. As per the submissions of the assessee, the allowability of commission in the subsequent year has not been questioned by the department and that since the provision of Rs.75 lakhs has been reversed on 01.04.2008, credited to the P & L A/c disallowance in the year under consideration would amount to double taxation. We notice that the assessing officer has not

considered the submission of the assessee that the provision towards commission is reversed in the subsequent and paid as part of the salary on which tax was duly deducted. In our considered view, the submissions of the assessee with regard to provision made, subsequent reversal and tax deduction on actual payment etc., needs to be factually verified in order to decide the allowability of the claim. Therefore we deem it fit to remit the issue back to the assessing officer for a de-novo verification of the issue by calling for the relevant details as may be required in this regard. The assessee is directed to submit the details and cooperate with the proceedings. It is ordered accordingly.

DISALLOWANCE OF Rs.30,317 FOR DELAYED PAYMENT OF ESIC UNDER SEC.36(1)(va) – Ground No.8

43. The Assessee had, under sec.36(1)(va) added back employees' contribution of Rs.5.87 lakhs deposited late. The sum of Rs.30,715/- was deposited within the grace period of 5 days permitted under the ESIC Act and hence, the same was claimed. The assessing officer disallowed the said amount on the ground that no grace period was provided under the ESIC Act. The CIT(A) has rejected the Assessee's contention relying upon 2 judgments holding that provisions of sec.43B are not applicable to employees' contribution to PF/ESIC and the fact that the same has been paid before the due date of filing the return is not applicable.

44. The Ld.AR of the assessee has fairly conceded that this ground has to be decided against the assessee in view of the judgement of the Hon'ble Supreme Court in the case of Checkmate Services P Ltd vs CIT Civil Appeal No.2833 of 2016 dated 12/10/2022 .

45. We find that now, the issue in question "as to whether the assessee is entitled for deduction claimed towards contribution of sum to provident fund on behalf of the employees deposited after due date prescribed under the Act but before the date of filing the return;" has been set at rest by the Hon'ble Supreme Court in case of Checkmate Services P Ltd vs CIT Civil Appeal No.2833 of 2016 dated 12/10/2022 that assessee is not entitled for claim of deduction qua the amount deposited towards employees contribution on account of provident fund after due date prescribed under the Act by returning following findings:-

> *"51. The analysis of the various judgments cited on behalf of the assessee i.e., Commissioner of Income-Tax v. Aimil Ltd.; Commissioner of Income-Tax and another v. Sabari Enterprises; Commissioner of Income Tax v. Pamwi Tissues Ltd.; Commissioner of Income-Tax, Udaipur v. Udaipur Dugdh Utpadak Sahakari Sandh Ltd. and Nipso Polyfabriks (supra) would reveal that in all these cases, the High Courts principally relied upon omission of second proviso to Section 43B (b). No doubt, many of these decisions also dealt with Section 36(va) with its explanation. However, the primary consideration in all the judgments, cited by the assessee, was that they adopted the approach indicated in the ruling in Alom Extrusions. As noticed previously, Atom Extrutions did not consider the fact of the introduction of Section 2(24)(x) or in fact the other provisions of the Act.*
> *52. When Parliament introduced Section 43 B, what was on the statute book, was only employer's contribution (Section 34(1) (iv)). At that point in time, there was no question of employee's contribution being considered as part of the employer's earning. On the application of the original principles of law it could have been treated only as receipts not amounting to income. When Parliament introduced the amendments in 1988-89, inserting Section 36(l)(va) and simultaneously inserting the second proviso of Section 43 B, its intention was not to treat the disparate nature of the amounts, similarly. As discussed previously, the memorandum introducing the Finance Bill clearly stated that the provisions - especially second proviso to Section 43B - was introduced to*

ensure timely payments were made by the employer to the concerned fund (EPF, ESI, etc.) and avoid the mischief of employers retaining amounts for long periods. That Parliament intended to retain the separate character of these two amounts, is evident from the use of different language. Section 2(24)(x) too, deems amount received from the employees (whether the amount is received from the employee or by way of deduction authorized by the statute) as income - it is the character of the amount that is important, i.e., not income earned. Thus, amounts retained by the employer from out of the employee's income by way of deduction etc. were treated as income in the hands of the employer. The significance of this provision is that on the one hand it brought into the fold of "income" amounts that were receipts or deductions from employees income; at the time, payment within the prescribed time - by way of contribution of the employees' share to their credit with the relevant fund is to be treated as deduction (Section 36(1)(va)). The other important feature is that this distinction between the employers' contribution (Section 36(1) (iv)) and employees' contribution required to be deposited by the employer (Section 36(l)(va)) was maintained - and continues to be maintained. On the other hand, Section 43 B covers all deductions that are permissible as expenditures, or out-goings forming part of the assessees' liability. These include liabilities such as tax liability, cess duties etc. or interest liability having regard to the terms of the contract. Thus, timely payment of these alone entitle an assessee to the benefit of deduction from the total income. The essential objective of Section 43B is to ensure that if assessees are following the mercantile method of accounting, nevertheless, the deduction of such liabilities, based only on book entries, would not be given. To pass muster, actual payments were a necessary pre-condition for allowing the expenditure.

53. The distinction between an employer's contribution which is its primary liability under law - in terms of Section 36(l)(iv), and its liability to deposit amounts received by it or deducted by it (Section 36(l)(va)) is, thus crucial. The former forms part of the employers' income, and the later retains its character as an income (albeit deemed), by virtue of Section 2(24)(x) - unless the conditions spelt by Explanation to Section 36(l)(va) are satisfied i.e., depositing such amount received or deducted from the employee on or before the due date. In other words, there is a marked distinction between

the nature and character of the two amounts - the employer's liability is to be paid out of its income whereas the second is deemed an income, by definition, since it is the deduction from the employees' income and held in trust by the employer. This marked distinction has to be borne while interpreting the obligation of every assessee under Section 43 B.

54. In the opinion of this Court, the reasoning in the impugned judgment that the non-obstante clause would not in any manner dilute or override the employer's obligation to deposit the amounts retained by it or deducted by it from the employee's income, unless the condition that it is deposited on or before the due date, is correct and justified. The non-obstante clause has to be understood in the context of the entire provision of Section 43B which is to ensure timely payment before the returns are filed, of certain liabilities which are to be borne by the assessee in the form of tax, interest payment and other statutory liability. In the case of these liabilities, what constitutes the due date is defined by the statute. Nevertheless, the assessees are given some leeway in that as long as deposits are made beyond the due date, but before the date of filing the return, the deduction is allowed. That, however, cannot apply in the case of amounts which are held in trust, as it is in the case of employees' contributions- which are deducted from their income. They are not part of the assessee employer's income, nor are they heads of deduction per se in the form of statutory pay out. They are others' income, monies, only deemed to be income, with the object of ensuring that they are paid within the due date specified in the particular law. They have to be deposited in terms of such welfare enactments. It is upon deposit, in terms of those enactments and on or before the due dates mandated by such concerned law, that the amount which is otherwise retained, and deemed an income, is treated as a deduction. Thus, it is an essential condition for the deduction that such amounts are deposited on or before the due date. If such interpretation were to be adopted, the non-obstante clause under Section 43B or anything contained in that provision would not absolve the assessee from its liability to deposit the employee's contribution on or before the due date as a condition for deduction.

55. In the light of the above reasoning, this court is of the opinion that there is no infirmity in the approach of the impugned judgment. The decisions of the other High Courts, holding to the contrary, do

not lay down the correct law. For these reasons, this court does not find any reason to interfere with the impugned judgment. The appeals are accordingly dismissed."

46. By following the decision rendered by Hon'ble Supreme Court in case of Checkmate Services P. Ltd. vs. CIT (supra), we are of the considered view that Ld. CIT(A) has rightly decided the issue against the assessee as the employees contribution on account of ESI lying deposited with the employers has to be deposited before the due date prescribed under the Act. Since the assessee has failed to comply with the condition precedent for depositing the employees contribution on account of PF & ESI before the due date prescribed under the Act he is not entitled for any deduction. So finding no illegality or perversity in the impugned order passed by the Ld. CIT(A) appeal filed by the assessee is hereby dismissed.

TREATY RATE TO BE APPLIED FOR DIVIDEND DISTRIBUTED INSTEAD OF RATE PRESCRIBED IN SEC.115-O – Additional Ground

47. The additional grounds raised are pure legal issue, which does not require investigation of new facts. Hence, placing reliance on the judgment of the Hon'ble Apex Court in the case of National Thermal Power Co. Ltd. v. CIT (1998) 229 ITR 383 (SC), we admit the additional grounds.

48. The ld AR fairly conceded that the issue is covered by the decision of the Special Bench decision in the case of Total Oil (P) Ltd., 104 ITR (T) 1 against the assessee. Respectfully following the decision of special bench we dismiss the additional ground raised by the assessee.

49. In result the appeal for AY 2008-09 is partly allowed.

I.T.A. No.3385/Mum/2014 - AY 2009-10

50. The grounds of appeal raised by the assessee for the assessment year 2009-10 are tabulated in the earlier part of this order, from which it is clear that all the issues arising in AY 2009-10 are similar to AY 2008-09. Considering the fact that the facts being identical our decision with respect to all the issued contended through Ground Nos.1 to 6 are mutatis mutandis are applicable to AY 2009-10 also. It is ordered accordingly.

I.T.A. No.3642/Mum/2016 - AY 2010-11

51. The grounds of appeal raised by the assessee in assessment year 2010-11 are tabulated in the earlier part of this order, from which it is clear that all the issues arising in AY 2010-11 are similar to AY 2008-09 except Depreciation on UPS (Ground No.2) and Disallowance for excess depreciation claim on assets eligible for 100% depreciation (Ground No.8). Considering the fact that the facts being identical our decision with respect to all the issued contended through Ground Nos.1 to 9 including additional ground except Ground no.2 & 8 are mutatis mutandis applicable to AY 2010-11 also. It is ordered accordingly. During the course of hearing, the ld AR submitted that Ground No.8 is not pressed and hence the same is dismissed as not pressed.

DEPRECIATION ON UPS – Ground No.2

52. The Assessee bought UPS amounting to Rs. 30,63,800. These UPS were attached to computers and were meant for providing temporary power supply for running the computers uninterruptedly during the power cuts and it is capitalised

by Assessee as part of computers and claimed depreciation at the rate of 60%. The AO has calculated depreciation on UPS by applying general rate of 15% for plant and machinery and relying in the decision of ITAT Delhi, in case of Nestle India (111 TTJ 498). The CIT(A) has confirmed the disallowance.

53. The ld AR submitted that the UPS form an integral part of the overall computer system and it is not used as a standalone generator. The UPS don't merely ensure uninterrupted power supply to computer network, but more importantly, also regulated the flow of power to avoid any kind of damage to the computer network due to fluctuation in power. Therefore, UPS is a necessary part of computer system. Since UPS are necessary for proper and continuous functioning of computer, applying the 'functional test' the same were capitalized as part of computers and accordingly depreciation at the rate @ 60% as applicable to the computer was claimed. The ld AR relied on following case laws in this regard

(a) Pr.CIT v Goa Tourism Development Ltd. (2019) 102 taxmann.com 437
(b) Delhi High Court In Nestle India (2023) 153 taxmann.com 201
(c) CIT Vs Orient Ceramics &Inds Ltd (200 Taxman 64) (Del)
(d) CIT v. BSES Yamuna Power Ltd. [IT Appeal No. 1267, dated 31-8-2010 (Del HC)]
(e) Nokia India (P.) Ltd Vs CIT (52 SOT 103) (TDel)
(f) American Express Services India Ltd Vs DCIT (151 TTJ 743) (TDel),
(g) CIT v. Orient Ceramics & Industries Ltd. (200 Taxman 64) (Del)

54. The ld AR made a without prejudice submission assuming without admitting that UPS is not a part of computers / computer system but it is merely an electrical device which regulates electricity and acts as an alternate source of electricity in power cuts, then it should be eligible for depreciation at the rate of 100% as held

by the Hon'ble Mumbai Tribunal in case of Venture Infotech Global (P) Ltd (25 SOT 184) i.e. as per the entry appearing in Appendix I of the Income-tax Rules, 1962, item no. III (8)(ix)(E)(c).

55. We heard the ld DR. We have considered rival submissions and perused the material available on record. It is noticed, in the case of PCIT vs Goa Tourism Development Ltd. the Hon'ble Jurisdictional High court has held that UPS being a part/accessory of computer is eligible for depreciation at 60%. The same view has been expressed by the Hon'ble Delhi High court in case of CIT vs Orient Ceramics and Industries Ltd. In view of the ratio laid down in the judicial precedents referred to above, we allow assessee's claim of depreciation on UPS @ 60%. This ground is allowed.

56. In result appeal for AY 2010-11 is partly allowed.

I.T.A. No.4562/Mum/2017 - AY 2011-12

57. The grounds of appeal raised by the assessee in assessment year 2011-12 are tabulated in the earlier part of this order, from which it is clear that all the issues arising in AY 2011-12 are similar to AY 2008-09 except Depreciation on UPS (Ground No.2) which is considered while adjudicating the appeal of AY 2010-11. The fact that the facts and circumstances being identical our decision in AY 2008-09 & AY 2010-11 with respect to all the issued contended through Ground Nos.1 to 8 including additional ground are mutatis mutandis applicable to AY 2011-12 also. It is ordered accordingly.

I.T.A. No.4607/Mum/2017 - AY 2011-12 (Revenue Appeal)

TP ADJUSTMENT TOWARDS SALE OF GOODS TO AE – Ground No.1&2

58. During the year under consideration the assessee exported manufactured water based paints name "Acrylic CED Shd-40 Black Resin Emulsion" to its AE in Philippines namely Kansai Paint Philippines Inc for Rs.64,41,030 based on the request of the said AE. The benchmarking analysis done by the assessee for this transaction comparing the contribution margin (Sale minus Direct costs) in respect of same type of products and service sold to non-AEs with the contribution margin of sale made to AE. The ALP of the said transaction was calculated by the assessee at Rs.23,48,458/- using TNMM method and the assessee accordingly made a TP adjustment of Rs.7,51,800/- as tabulated below –

Customer and Product	**Volume**	**Sales Proceed**	**Cost**	**Cont.**	**Cont.**
	(Lt/Kg)	**Rs.**	**Rs.**	**Rs.**	**%**
Honda Motor Cycles & Scooters	121430	24345416	15302569	9042846	37.14%
Jai Bharat Maruti Ltd.	13200	2693526	1729762	963763	35.78
				Average Margin	**36.46**

Sr.	**Particulars**	**Actual Contribution**	**Average on uncontrolled Transactions**	**ALP Contribution**	**Difference in contribution**
		Rs.	**%**	**Rs.**	**Rs.**
1.	Kansai Paint Philippines Inc.	15,96,658	36.46	23,48,458	**7,51,800**

59. The TPO did not accept the benchmarking done by the assessee and held that TNMM cannot be accepted as most appropriate method. The TPO proceeded to apply CUP method and arrived at an additional TP adjustment of Rs.17,57,731/-

60. Aggrieved the assessee filed the appeal before the CIT(A). The assessee submitted before the CIT(A) that the same in the domestic market and export sales stand in different footings and the circumstances, functions performed, risk assumed, terms and conditions of sales are different for export and domestic sale are different even if the same product is sold in both the markets. The assessee further submitted that in the absence of any export of the same product to non-AE, it is not appropriate to use CUP method. The assessee also submitted that the average contribution margin earned by the assessee in the domestic market on sale of the products to non-AE is a good profit level indicator (PLI) for calculating the ALP for export of the same products to AE and that TNMM is the most appropriate method to be applied in this case

61. The CIT(A) deleted the further TP adjustment made by the TPO by holding that –

"10. ***Decision:***

I have considered the fact of the case and the observations of the AO, It is important to analyze the stands of the AO vis a vis submissions of the appellant and the same is discussed herein below:

The question herein before me is whether the Assessing Officer is correct in making adjustment by disregarding the TNMM method adopted by the assessee and adopting CUP Method for determining the arm's length price for export of paints to AE in the absence of any comparable transaction of export to Non-AE. The appellant submitted before me that

the circumstances, functions performed, assets used, risked assumed e.g. foreign currency risk and terms and conditions e.g. credit period of exports sales and domestic sales are different, even if the same product is sold in both the markets. Use of CUP method by simply comparing the sales prices of export sales and domestic sales without taking into account various points of differences between export and domestic sale is not justified. Therefore, Average contribution margin earned by the appellant in the domestic market on sale of product to non-AEs is a good profit level indicator for calculating the ALP for export of the same product to AE and therefore TNMM is a most appropriate method.

The AO on the other hand has simply adopted the average sales price of the said product sold in the domestic market as Arms Length price for export to AE without taking into account differences in both the types of sales or without making any adjustments to the domestic price.

> *The concept of TP cannot be that of an exact science and that constant application of mind has to occur to determine whether a transaction is at ALP or not. Considering, in the given circumstances comparing average contribution margin earned by the appellant in the domestic market on sale of product to non-AEs is a good profit level indicator for calculating the ALP for export of the same product to AE, which will take care of all the differences in the circumstances, functions performed, assets used, risked assumed and other terms and conditions of the sales. Therefore TNMM can be considered as the most appropriate in the given case. Adopting CUP method, will involved lot of subjectivity in assigning values to the various differences and arriving at the comparable price.*

Accordingly, the action of TPO in applying CUP method is not justifiable. As pointed out correctly by the appellant before me instead of making adjustments to the price charged to the non-AE in the domestic market on account of various differences, which will involved lots of subjectivity, to arrive at the Arms Length Price, it is most appropriate to compare average contribution margin earned by the appellant in the domestic market on sale of product to non-AEs is a good profit level indicator to take care of all differences, therefore TNMM is the most appropriate method to be worked out the ALP.

As per the discussions above, the adjustment of Rs. 17,57,731/- made by the appellant by adopting TNMM method for calculating the ALP of the transaction in the return of income is appropriate and justified and therefore adjustment made by the TPO by adopting CUP method is deleted.

In view of this, this ground of appeal is allowed."

62. The ld DR submitted that the TPO has correctly applied CUP method and accordingly supported the order of the TPO. The ld AR on the other hand reiterated the submissions made before the CIT(A) and prayed that the decision of the CIT(A) be upheld.

63. We heard the parties and perused the material on record. The assessee has exported the water based paints to its AE in Philippines and benchmarked the same by applying TNMM method. Average contribution margin is used as the PLI. The TPO rejected the bench marking and applied CUP to make an additional TP adjustment. The TPO has used the same comparables used by the assessee and compared the average rate per unit of domestic sales with the rate per unit charged to AE and accordingly arrived the additional TP adjustment. The argument of the ld AR is that the domestic pricing and export pricing cannot be compared as it is by applying CUP, since the FAR of both markets are different. In this regard we notice that a similar issue has been considered by the coordinate bench in the case of Dow Chemicals International (P) Ltd., vs DCIT [(2021) 126 Taxmann.com 312 (Mum-Trib)] where it has been held that –

"15. We have considered rival submissions in the light of decisions relied upon and perused the material on record. The basic dispute between the parties is with regard to the most appropriate method for benchmarking the export of finished goods to the AEs. While the assessee has applied TNMM on segmental basis, the Transfer Pricing Officer has applied CUP to

determine the arm's length price of the transaction. From the material placed on record, it is very much clear that the sales made to the non-AEs situated in India have been applied as CUP to determine the arm's length price of export made to the AEs. It is the case of the assessee that no comparable export sales to non- AEs are available to apply as CUP. The aforesaid factual position has not been controverted by the Revenue. Therefore, the moot point which arises for our consideration is, whether the domestic sales can be applied as CUP for determining the arm's length price of export sales. It is fairly well settled, CUP method requires strict comparability. It cannot be denied that the pricing of a product varies on the basis of geographical location. Thus, primarily, the price of products sold in domestic market cannot be compared with the price of the product sold in foreign country due to various factors. Therefore, if the Transfer Pricing Officer selects CUP as the most appropriate method to benchmark the transaction, it is his duty to find out and bring on record price charged for uncontrolled transactions carried out under similar circumstances. If, suitable comparable uncontrolled transaction is unavailable, CUP method cannot be applied."

64. In assessee's case we notice that the TPO has made a direct comparison without making any adjustments to the domestic price charged for the similar product in a non-AE transaction. Applying the ratio laid down by the coordinate in the above decision in our considered view the TPO is not correct in applying CUP which requires strict comparability and given that the geographical location would have an impact on the pricing the bench marking done by the TPO is not tenable. Accordingly we see no infirmity in the decision of CIT(A) and uphold the decision of the CIT(A). This ground of the revenue is dismissed.

65. **Ground No.2** of the revenue pertains to CIT(A) deleting the addition made towards CENVAT credit to closing stock by the assessing officer. This issue is similar to Ground No.3 in assessee's appeal for AY 2008-09 where we have already remitted the issue back to the assessing officer. The facts of the issue under consideration being identical we remit the issue for AY 2011-12 also back to the

assessing officer with similar directions. This ground of the revenue is allowed for statistical purposes.

66. **Ground No 4 & 5** are general not warranting any separate adjudication.

67. In result the assessee's appeal for AY 2008-09 to 2011-12 and the revenue's appeal for AY 2011-12 are partly allowed.

Order pronounced in the open court on 04/12/2023

Sd/- **Sd/-**

(AMIT SHUKLA)	**PADMAVATHY S.**
JUDICIAL MEMBER	**ACCOUNTANT MEMBER**

Mumbai, Dt : 4th December, 2023

प्रतिलिपि अग्रेषितCopy of the Order forwarded to :

1. अपीलार्थी/The Assessee ,
2. प्रतिवादी /The Respondent.
3. आयकर आयुक्त CIT
4. विभागीय प्रतिनिधि ,आय.अपी.अधि ,.मुबंई/DR, ITAT, Mumbai
6. गार्ड फाइल/Guard file.

BY ORDER,

//True Copy//

Asstt. Registrar
ITAT, Mumbai