

IN THE INCOME TAX APPELLATE TRIBUNAL  
[ DELHI BENCH: 'I' NEW DELHI ]

BEFORE SHRI G. S. PANNU, VICE PRESIDENT  
AND  
SHRI YOGESH KUMAR U.S., JUDICIAL MEMBER

I.T.A. No. 9482/DEL/2019 (A.Y. 2015-16)

Samsung India Electronics Pvt. Ltd., 20 <sup>th</sup> to 24 <sup>th</sup> Floor, Two Horizon Centre, Golf Course Road, Sector 43 DLF Phase-V, Gurgaon, Haryana - 122 002.  <b>PAN No. AAACS5123K</b>  <b>(APPELLANT)</b>	Vs.	DCIT, Circle : 22 (2), New Delhi - 110002     <b>(RESPONDENT)</b>
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Appellant by : S/Shri Himanshu S. Sinha & Bhuwan Dhoopar, Adv.

Respondent by : S/Shri Mahesh Shah, CIT(DR) & Kanv Bali, Sr. DR

Date of Hearing	03.05.2024
Date of Pronouncement	29.07.2024

**ORDER**

**PER YOGESH KUMAR U.S., JM**

The assessee has filed this appeal against the assessment order dated 20/11/2019 passed by Deputy Commissioner of Income Tax, Circle-22(2), New Delhi (hereinafter referred as "AO") u/s. 144C(13) of the Income Tax Act, 1961 (hereinafter referred as "Act"), which was issued in pursuance to the directions dated 23.09.2019 issued by the Ld. Dispute Resolution Panel-1, New Delhi (hereinafter referred as "DRP"), pertaining to assessment year 2015-16.

2. The assessee, an Indian company, is a wholly owned subsidiary of the Korean conglomerate Samsung Electronics Co. Ltd and engaged in the business of manufacturing and trading of consumer electronics, home

appliances, mobile phones, and information technology products. It also carries out contract software development activities for its Korean parent and is also engaged in trading of telecommunication networking equipment whereby network equipment purchased from its Korean parent were sold to a 3<sup>rd</sup> party customer (Reliance) in India.

3. The assessee filed its return of income for the AY 2015-16 on 29.10.2015 declaring an income of Rs. 2415,02,39,200/- through e-filing mode and also filed its revised Income Tax Return on 14.03.2017 keeping the same income at Rs. 2415,02,39,200. The case of the assessee was selected under limited scrutiny and notice u/s. 143(2) was issued on 21.6.2016 and another notice u/s. 143(2) was issued on 27.7.2016. A detailed questionnaire alongwith notice u/s. 142(1) of the Act was issued on 27.9.2016. The AO initiated scrutiny proceedings under section 143(2) of the Act and referred the case to the Transfer Pricing Officer (hereinafter referred as "TPO") u/s. 92CA of the Act for the examination of the arm's length price of its various international transactions.

4. The TPO in her order dated 31.10.2018 passed u/s 92CA(3) of the Act proposed adjustments under the following heads: (a) Advertisement, Marketing and Promotion (AMP) expenses; and (b) International transactions in the trading, manufacturing and networking segments. These adjustments were adopted by the AO in her draft assessment order dated 28.12.2018 issued u/s. 144C(1) of the Act. Besides these, the AO proposed following additions: (a) disallowance of salary expenditure incurred on expatriate employees on secondment; and (b) disallowance of royalty paid to the parent entity.

5. The assessee filed objections against the aforesaid proposed adjustments and disallowances before the Ld. DRP-1, New Delhi which were examined and disposed of vide DRP's order dated 23/09/2019. Thereafter the AO has issued the final assessment order on 20/11/2019. The final adjustments and additions made by the AO following the issuance of directions of the DRP are as under: (a) AMP expenditure incurred in manufacturing, trading and networking segments of the assessee - on substantive basis by applying the Transaction Net Margin Method (TNMM) and on protective basis applying the Bright Line Test (BLT); (b) Adjustments to the arm's length price of the international transactions in the (i) manufacturing; (ii) trading; and (iii) networking segments; (c) disallowance of royalty paid to the parent entity; and (d) disallowance of the salary expenditure pertaining to expatriate employees on secondment from the parent entity.

6. The assessee has challenged the aforesaid adjustments and disallowances made in the final assessment order by preferring the present appeal on the following Grounds of Appeal:-

**GROUND OF APPEAL**

- "1. That on the facts and circumstances of the case and in law, the Ld. AO has erred in assessing the total income of the Appellant at Rs.8155,44,45,700/- as against the returned income of Rs.2415,02,39,200/-.*
- 2. That on the facts and circumstances of the case and in law, the Ld. Dispute Resolution Panel ("DRP")/AO/Transfer Pricing Officer ("TPO") erred in making a transfer pricing adjustment of Rs. 5547,96,65,313/- on account of the following transactions: (i) advertising, marketing, promotion ("AMP") expenses amounting to Rs. 2310,30,56,382/- (ii) trading segment amounting to Rs. 250,89,73,885/-(iii) networking segment amounting to Rs. 978,46,08,952/-(iv) manufacturing segment amounting to Rs. 1105,54,54,842/- and (v) payment of royalty amounting to Rs.902,75,71,252/- alleging the same to be not at arm's length in terms of the provisions of section 92C of the Act read with Rule 10B of the Income Tax Rules, 1962 ("the Rules").*

3. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO erred in making an addition of Rs. 192,45,41,190/- on account of disallowance of salary expenditure incurred in relation to expatriate employees under section 37(1) of the Act.*

**GROUNDINGS AGAINST SUBSTANTIVE ADJUSTMENT MADE IN RELATION TO AMP EXPENSES**

4. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in making substantive adjustment of Rs. 2310,30,56,382/- on account of AMP which comprised of Rs. 1021,16,52,791/- for the Manufacturing Segment (Non-IT), Rs. 978,46,08,952/- for Networking Segment (Non-IT) and Rs.310,67,94,639/- for trading segment (Non-IT)*
5. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in holding that the AMP expenditure incurred by the Appellant in India is an 'international transaction' as per the provisions of the Act.*
6. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO erred in:*
  - a. *not demonstrating the existence of an 'understanding' or an 'arrangement or 'action in concert' between the Appellant and its Associated Enterprises (AEs) w.r.t. the AMP spend; and*
  - b. *not appreciating that the AMP expenses incurred by the Appellant are wholly and exclusively focused on generating domestic sales for its own business operations (and aligned with the risk profile of the Appellant) and the benefit arising from the incurrence of the AMP expenses by the Appellant has been received by the Appellant and the benefit, if any, resulting to its AEs is merely incidental.*
7. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO erred in holding that the AMP expenses incurred by Appellant has led to the creation of marketing intangibles and resulted in promotion of 'Samsung Brand' for which the Appellant should be compensated by the legal owner of the brand.*
8. *That on the facts and circumstances of the case and in law, the Ld. DRP/ AO/ TPO have erred in adopting intensity-based approach which is not a prescribed method under the Income-tax Rules, 1962.*
9. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO erred in applying mark-up on the alleged incurred excessive AMP expenditure by selecting companies providing market support functions in order to determine the mark-up to be imputed on AMP adjustment.*
10. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO failed to appreciate that artificially making duplicative adjustments on account of AMP is perverse and contrary to law as the alleged AMP expenses and AMP activities for the trading segment, manufacturing segment and networking segment are already included in the arm's length determination of the trading segment, manufacturing segment and networking segment.*
11. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in not appreciating that after application of Transactional Net Margin Method ("TNMM") as the Most Appropriate Method ("MAM") for benchmarking the international transactions, no separate arm's length analysis was required in respect of the individual elements of cost (AMP expenditure) as it is inconsistent with the tenets of applications of TNMM as per Rule 10B(1)(e) of the Rules.*

12. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in making transfer pricing adjustment on account of AMP expenditure in networking segment ignoring the fact that under networking segment, the Appellant operates under a Business-to-Business ('B2B') model wherein the it caters to a single customer and does not undertake any activity pertaining to AMP.*
13. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in considering all 'value added expenses' (excluding employee costs) as part of the AMP expenditure on the premise that all value-added expenses lead to promotion of the brand 'Samsung' disregarding the fact that many of such expenses are purely operational in nature.*
14. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in not allowing the exclusion of sales related expenses from the ambit of AMP disregarding the fact that exclusion of such expenses has been allowed in Appellant's own case by DRP in prior years.*
15. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO erred in modifying the comparable set, in contravention of section 92C(3) of the Act read with Rule 10B(2) of the Rules, by including/selecting companies that are not comparable to the Appellant in terms of functions performed, assets employed, risks assumed and rejecting companies selected by the Appellant.*
16. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO erred in incorrectly computing margin of the Appellant and the comparables.*

**GROUNDINGS AGAINST PROTECTIVE ADJUSTMENT MADE IN RELATION TO AMP EXPENSES UNDER BRIGHT LINE TEST METHOD**

17. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in making protective adjustment of Rs. 2169,56,70,875/- on account of AMP which comprised of Rs. 1673,50,85,621/- for Manufacturing Segment and Rs 496,05,85,254/- for Trading Segment which is impermissible under law.*
18. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in making protective adjustment when substantive adjustment has already been done in the hands of the same Assessee for same assessment year, which is impermissible under law.*
19. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred applying the 'bright line' test as a tool to identify and benchmark the alleged AMP transaction which has no statutory mandate under the Act as laid down by the Hon'ble Delhi HC in the case of Sony Ericson Mobile Communications India Pvt. Ltd. [2015] 374 ITR 118 (Delhi).*
20. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in levying a further mark up on the alleged AMP expenses incurred over and above the so-called 'bright-line' limit, stating that it tantamount to services being provided by Appellant to its AEs.*

**GROUNDINGS AGAINST SUBSTANTIVE ADJUSTMENT MADE UNDER TNMM IN THE TRADING SEGMENT, MANUFACTURING SEGMENT AND NETWORKING SEGMENT**

21. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in making an adjustment of Rs. 250,89,73,885/- in trading segment by rejecting Resale Price Method applied by the Assessee and instead applying TNMM as the MAM and by including companies that are not comparable to the Assessee in*

*terms of functions performed, assets employed, risks assumed, and rejecting comparable companies selected by the Assessee.*

22. *That on the facts and circumstances of the case and in law, the Ld. AO/TPO have erred in making the adjustments in networking segment and manufacturing segment as substantive adjustments in the final assessment order and order giving effect to the DRP directions despite the fact that the said adjustments were made as protective adjustments in the TPO Order and there is no direction of the DRP to make the said adjustments as substantive adjustments.*
23. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in making an adjustment of Rs. 978,46,08,952/- in networking segment under TNMM by including companies that are not comparable to the Assessee in terms of functions performed, assets employed, risks assumed, and rejecting comparable companies selected by the Assessee.*
24. *That on the facts and circumstances of the case and in law, the Ld. TPO erred in making an adjustment of Rs. 1105,54,54,842/- in Manufacturing Segment under TNMM by including companies that are not comparable to the Assessee in terms of functions performed, assets employed, risks assumed, and rejecting comparable companies selected by the Assessee.*
25. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in incorrectly computing the margin of the Assessee and the comparables for all the three segments i.e. trading segment, manufacturing segment and networking segment.*
26. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO erred in considering the foreign exchange gain as non-operating in nature for the purpose of computation of margins of the Appellant as well as of the comparables.*
27. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in denying working capital adjustment under Rule 10B(l)(e) for the purpose of determination of ALP to account for the difference in working capital employed by the Assessee vis-a-vis the comparable companies by ignoring the fact that working capital adjustment was allowed by Ld. TPO in AY 2005-06, 2006-07, AY 2010-11 and 2011-12 and by Hon'ble DRP in AY 2013-14.*
28. *That on the facts and circumstances of the case and in law, the Ld. DRP/ TPO/AO erred in wrongfully computing proportionate adjustment.*

#### **GROUND'S AGAINST ROYALTY ADJUSTMENT**

29. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO have erred in making an adjustment of Rs. 902,75,71,252/- on account of royalty payment by rejecting TNMM applied by the Assessee and instead applying CUP as the MAM.*
30. *That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO erred in not appreciating the fact that payment of royalty is intrinsically linked with the manufacturing activity, thus segregating and benchmarking the transaction of royalty is in violation of transfer pricing provisions.*
31. *That on the facts and circumstances of the case and in law, the Ld. DRP erred in directing the TPO to carry out a transfer pricing adjustment of the transaction of payment of royalty without appreciating the fact that TPO during transfer pricing assessment proceedings had carried out benchmarking analysis of royalty and no adverse inference was drawn in the TP order.*

32. That on the facts and circumstances of the case and in law, the Ld. DRP/AO/TPO erred in modifying the comparable set, in contravention of section 92C(3) of the Act read with Rule 10B(2) of the Rules, by including/selecting companies that are not comparable to the Appellant in terms of functions performed, assets employed, risks assumed.

**GROUNDINGS AGAINST CORPORATE TAX ADJUSTMENT**

33. That on the facts and circumstances of the case and in law, the Ld. DRP /AO erred in disallowing the salary expenditure of INR 192,45,41,190/- incurred in relation to expatriate employees under section 37(1) of the Act ignoring the fact that this Hon'ble Tribunal has decided the issue in favour of the Appellant in the case of Samsung Electronics Co. Ltd v DCIT: [2018] 92 taxmann.com 171 (Delhi - Trib.).

34. That on the facts and circumstances of the case and in law the Ld. DRP /AO in holding that there was no employer-employee relationship between expatriate employees and the Appellant and the expatriate employees were the employees of the parent company, i.e., Samsung Electronics Co. Limited

35. That on the facts and circumstances of the case and in law the Ld. DRP /AO erred in holding that expatriate employees were not working wholly and exclusively for the business of the Assessee and accordingly, their salary expenditure is disallowable under section 37( 1) of the Act.

36. That on the facts and circumstances of the case and in law, the AO has erred in charging interest under Sections 234A and 234B of the Act.

37. That on the facts and circumstances of the case and in law, the AO erred in initiating penalty proceedings under Section 271(l)(c) and Section 271 BA and Section 271AA of the Act for furnishing of Inaccurate particulars and concealment of income."

7. For the sake of convenience, we are dealing with the aforesaid grounds of appeal by clubbing them under the following six issues:-

- i. Adjustment made to the arm's length price of the AMP expenditure by treating the same as an international transaction with its parent;
- ii. Adjustment made to the arm's length price of the international transactions in Trading segment;
- iii. Adjustment made to the arm's length price of international transactions in Networking segment;
- iv. Adjustment made to the arm's length price of international transactions in Manufacturing segment;
- v. Disallowance of a part of the royalty payment made to the parent by treating the same as excessive and unreasonable; and

- vi. Disallowance of salary paid to expatriate employees on secondment from Korea.

8. Grounds 1 and 2 being general are being adjudicated with other grounds. Ground no. 3 is on issue no. vi. and is being dealt later. Grounds 4 to 20 pertain to the first issue of transfer pricing adjustment made to the international transaction of AMP Expenditure incurred by the assessee. Whereas, the assessee has declared a small amount of Rs. 5.5 crore as reimbursement received from its parent Samsung Electronics Co. Ltd., Korea on account of certain marketing expenses as an international transaction eligible for a cost to cost recharge, the TPO has treated the entire amount of AMP expenditure incurred by the assessee in its manufacturing, trading and networking segments as international transactions of intra-group service rendered by the assessee to its parent for the promotion of the brand 'Samsung' leading to a substantive adjustment of Rs. 2013,99,22,624/- and a protective adjustment of Rs. 2083,75,34,081/-. This issue has been recurrent for the last several years and the TPO, DRP and the Tribunal have been consistent in their approaches. The TPO and the DRP have all along held that the assessee is incurring "excessive" AMP expenditure as compared to other independent and uncontrolled comparable Indian companies (referred to as the Bright Line). This "excessive" expenditure incurred by the assessee is primarily for the promotion of the brand 'Samsung' and since the brand is owned by the assessee's Korean parent Samsung Electronics Co Ltd., the "excess" AMP expenditure above the Bright Line should be treated as a separate international transaction of brand-promotion service. Applying this Bright Line Test, the TPO and the DRP have held that the excess amount alongwith

an arm's length mark-up (profit that comparable service companies would earn) should be treated as the arm's length price of this international transaction. However, since this Bright Line Test has been held to be illegal and untenable by the Hon'ble Delhi High Court in Sony Ericsson Mobile Communications v. CIT (2015) 374 ITR 118 (Delhi) and this order of the High Court is in appeal before the Hon'ble Supreme Court by way of a Special Leave Petition, the TPO, DRP and AO have kept the adjustment on protective basis.

9. On the other hand, while dealing with this issue on "substantive" basis, the TPO and the DRP have adopted an alternative way of determination of arm's length price of the international transaction of the AMP expenditure. This approach was adopted in earlier years as well and has been referred to as Transaction Net Margin Method (TNMM) intensity-based approach. The excessive nature of AMP expenditure, in TPO's view, results in much higher intensity of functions reflected in the higher levels of operating expenditure vis-a-vis the companies that are taken to be comparable under TNMM, and hence requires economic adjustment. This adjustment has been carried out by increasing the profit margins of the comparables in all the three segments - Trading, Manufacturing and Networking. This approach of the TPO has been approved by the DRP subject to certain minor modifications regarding choice of certain comparables resulting in the impugned adjustment on substantive basis.

10. Ld. Counsel for the assessee, at the outset submitted that this issue being recurrent in nature has come up in each of the ten prior assessment years and has been decided in its favour in all these prior assessment years

(A.Ys 2005-06 to 2014-15). Taking us through the orders of the Coordinate Benches in the prior years, he pointed out that the Tribunal has consistently held that TPO and the DRP did not have any basis to conclude that there is an understanding, arrangement or action in concert between the assessee and the associated enterprise (AE) to incur "excessive" level of AMP expenditure with a view to benefit the "Samsung" brand beyond what was necessitated by its local Indian requirements. In the past years, the assessee has consistently disclosed a limited amount received as reimbursement from its AE as marketing support grant under an agreement referred to as Marketing Development Fund (MDF) agreement. Under this agreement, the AE would pre-approve certain marketing costs purely in its discretion as reimbursement for the assessee to support its marketing function in Indian market for Samsung products. It was pointed out that during this year this amount has been much lower and has been paid under an identical arrangement of pre-approval but without any MDF agreement. This reimbursement on cost-to-cost basis has been consistently disclosed as an international transaction by the appellant in its Form 3CEB and transfer pricing report under Rule 10D. The TPO, however, has expanded the scope of the international transaction arbitrarily by referring to an unjustifiable allegation of "excessive" AMP expenditure.

11. It was further submitted that based on the decisions of the Hon'ble Delhi High Court in Maruti Suzuki (2015) 381 ITR 117 (Delhi); and Bausch & Lomb (2016) 381 ITR 227 (Delhi), the Tribunal in prior years has given a categorical finding that there is no basis to expand the ambit of international transaction pertaining to cost to cost reimbursement of

marketing expenses to a much larger "excessive" AMP expenditure. It was further submitted that once the existence of an international transaction is itself negated, there would be no question of determination of its arm's length price. As regards TNMM intensity approach, the Ld. AR submitted that the steps adopted to adjust for the higher intensity of marketing function are nothing but a disguised form of Bright Line Test. Further, there is no economic or logical justification in first increasing the cost base and then applying an artificial profit margin of marketing and advertising companies on the artificially enhanced cost base. Such a method has not basis in rules.

12. On the other hand, Ld. CIT(DR) countered the arguments and contentions raised by the assessee's AR. He submitted that though the Tribunal has decided this issue in favour of the assessee in prior years, principle of *res-judicata* does not apply to income tax proceedings and each assessment year is to be judged on its own basis. Unlike preceding years, there is no MDF agreement this year and the fact that the assessee itself has accepted that the reported transaction of reimbursement of marketing expenses of Rs. 5,51,13,066/- is an international transaction demonstrates that there is an arrangement between the assessee and its parent that brand promotion service would be provided by incurring AMP expenditure in India. He further submitted that though MDF agreement is not present in the current year, the MDF agreement of the prior years provided for an arrangement whereby the assessee and the AE had agreed that the assessee would incur AMP expenditure to promote the "Samsung" brand owned by the parent. He placed reliance on the Hon'ble Delhi High Court

decision of Sony Ericsson Mobile Communications (supra) to contend that the Court had approved application of intensity type of adjustments in suitable cases. In the present case, since the Bright Line Test could not be applied as the court has held it to be untenable, a modified version of TNMM intensity approach could justifiably be used as a "substantive" adjustment till such time the Supreme Court decides the fate of the Bright Line Test in the pending special leave petitions.

13. We have given our anxious consideration to the issue at hand and the rival contentions and arguments along with the material on record. In our considered view, the issue whether AMP is an international transaction in respect of the assessee is no longer *res integra qua* the assessee, since Coordinate Benches of this Tribunal in ten prior assessment years have consistently held that AMP expenditure incurred by the assessee could be treated as an international transaction only to the extent of what has been agreed with its associated enterprises to be reimbursed. Any amount beyond such agreed reimbursements do not warrant inclusion within the ambit of the international transaction as these expenses have not been necessitated by any understanding, arrangement, or agreement with the AEs. In the absence of any evidence of this common understanding or action in concert, any such conclusion would be a mere surmise.

14. During the instant year, we find that not only there was no MDF agreement in effect between the assessee and the AE, the amount of reimbursement of marketing expenses received by the assessee has diminished to a meagre sum of Rs. 5,51,13,066/. However, the TPO and the DRP have proceeded on an assumption that there was an

understanding between the assessee and its AE that "excessive" AMP expenditure would be incurred in India to promote the 'Samsung' brand in a manner that was not justified by the scale and nature of Indian business but at the behest and requirement of the foreign parent that owned the brand. We do not find any merit in the approach taken by the TPO and the DRP as well the contention raised by the Ld. CIT(DR) that consistency of approach by the Tribunal should be disregarded. The Transfer Pricing Report of the assessee states very clearly in Para 4.4.3 that the reimbursement of marketing expenses of the assessee is strictly limited to those items for which prior approval is received from the AE and consequently there is no element of service to the AE. The reimbursement is restricted to the actual expense without any mark-up as per the prior approval granted by the AE. In the prior years, the Tribunal had found that identical system of reimbursements was adopted. Accordingly, even without any express MDF agreement, the assessee and its AE have been consistently following the same approach over the years.

15. Since it has consistently been held that the scope of international transaction pertaining to AMP expenses cannot be expanded beyond what has already been disclosed by the assessee in its transfer pricing report and Form 3CEB, any adjustment either by way of Bright Line Test or intensity based TNMM approach is not tenable in law. Reliance placed on Sony Ericsson Mobile Communications India Pvt. Ltd. v. CIT (2015) 374 ITR 118 (Del) by the Ld. CIT(DR) to justify the TNMM intensity-based approach is wholly misplaced. The justification of adoption of a method can be examined only after the issue of existence of an international transaction is

established. If no international transaction is found to exist, the occasion to select the most appropriate method to determine the arm's length price would not arise at all.

16. The finding of the Coordinate Benches in ten prior assessment years that the AMP expenditure could not be treated as an international transaction in the absence of any evidence or material to demonstrate an understanding, arrangement, or action in concert between the assessee and its AE is based on the principles laid down in the subsequent decisions of the Hon'ble Delhi High Court in Maruti Suzuki (2015) 381 ITR 117 (Delhi) and Bausch & Lomb Eyecare (India) (2016) 381 ITR 227 (Delhi). In these decisions their Lordships have observed that in Sony Ericsson (supra), the existence of an international transaction was not in issue. The following extract from the Maruti Suzuki (supra) makes this amply clear:

*"..43. Secondly, the cases which were disposed of by the Sony Ericsson Mobile Communications India (P.) Ltd. (supra) judgment, i.e. of the three Assesseees Canon, Reebok and Sony Ericsson were all of distributors of products manufactured by foreign AEs. The said Assesseees were themselves not manufacturers. In any event, none of them appeared to have questioned the existence of an international transaction involving the concerned foreign AE. It was also not disputed that the said international transaction of incurring of AMP expenses could be made subject matter of transfer pricing adjustment in terms of Section 92 of the Act.*

*44. However, in the present appeals, the very existence of an international transaction is in issue. The specific case of MSIL is that the Revenue has failed to show the existence any agreement, understanding or arrangement between MSIL and SMC regarding the AMP spend of MSIL. It is pointed out that the BLT has been applied to the AMP spend by MSIL to (a) deduce the existence of an international transaction involving SMC and (b) to make a quantitative 'adjustment' to the ALP to the extent that the expenditure exceeds the expenditure by comparable entities. It is submitted that with the decision in Sony Ericsson Mobile Communications India (P.) Ltd. (supra) having disapproved of BLT as a legitimate means of determining the ALP*

*of an international transaction involving AMP expenses, the very basis of the Revenue's case is negated.*

*45. Since none of the above issues that arise in the present appeals were contested by the Assessee who appeals were decided in the Sony Ericsson Mobile Communications India (P.) Ltd. case (supra), it cannot be said that the decision in Sony Ericsson Mobile Communications India (P.) Ltd. (supra), to the extent it affirms the existence of an international transaction on account of the incurring of the AMP expenses, decided that issue in the appeals of MSIL as well..."*

16.1 In the instant case, therefore, where the assessee does not accept the existence of any such transaction, the onus is on the TPO to bring evidence and material on record to rebut the assessee's position. From the facts on record, it is manifest that the Revenue's position is not backed by any evidence that the assessee had agreed either explicitly or implicitly to incur any AMP expenditure on behalf of the parent company. There is no material that would show that the assessee's advertising and marketing budget was finalised or determined at the behest of the parent entity.

17. The relevant paragraphs of the Coordinate Bench decisions in the assessee's appeals on this issue in prior assessment years reproduced below manifest the position of this Tribunal that has been consistently taken over the past ten assessment years:

ITA Nos. 3248 & 3410/Del/2012; 5856/Del/2010; 5315/Del/2011; 52/Del/2013; 1567/Del/2014; 6741/Del/2014; 868/Del/2016; 251/Del/2018 (AYs 2005-06 to AY 2011-12) vide a combined order dated 4.10.2019

*"43. In the present case we find that the Revenue has not been able to place any material to record to show or suggest that the Appellant's AMP activity was carried out at the behest of its AE, beyond what was approved and reimbursed under the MDF Agreement. No understanding or arrangement or "action in concert" can be inferred from the terms of the MDF agreement or the conduct of the appellant to show that "excessive" AMP expenditure has been incurred at the behest of the brand-owing AE. The*

*appellant being one of the major players in the Indian market has carried out its AMP activity and function based on its own judgement and commercial realities. Revenue has not placed any material or evidence to show that there existed an understanding to incur "excessive" AMP expenditure. The arrangement and understanding were limited to the amounts agreed to be paid as assistance under the MDF Agreement. The amounts incurred as AMP expenditure by the appellant under the MDF Agreement have already been received as reimbursement/assistance and have indisputably been disclosed as an international transaction in Form 3CEB and form part of the transfer pricing study conducted under Rule 10D. The AMP expenditure which is outside the ambit of reimbursement received under the MDF Agreement, has been incurred by the appellant on its own volition as per its own requirements and without any interference of the AE and have been paid to third parties.*

44. *In view of the above, we hold that the scope and value of international transaction cannot be expanded beyond the reimbursements received under MDF agreement to cover the entire gamut of AMP expenditure incurred by the Appellant during the year.*
45. *In view of the above, we hold that the "bright line" approach is untenable in law either as a way to determine the existence of an international transaction or as a method to determine the ALP of an international transaction pertaining to AMP. No international transaction can be presumed to exist merely on the basis of "bright line" of expenditure incurred by comparable companies."*

ITA No. 6813/Del/2017 (AY 2012-13) vide order 7.01.2020

- "6. *Heard the arguments of both the parties and perused the material available on record. This matter stands adjudicated by the Co-ordinate Bench of /TAT wherein it was held that the scope and value of the International Transaction cannot be expanded beyond the reimbursement received under MDF agreement to cover the entire gamut of AMP expenditure incurred by the Appellant during the year.*
7. *Regarding the applicability of the Bright Line Text (BLT) (specific grounds at 11, 12 & 13) to determined the adjustment in the AMP expenditure has been rejected by the Hon'ble Jurisdictional High Court in the case of Sony Ericsson Mobile Communication India Pvt. Ltd. in Tax Appeal No. 16 of 2014. In view of the judgement of the Hon'ble High Court, we hereby hold that no International Transaction can be presumed to be in existence and hence no addition is called for."*

ITA No. 7285/Del/2018 (AY 2013-14) vide order dated 14.12.2020

*" 8.... Thus, the entire issue relating to AMP raised in the present assessment year is identical to that of earlier year as well as subsequent year and there is no different facts emerging either from the order of the TPO or from the perusal of the record. Therefore, Ground Nos. 3 to 15 are allowed. "*

ITA no. 9481/Del/2019 (AY 2014-15) vide order 31.08.2020

*"18. So, in view of what has been discussed above, we are of the considered view that merely by applying the BIT method which has no legal existence and merely on the basis of MDF agreement vide which taxpayer has received part reimbursement of the AMP expenses incurred by it duly disclosed this expenditure in Form 3CEB and in TP study, so called excessive AMP expenditure of the taxpayer cannot be treated as international transactions u/s 92B of the Act. So, we cannot infer the existence of international transactions qua AMP expenses between taxpayer and AE beyond the reimbursement already made by the AE under MDF Agreement. ..*

*24. Id. TPO by adopting the intensity approach qua trading segment and network segment proceeded to make alternative benchmarking as a substantive adjustment. In AY 2012-13, similar adjustment was made by the Id. TPO by adopting the intensity approach which was held not to be sustainable by the coordinate Bench of the Tribunal in ITA No.6813/Del/2017 for AY 2012-13 order dated 07.01.2020 in taxpayer's own case by following the order passed by the coordinate Bench of the Tribunal in taxpayer's own case in earlier years.*

*25. So, in view of what has been discussed above and by following the aforesaid order passed by the coordinate Bench of the Tribunal, we are of the considered view that scope and value of the international transactions cannot be extended to the so called excessive expenditure incurred by the taxpayer on account of non-routine AMP beyond the reimbursement already received by the taxpayer under MDF agreement and as such, adjustment made by the TPO on account of AMP expenses is not sustainable in the eyes of law, hence, ordered to be deleted."*

17.1 Following the aforesaid decisions rendered by various Coordinate Benches in ten prior assessment years on this issue, we hold that the transfer pricing adjustments to the arm's length price of the alleged international transaction of AMP expenditure of the appellant is bad in law and liable to be deleted. Grounds 4 to 20 are accordingly allowed.

18. The next issue is in respect of the adjustment of Rs. 250,89,73,885/- made by the TPO to the arm's length price of the international transactions in the Trading segment under TNMM by altering the set of comparable companies. In Ground no. 21 the assessee has contested the erroneous inclusion of three companies as comparables. The relevant facts pertaining to the trading segment are as follows: in this segment the company's business comprises of distribution of consumer electronics, home appliances, mobile phones, IT product and medical equipment. The main international transactions in this segment are purchase of finished goods, software, stores and service spares, besides other ancillary transactions of sale of stores and service spares and provision of after sales support services. To determine the arm's length price of these transactions, the assessee has chosen Resale Price Method (RPM) as the most appropriate method and has aggregated all the transactions to determine the gross profit margin of the segment at 17.40%.

The economic analysis carried out on the database showed 12 uncontrolled independent comparable companies whose mean gross profit margin came to 3.92%. Since the gross profit margin of the appellant in the trading segment was higher at 17.40%, it was concluded that the international transactions in this segment were at arm's length.

19. The TPO recomputed the arm's length price by applying TNMM as the most appropriate method and rejecting the RPM method applied by the appellant in its transfer pricing study. The TPO rejected 9 out of 12 comparables taken by Applicant and introduced 5 new comparables and arrived at a final set of 8 comparables with a median operating profit on revenues (OP/OR) of 5.01% (35th percentile of 2.74% and 65th percentile of 5.78%). The TPO also recomputed the operating margin of the Applicant at (-)1.83% as against 0.94% as submitted by the appellant during the assessment proceedings.

20. The Ld. DRP upheld the order of the TPO regarding the addition made in the trading segment except for allowing the objection of the assessee regarding inclusion of 2 comparables selected by the appellant in its TP study namely Redington India Ltd and Ingram Micro India Limited and exclusion of 2 comparables, namely. Micromax Infomatics Ltd, and United Telelinks (Bangalore) Pvt. Ltd. As a result, the final set comprised of 8 comparables

with a median OP/OR of 2.74% (35<sup>th</sup> percentile of 1.92% and 65th percentile 3.53%).

21. The assessee is aggrieved by the inclusion of three comparable companies, namely OTS E-Solutions Pvt. Limited, Virtual Netcom Pvt. Limited, and Sataytej Commercial Co. Limited.

22. OTS E-Solutions Pvt. Ltd: The TPO has observed that this comparable has been included since it is engaged in trading activities and does not own any intangible related to online portal. On objections being filed by the assessee, Ld. DRP did not give any finding on the inclusion/exclusion of this comparable. The Ld. AR submitted that this comparable company has been rejected by this Tribunal in assessee's appeals for AYrs. 2013-14 and 2014-15 on the ground of functional dissimilarity. This company is engaged in providing an online marketing platform by the name 'GadgetGuru' for sale of electronic products. It acts as an aggregator in the online marketing space. Taking us through the relevant pages of the Paper Book, the Ld. AR submitted that the company sells electronic products of various brands on its online platform, hence, it is not a 'Sole-Selling Agent' of any brand, whereas the assessee is the sole seller of Samsung goods in India. The Ld. AR further submitted that OTS E-Solutions is a routine distributor and does not perform critical functions such as quality control and post-sale/ warranty support unlike the assessee which performs other functions as well, making it functionally dissimilar to the assessee.

23. On the other hand, Ld. CIT(DR) submitted that this company is engaged in the distribution of consumer electronic products like mobile phones, air-conditioners, refrigerators etc. similar to the business of the appellant in the distribution segment. Merely because the company deals with consumer products of different brands and uses an online portal to sell the products, it cannot be rejected as a valid comparable. Moreover, since the TPO has applied TNMM as the most appropriate method to benchmark the trading segment which allows some flexibility in terms of the functional and product profile of the comparable companies, OTS E-solutions should be included as a comparable.

24. Upon perusal of the relevant Annual Report of this company, we find

that its business model remains unchanged. It is an e-retailer that provides an electronic platform called 'GadgetGuru' for various sellers to sell their electronic goods (consumer electronics and home appliances) to retail customers. The goods are sold by the companies like Whirlpool India, Amazon Seller Services Pvt. Ltd, Flipkart, Snapdeal etc. In fact the balance sheet of the company for this year shows that Samsung India Electronics Pvt Ltd (appellant) is also a debtor. It is quite clear that companies like Samsung and Whirlpool are directly selling their goods on this platform to retail customers. It is quite evident that the functions, assets and risks of this company are quite distinctive and dissimilar to those of the appellant. Whereas OTS E-Solutions does not bear any material risk of inventory or capital deployment as it does not own or stock any inventory but merely provides a platform for other companies to sell their products, companies like the appellant and Whirlpool buy and store their own branded goods. The position of the appellant in the supply chain is of a wholesale distributor as against OTS E-Solutions which is merely a e-retail platform. The warranty on the goods sold through the GadgetGuruplatform is not provided by OTS E-Solutions but by the respective seller like Whirlpool or Samsung. The TPO had included this comparable in A.Yr 2014-15 and the same was directed to be excluded by the Coordinate Bench in ITA No. 6813/Del/2017 by observing as under:

*"34. ..Keeping in view the fact that OTSE is a routine distributor/supply chain shows that the functions performed, risks assumed and expected reward is not comparable to the taxpayer. The taxpayer is also performing critical functions such as quality control and post sale warranty support as a routine distributor whereas OTSE being an aggregator provides a platform for sale of electronic products of multiple brands and as such having a different business model vis-a-vis taxpayer having routine buy-sell model. So, in these circumstances, we are of the considered view that OTSE is not a suitable comparable vis-a-vis the taxpayer hence ordered to be excluded. "*

24.1 In view of the aforesaid factual matrix and the coordinate bench, this company is directed to be excluded from the list of comparables.

25. Virtual Netcom Pvt Ltd: The TPO as well as the Ld. DRP have not provided any reasoning or finding for this company's inclusion. The Ld. AR submitted that the company offers comprehensive information management solutions including information security, networking & network management

etc. to customers in India and SAARC through its alliance with technology partners like Barracuda Networks, Blue Coat, Extreme Networks, ForeScout, Palo Alto Networks, Radvision, Ruckus Wireless and Splunk, which is nowhere comparable with the appellant's trading functions. On perusal of the annual report of the company, it is noted that the company is carrying on the business of computer software developers and providing IT services. The Ld. AR also pointed out that the company operates on an entirely different business model, i.e. majority of sales are exports, and major portion of purchases are import.

26. The Ld. CIT(DR) submitted that this company is engaged in trading of computers and allied products as evident from the details of purchase of stock in trade provided in its financials. Upon perusal of Schedule Q of the financials which gives the particulars of the stock in trade, we find that the company purchases "Equipments Software and Support" and earns revenue by way of export of services. During the relevant year, out of a total sales revenue of INR 16.04 Crores, the company's exports stand at INR 15.04 Crores i.e. 94.10% and out of a total purchase of INR 14.27 Crores, the company's imports stood at INR 12.16 Crores i.e. 85.20%. This business model is just the opposite of that of the assessee. In its Trading segment, the assessee imports finished goods from its AEs and sells them in the domestic Indian market whereas Virtual Netcom imports software and almost entirely derives its revenues from export of services. The company's annual revenue of INR 16.62 Crores and cost base of INR 16.52 in FY 2014- 15 is negligible in comparison to the appellant's revenue base of INR 7,096 Crores and cost base of INR 7,080 Crores. This comparable therefore fails the test of functional similarity and therefore directed to be excluded.

27. Satytej Commercial Co. Ltd: This company was selected as a comparable by the assessee in its TP study report which was accepted by the TPO and DRP. However, the assessee submits that its inclusion was a mistake, and this company is functionally different than the assessee and must be excluded. It was submitted that this company was involved in sale of surgical and medical equipment which are not comparable to the assessee's product profile. For this reliance was placed on annual report of the company. It was also submitted it was rejected by this Tribunal in assessee's own case for AY

2014-15 on functional dissimilarity. Lastly, it was submitted that it is settled law that there is no estoppel in the statute and once the assessee can substantiate its claim that it had wrongly taken a particular comparable in the TP study, then the comparable ought to be rejected. For this reliance was placed on Deputy Commissioner of Income-tax v. Quark Systems (P.) Ltd. [2010] 38 SOT 307 (CHO.) (SB) (Para 38) affirmed by the Punjab & Haryana High Court [2011] 11 taxmann.com 427 and Navisite India Pvt. Ltd vs. ITO (ITA No. 5329/Del/2012).

28. The Ld. CIT(DR) submitted that this company was selected as a comparable by the assessee itself in its TP study report which in turn was accepted by the TPO and the Ld. DRP. At this stage, the assessee cannot be allowed to change its stand and argue for its exclusion. It was also submitted that the grounds of appeal do not have any specific reference to this comparable and in the absence of such ground, it is not open for the Tribunal to examine the same. We do not agree with this contention. The rules do not require a specific ground to be taken in respect of each comparable. A general ground in respect of arm's length price of the international transactions of the Trading segment is wide and comprehensive to include within its sweep any aspect of the determination of the arm's length price — whether it is inclusion or exclusion of a comparable or computation of the profit level indicator.

29. The purpose of the provisions of the Act is to enable the TPO and AO is to determine the correct taxable income and technical objections cannot be set up as barrier to adopt an admittedly correct position of fact and law. In the present situation, the comparable that is sought to be included by the Revenue evidently and admittedly lacks comparability on account of sharp differences in product profile. This aspect was examined by the coordinate bench in the prior assessment year 2014-15 as well and it was observed as under:

*"Perusal of pages 66 & 67 of the annual report for F. Y13-14 goes to prove that Sataytej is into sale of surgical and medical equipment which is not comparable to taxpayer..."*

29.1 The product profile of this company as well as that of the assessee has remained unchanged and therefore the findings of the Tribunal in the prior year squarely apply to this year as well. A perusal of the annual report of this

company for this year shows that the principal business of this company is sale of surgical and medical goods (heart valves). In our considered view, there cannot be any estoppel against the statute. If the company fails the test of comparability, it cannot be allowed to remain a part of the comparables. It is, accordingly, directed that this company should be excluded from the list of comparables. Accordingly, the Ground no. 21 is disposed of in terms of the aforesaid directions.

30. The next issue is in respect of transfer pricing adjustments made to the arm's length price of the international transactions of the Networking segment. Under Ground no. 23, it has been contended that the TPO has erred in including/excluding certain comparables under TNMM. In brief, the facts of this segment indicate that the appellant company is engaged in the trading of networking equipment. The telecom networking equipment are imported from its AE and is supplied to a third party telecom service provider. Besides supply of equipment, the assessee also designs, installs and commissions the network. To justify the arm's length price of the import transaction under this segment, the assessee in its transfer pricing report has adopted TNMM with operating profit margin on revenues (OP/OR) as the profit level indicator. The assessee's profit margin being 5.31% being higher than the mean margin of the uncontrolled party comparables (4.08%) it was concluded that the transactions were at arm's length. Four comparables were selected in the TP study.

31. The TPO recomputed and adjusted the arm's length price by Rs. 978,46,08,952, by rejecting 3 out of 4 comparables taken by assessee, introducing 8 new comparables and arriving at a final set of 9 comparables with OP/OR of 23.87%. The TPO also recomputed the operating margin of the appellant at 5.30%. While arriving at the operating margin, the TPO denied working capital and risk adjustments. The Ld. DRP did not give any finding on the objections raised by the assessee on inclusion/exclusion of comparable companies and accordingly, the adjustments made in the original TP order were incorporated in the impugned order. The Ld. AR submitted that the assessee is aggrieved by the inclusion of seven (7) comparable companies, and wrongful exclusion of 2 comparable companies.

32. The Ld. AR submitted that all the companies introduced by the TPO are

service providers and are not engaged in any sort of buy-sell activity, whereas the assessee is a trader who supplies telecom equipment to its customer (Reliance) wherein it performs buy-sell functions. For each of the comparable company, the Ld. AR made submissions reproduced below:

33. Altruist Technologies Ltd: It was submitted that the company is a pure service provider engaged in the provision of telecom solutions in the nature of content-based value-added services, revenue assurance, media related solutions etc. Reliance was placed on various extracts of the annual report of the company to substantiate the fact that this company is an IT service provider. Ld. AR also referred to the financial statement of the company to show that there was no expenditure on purchase of goods and no revenue from sale of goods or products.

34. AT & T Global Network Services India Private Limited: The Ld. AR submitted that the company is not a trader, but a service provider engaged in providing IT enabled services and telecommunication related services such as internet, voice services, application services, hosting services etc. Reliance was placed on company's website and annual report to show that the company is engaged in provision of IT and internet-based services. Ld. AR also referred to the financial statement of the company to show that there was no revenue from sale of goods or products. Another relevant point highlighted by the Ld. AR was the cost of goods sold to total cost ratio. In the case of AT&T it was only 26% as compared to the assessee 's 94%. High percentage of this ratio is an important attribute of a trader.

35. Bharti Airtel Limited: TPO included this company as a comparable on the ground that the company's 'Tower infrastructure segment' is comparable to the appellant's business. It was submitted that the finding of the TPO that the company's 'Tower infrastructure segment' is comparable to the assessee's business is factually incorrect. This company operates in three segments, namely, Mobile services. Tele media services and Airtel Business and there is no 'Tower Infrastructure Segment' reported by this company. It was also submitted that Airtel is a pure service provider earning income from telecommunications services, data messaging services and other value-added services. It earns a miniscule revenue (0.01 %) from the sale of products whereas the assessee is a trader of networking equipment earning around

97% of its revenue from sale of products. Another distinguishing factor pointed out by the Ld. AR was that the company owns a significant intangibles which accounts for 55% of its total fixed assets whereas the appellant does not own any intangible in this segment.

36. Planetcast Media Services Limited: It was submitted that the finding of the TPO that this company is engaged in trading of networking equipment is incorrect. Taking us through the financial statements, the Ld. AR submitted that the company provides technology-led managed services to the broadcasting industry comprising of digital media distribution services, digital media technology services, content production and acquisition services, content management and postproduction, cloud based content management services, outdoor media acquisition and media/live event coverage. It was also submitted that this company earns 99% of its revenue from sale of services.

37. Avantel Ltd, Hughes Communication Ltd and PCS Technology Ltd: Ld. AR submitted that the TPO committed the same error in these 3 comparable companies by treating these as trader of networking equipment, whereas on perusal of their financials, it is clearly evident that these companies are pure services provider.

38. On the contrary, Ld. CIT(DR) submitted that the TPO/DRP while dealing with the networking segment and selecting the comparable companies did not distinguish between a service provider and a trader since in common parlance the meaning of 'network infrastructure' includes both rendition of services and trading of networking equipment. In fact, provision of services is an essential ingredient of networking segment and thus the comparables chosen by the TPO/DRP cannot be rejected merely because they are network service providers. It was further submitted that each comparable chosen by the TPO is functionally similar to the assessee as the assessee's business is of network infrastructure service.

39. We have perused the annual reports and financials of these companies that have been taken as comparables to the Networking segment of the assessee. We find merit in the contention that all these seven companies are service companies and are not engaged in trading of any goods. The services provided by these companies range from IT services, telecom services,

content based services, digital media distribution services, to mobile and internet services. The assessee, in contrast, derives 95% of its revenues in this segment from sale of telecom equipment to Reliance. The design, installation, and commissioning fee is a small part of the composite sale agreement and this fee is a meagre 5% of the total revenues. In these circumstances, there is no justification in permitting these companies as comparables. These service companies are, therefore, ordered to be excluded from the list of comparables.

40. Apart from exclusion of comparable companies, the assessee has sought inclusion of 2 comparable companies namely, Nu Tech India Limited and HCL Comnet. For Nu Tech, the Ld. AR submitted that the TPO rejected this comparable merely on the basis that this company has diminishing net worth and sales in the last 3 years. However, the TPO did not make any adverse remark on the functional comparability of the company with the appellant. It was submitted that Nu Tech's net worth has remained the same for the year ending 2014 and 2015. Moreover, its sale has also increased by 16% in 2014 vis-a- vis 2013. Therefore, there is no diminishing trend and the contention of the TPO is incorrect. The Ld. CIT(DR) submitted that a company with a diminishing net worth cannot be taken as a valid comparable. The argument that there is an increase in sales on a year-on-year basis does not hold ground if the overall net worth of the company is declining.

41. We have considered the rival contentions and perused the financials, and the facts recorded by the TPO in her order on page 22 it is seen that the net worth of this company as on 31.3.2015 (last day of the financial year) was Rs. 488.38 crore. This figure remained unchanged since 31.03.2014 as the net worth recorded on that date was the same figure of Rs. 488.38 crore. Though, this figure on 31.03.2014 and 31.03.2014 was 15% less than the net worth as on 31.03.2013, it is not correct to state that there is downward trend in net worth. Moreover, the decline that was witnessed two years earlier of 15% cannot be treated as extraordinary in nature. Increase or decrease of net worth of businesses are normal incidents and there is nothing unusual regarding its change unless the going concern status is threatened. Similarly, we note that the TPO's observation that the company has seen a declining trend in sales is also factually incorrect as the sales in F.Yr 2012-13 was

Rs. 119 crore which went up to Rs. 139 crore in F.Yr 2013-14 and subsequently declined to Rs. 66 crore in F.yr. 2014-15. In our considered view, fluctuating sales figures, by themselves, do not disqualify a company from being treated as a comparable unless it can be shown that there are factors which are unusual and extraordinary which render the company as incomparable. No such factor is evident from the annual report or has been pointed out by the Ld. CIT (DR). On the functional level, this company is found to be comparable as it is trading in telecom equipment. It has another segment which has not been taken into account. We accordingly, approve the inclusion of the trading segment of this company as a comparable.

42. On HCL Comnet, the Ld. AR submitted that the TPO rejected this comparable merely on the basis that the company has different financial year ending. There are numerous judicial precedents which lay down the principle that functionally comparable companies can be selected even if they have different financial year ending. Ld. CIT(DR) has objected to the inclusion of this company on various grounds and has pointed out that the audited quarterly reports of this company have not been made available in the public domain and therefore it is not possible to reconstruct the annual financials. We find force in the submissions of the Ld. CIT(DR). In the absence of quarterly report which are audited, it is not possible to examine the same and construct an accurate financial statement for the financial year in question. Due to unavailability of audited and accurate information in public domain, we cannot permit the inclusion of this comparable.

43. The fourth issue is regarding the transfer pricing adjustments made to the arm's length price of the international transactions in the Manufacturing segment. In this segment, the assessee is engaged in manufacturing of consumer electronic goods, home appliances and mobile phones. These products are manufactured and sold on the basis of know-how and trademarks licensed from its parent. International transaction in this segment are import of raw material, payment of royalty, sale of finished goods besides other ancillary transactions. These transactions have been aggregated under TNMM and tested on the profit level indicator of operating profit margin on revenues (OP/OR). The assessee has earned a profit margin of 6.17% which is higher than the margin earned by the comparable companies (2.58%) chosen in the

TP study.

44. The TPO made a transfer pricing adjustment of Rs. 11,05,54,54,842/- to the arm's length price of the international transactions in the Manufacturing segment by rejecting 3 out of 5 comparables taken by assessee and introducing 2 new comparables and arriving at a final set of 4 comparables with operating profit margin on revenues (OP/OR) of 14.95%. The Ld. DRP did not give any finding on the objections raised by the assessee on inclusion/exclusion of comparable companies and accordingly, the adjustments made in the original TP order were incorporated in the impugned order. Under Ground no. 24, the assessee is aggrieved by the inclusion of two (2) comparable companies, namely Frog Cellsat Ltd. and Glen appliances, and wrongful exclusion of 3 comparable companies namely Value Industries Limited, Trend Electronics Limited and Penguin Electronics Limited.

45. Frog Cellsat Ltd: The TPO included this comparable on the ground that the company is engaged in the business of manufacturing equipment. DRP did not give any finding. The Ld. AR submitted that Frog Cellsat Ltd. is engaged in manufacturing of telecom repeaters, line amplifiers and other networking monitoring systems whereas the appellant is engaged in manufacturing of mobile phones, washing machines, refrigerators, colour television, air conditioners. The Ld. AR pointed out that the company's business model is different since it follows a B2B business-to-business model with sales being made to telecom companies. On the other hand, the assessee follows Business-to-customer (B2C) model with sales being made in the retail market. The Ld. AR also submitted that the company carries out R&D activities on its own through its design & development centre whereas the appellant relies on technology of the parent company (SEC Korea), in lieu of payment of royalty. Another distinguishing factor pointed out by the Ld. AR was the scale of operations. The assessee is large company having turnover of INR 24,891 Cr. which is 381 times more than that of Frog Cellsat.

46. The Ld. CIT(DR) submitted that this company is also engaged in the manufacturing of electronic equipment similar to the manufacturing segment of the appellant. Merely because the company does not manufacture identical products, it cannot be rejected as a valid comparable. Moreover, the appellant has applied TNMM as the most appropriate method to benchmark the

manufacturing segment. It is a well accepted principle that TNMM allows higher degree of flexibility in terms of the functional and product profile of the comparable companies. Therefore, this comparable has been rightly included. He referred to the details of the revenues of the company to show that it has received Rs. 62.65 crore as revenues from sale of repeaters and it also derived revenue of Rs. 3.17 crore from installation/de-installation/maintenance. In our considered view, the dissimilarities in product profile is too stark, vitiating the comparability with the assessee. The products manufactured by this company-repeaters are used by mobile service providers as a telecom equipment. It does not fall under the category of consumer electronics or home appliances. The goods manufactured by the appellant are TVs, refrigerators, mobiles, microwave ovens, air conditioners etc.. These products form part of rapidly growing section of the Indian market. Whereas products meant for industrial and technical use face very different economic dynamic and the risks involved are wholly dissimilar. Another factor which differentiates them is the R&D function. While the assessee is wholly dependent on its AE for the R&D, Frog Cellsat has its own R&D function. This further vitiates functional similarity. In view of the aforesaid there is little justification in including this comparable. It is, accordingly, directed that Frog Cellsat Ltd. be excluded from the list of comparables.

47. Glen Appliances Limited: Both the TPO and Ld. DRP did not give any specific reason for its inclusion. The Ld. AR submitted that this company is admittedly a distributor company and is not engaged in manufacturing function. On account of this fundamental difference, Glen Appliances has no basis to be included. It was submitted that this company was held to be a non-routine distributor of goods by the TPO himself while he examined the suitability of this company for the TNMM based intensity approach for AMP expenditure. Accordingly, it is an admitted position that Glen is a distributor and therefore cannot be included in the manufacturing set. The Ld. AR further submitted that Glen deals with products like gas stove, burners etc which do not involve any sophisticated technology. They have a mechanical mode of functioning and operate on ignition mechanism. On the other hand, the assessee is engaged in manufacturing of sophisticated products like mobile phones, washing machines, colour television, air conditioners etc.. These

products increasingly use digital technologies and softwares in their making. The Ld. CIT(DR) submitted that, since the manufacturing segment is benchmarked using the TNMM method, comparables can be chosen even if there are some functional differences since TNMM method allows flexibility in terms of the functional and product profile of the comparable companies. Therefore, this comparable has been rightly included. We have perused the annual report and financials of this company. We find that the main product of this company is distribution of "cooker range build in hood". It is a kitchen related product and strictly speaking not an appliance. Furthermore, the financials show that the income of this company is derived from distribution and not manufacturing. We have no hesitation in ordering the exclusion of this company on account of fundamental functional dissimilarity and dissimilarity of product profile.

48. Value Industries Limited and Trend Electronics: The Ld. AR submitted that these comparable companies were rejected by the TPO merely on the basis that they have a different financial year ending as compared to the appellant. It was submitted that this issue has already decided this issue in favour of the assessee and held that if the quarterly results are available and the information can be extrapolated, then the comparable should be included. The IT AT held as follows:

*"We accordingly remand the determination of these facts to the file of the TPO who is directed to examine whether quarterly results of R System and Caliber is available in public domain so that their annual profit margin can be determined in an accurate way. If such information is available, the comparable can be included. "*

48.1 Reliance was also placed on certain decisions wherein, it has been held that different financial year is not a criterion for rejecting a functionally comparable company when results can be extrapolated using quarterly results. It was submitted that admittedly the product profile of these companies matched with that of the appellant as these companies are engaged in manufacturing of consumer electronics goods including washing machines, air conditioners, refrigerators, and other home appliances which is similar to the functional profile of the Appellant. The Ld. CIT(DR) submitted that data of different accounting period cannot be taken under the rules. While we agree that a comparable with a different financial year can be taken if the

annual financials can be rebuilt using accurate quarterly audited data, if such data is not available in the public domain, there would be no justification in including the same. In the present case, the appellant has not filed the quarterly data of these two companies. Accordingly, we cannot accede to their demand and these companies cannot be included in the list of comparables.

49. Penguin Electronics Limited: TPO rejected this comparable on the ground of functional dissimilarity stating that it is engaged in manufacturing of different products and hence the same cannot be taken as a comparable company. The Ld. AR submitted that this comparable company was selected as a suitable comparable by the TPO himself in the TP Order for AY 2013-14 and the product profile of this company as well as that of the appellant has remained unchanged ever since. Penguin manufactures products such as radios, Walkman, audio products, domestic appliances etc., and hence it essentially operates as a manufacturer in the space of "Consumer Electronics" and "Home Appliances", which are the two broad categories in which the appellant operates. We are in agreement with the view that there is similarity of product profiles between this company and the appellant. Radios, Walkman, Audio products and domestic appliances form part of the same market space which has been referred to as consumer electronics and home appliances. They both cater to the same B2C segment and display similar functional characteristics. We also take note of the fact that the TPO had proposed use of this comparable in F.Yr. 2013-14 and accordingly consistency needs to be followed if the product profile has remained the same. This company is ordered to be included in the list of comparables.

50. Grounds 25, 27 and 28 are common pertaining to Trading, Networking and Manufacturing segments. For the determination of arm's length price of the international transactions of these segments, the appellant has contended that the TPO has erred in not granting working capital adjustment (Ground no. 27) despite there being a specific direction of the DRP in this regard and by using incorrect profit margins of certain comparables by erroneous treatment of certain operating income as non-operating and non-operating expenditure as operating in nature (Ground no. 25). Ld. AR has submitted that working capital adjustment has consistently been granted in the past assessment years and the DRP had directed the TPO to grant the same this year as well.

However, the TPO has inadvertently failed to do so. Ld. CIT(DR) does not contest the same and submits that this matter can be remanded to the file of the TPO for computation. In view of the same, we direct the TPO to grant working capital adjustment while computing the mean/median margin of the comparables in accordance with the binding direction of the DRP. Similarly, as regards incorrect computation of profit margins of the comparables, Ld. CIT(DR) does not oppose the issue in principle and submits that the TPO may be directed to carry out a factual verification of the income and costs that are sought to be included or excluded. We order accordingly. All items of income and expenditure which have a nexus with the business operations of the appellant are to be considered whereas any financing or non-recurring/non-operational item is to be excluded. Grounds no. 25 and 27 are disposed of in terms of the aforesaid directions.

51. The last common ground pertaining to the Trading, Networking and Manufacturing segments' adjustment is Ground no. 28 wherein the appellant has contended that the manner of computation of proportionate adjustment is erroneous. It was submitted that in prior years (A.Yrs. 2013-14 and 2014-15) similar errors were committed while determining the proportion of AE transactions and the Tribunal had remanded the matter back to the TPO for reconsideration. Ld. CIT(DR) did not object to the issue being remanded back to the TPO. We, accordingly, direct the TPO to determine the proportionate adjustment, if any, in an appropriate manner which considers the transactions with the AEs and excludes the unrelated party transactions after taking into account the computations submitted by the assessee.

52. The penultimate issue to be decided here is the adjustment/disallowance made in respect of royalty paid by the assessee to its parent for the know-how licensed for manufacturing of various products. The TPO has concluded that the rate of royalty is higher than the arm's length rate and has made adjustment of Rs. 902,75,71,252/- in this regard which has been contested in this appeal. Grounds 29 to 35 pertain to this issue.

53. As far as payment of royalty is concerned, appellant performs licensed manufacturing of products including colour televisions, washing machines, refrigerators, air conditioners and mobile phones. For this purpose, assessee entered into a license agreement for each category of product with its parent

SEC Korea, under which SEC Korea provides necessary technical know-how and assistance required to carry out the manufacturing activity. Such technical know-how includes proprietary and confidential technical knowledge, methods, processes, specifications, know-how, drawings, data, and information to facilitate manufacturing of licensed products by the assessee. Since the payment of royalty was closely linked with the manufacturing business, appellant did not benchmark this transaction separately and combined it with other international transactions of the Manufacturing segment and justified the same under TNMM. Since the assessee had earned 6.17% operating profit margin on sales as compared to the mean margin of 2.58% of the comparables, it had been concluded that all the international transactions of this segment including royalty were at arm's length.

54. The Ld. AR submitted that the assessee has been paying royalty to its parent company (SEC Korea) in consideration of technical know-how and other expertise since the year 2004-05. Being a licensed manufacturer of SEC Korea, appellant relies wholly on the technology/ know-how in order to carry out the manufacturing function. The technology and technical assistance received from SEC Korea is critical to the business operations of the appellant and hence the payments made by the appellant for the technology it receives are closely linked to its manufacturing business. Thus, the assessee has always aggregated the payment of royalty with its manufacturing function and has consistently applied TNMM on the manufacturing segment on an overall basis, which has consistently been accepted by the TPO. However, this year, despite there being no change in the manner in which the assessee's manufacturing business is organized and operated, the transaction of payment of royalty has been disaggregated and benchmarked separately. The actions of the DRP, TPO and AO in this regard suffer from various infirmities and are completely perverse in nature.

55. The Ld. AR drew our attention to the peculiar facts leading to this adjustment. During the course of the transfer pricing proceedings, the TPO had vide a show-cause notice (SCN) dated 17 September 2018 rejected the TNMM analysis (aggregated approach) adopted by the assessee. Instead, the TPO chose to apply the CUP method and thereby proposed three third party royalty agreements (with an ALP of 1.50%). This SCN was responded to vide

submission dated 9 October 2018, wherein the assessee raised its objections against 1) application of the CUP method while rejecting TNMM (Aggregated approach) and 2) the stark dissimilarities in the three third party royalty agreements v/s the assessee's license agreement. The TPO, after taking note of the appellant's arguments, did not make any adverse inference/ adjustment against the payment of royalty. Rather, the TPO in the TP order dated 31 October 2018 chose to adopt TNMM for the licensed manufacturing segment and carried out an aggregated analysis, wherein royalty was subsumed in the aforesaid analysis. The Ld. AR emphasized that the TPO was accordingly, convinced that royalty is an intrinsic part of the Licensed Manufacturing segment and accordingly, aggregated with the segment.

56. However, in the draft assessment order, ignoring the assessee's detailed submissions to the contrary, the AO held that the appellant had paid excessive royalty to the tune of INR 921.9 crores during the subject year and disallowed the same under Section 40A(2) of the Act. In the alternative, the AO also proposed to treat 75% of the royalty payment as capital in nature on a protective basis. Further, the AO held that excess royalty had been paid by the assessee to evade the payment of dividend distribution tax amounting to INR 156.67 crores. Accordingly, in addition to the disallowance of INR 921.9 crores, the AO also added INR 156.67 crores on account of non-payment of dividend distribution tax to the tax liability of the appellant. The Ld. DRP rejected the approach of the AO in entirety. The Ld. DRP however, erroneously stated in its directions that TPO had not carried out a benchmarking for the royalty payment and directed the TPO to carry it out while giving effect to the DRP directions.

57. Pursuant to the Ld. DRP directions, the TPO made an adjustment of Rs.902,75,71,252/- to the arm's length price of the royalty transaction by rejecting the TNMM method applied by the appellant and adopting CUP method (by using erroneous comparison with agriculture related royalty transactions). It is pertinent to note here that, for the purpose of imputing the royalty adjustment using the CUP method, the TPO has applied the same benchmarking analysis as proposed in the show cause notice during TP assessment proceedings which was later on dropped by the TPO himself, based on detailed submissions furnished by the assessee. On the basis of the

above facts, the Ld. AR submitted that the adjustment made on account of royalty is wholly without jurisdiction and bad in law as the DRP, TPO and AO have violated the mandatory requirements of Section 144C of the Act.

58. Ld. AR made detailed submissions in this regard and took us through the scheme of section 144C and the procedure provided there-under. He drew our attention to section 144C(8) which states that the DRP *"shall not set aside any proposed variation or issue any direction under sub-section (5) for further enquiry and passing of the assessment order"*. The Ld. DRP is required to adjudicate all questions before it based on the draft order, material submitted by the assessee, any remand report called for from the authorities and any inquiries that it may itself conduct. It was submitted that by issuing such directions the DRP has exceeded its jurisdiction. Reliance was placed on *Capstone Securities Analysis Pvt Ltd v DCIT* ITA no. 251/Pun/2017 in support of the above proposition. It has been contended that the assessee has been deprived of his right to object regarding any variation of his income before the DRP since the AO has passed the final assessment order based on the adjustment made by the TPO on the directions of the DRP. Placing reliance on *PCIT v. Woco Motherson Advanced Rubber Technologies Ltd.* 406 ITR 375, it was submitted that the machinery u/s 144C was a complete and exhaustive one and it does not give any room for the DRP to remand or set aside any matter to the TPO or the AO. Numerous decisions were cited in support of the proposition that a final assessment order passed in violation of the mandatory requirements of section 144C would vitiate the same and render it void and non-est.

59. Without prejudice to the above arguments, the Ld. AR submitted that the technology and technical assistance received from SEC Korea is critical to the business operations of the assessee and hence the payments made by the appellant for the technology it receives are closely linked to its manufacturing business. Therefore, an aggregated arm's length analysis of the segment is the most appropriate approach. The issue of aggregation of closely linked transactions was decided by the Tribunal in assessee's favour in AY 2005-06 to 2011-12 in the context of AMP expenditure. The Tribunal had held that once TNMM is accepted at an aggregated level for all the international transactions in one segment, it would not be open for the TPO to extricate one single

item/transaction/expenditure and subject it to a stand-alone benchmarking under some other method. Once the payment of royalty is aggregated within the manufacturing segment with all other transactions and benchmarked under TNMM by comparing the profit margin of the segment as a whole with that of the comparables, it is not open for the revenue authorities to proceed to benchmark the royalty transactions separately without there being any change in the underlying facts, and when the payment of royalty is inextricably linked with the manufacturing function.

60. It was also submitted that aggregation of closely linked transaction is permitted under law. Rule 10A(d) of the Income Tax Rules, 1962 defines the term 'transaction' in an inclusive manner and includes a number of closely linked transactions. OECD Guidelines 2017 - Para 3.9 states, as below:

*"Ideally, in order to arrive at the most precise approximation of the arm's length price, the arm 's length principle should be applied on a transaction-by-transaction basis. However, there are often situations where separate transactions are so closely linked or continuous that they cannot be evaluated adequately on a separate basis."*

60.1 The Ld. AR also relied on following judicial precedents to further buttress this point:

Magneti Marelli Powertrain India Pvt. Ltd. v. DCIT, [2016] 75 taxmann.com 213 (Delhi) / [2016] 389 ITR 469 (Delhi) upheld by Hon'ble Supreme Court vide order dated November 3, 2017, [2018] 89 taxmann.com 8 (SC); Kaypee Electronics & Associates Pvt Ltd vs DCIT, [2018] 94 taxmann.com 251 (Karnataka); M/s. Luwa India Pvt. Ltd. Vs. ACIT, [2016] 75 taxmann.com 145 (Bangalore - Trib.); Daksh Business Process Services (P) Ltd v DCIT, [2016] 72 taxmann.com 44 (Delhi - Trib.); DCIT v SNF (India) Pvt Ltd, 2019 SCC On Line ITAT 15119; Knorr Bremse India Pvt Ltd v ACIT, [2015] 63 taxmann.com 186 (Punjab & Haryana)/ [2016] 380 ITR 307 (Punjab & Haryana); and GBT India Pvt Ltd v ACIT, [2020] 117 taxmann.com 357 (Delhi - Trib.)

61. On the rejection of TNMM in favour of Comparable Uncontrolled Price (CUP) method based on certain royalty transactions taken as comparables by the TPO, the Ld. AR submitted that royalty agreements introduced by the TPO under CUP method belong to a completely different sector, i.e. agriculture.

The appellant (in its licensed manufacturing segment) is engaged in manufacturing of consumer electronics like TVs, home appliances like washing machines and mobile phones. The technology and other economic parameters in the electronics and communication industry is unique, fast evolving and affected by numerous global and local factors. The three comparable royalty agreements introduced by the TPO are entirely disparate and involve agricultural companies, engaged in developing products and tools in relation to seeds development which help farmers/ crop-growers make more efficient use of resources such as energy/ water/ land etc.

62. Ld. CIT(DR) opposed the contentions raised by the Ld. AR and submitted that the directions of the Ld. DRP to the TPO to benchmark the royalty transaction has resulted in partial relief to the assessee. Further, the directions issued by the Ld. DRP do not amount to "setting aside" of the matter to the TPO but to carry out a benchmarking exercise under a set of laid down guidelines. It was further submitted that the Ld. DRP has not set aside the matter to the AO but to the TPO which is not in violation of the section 144C. On merits, he submitted that TNMM is not an appropriate method to judge the arm's length price of royalty as the same is not inextricably linked with other transactions. The payment of royalty is not under a "package deal" comprising of numerous transactions. Each transaction is separate and diverse. Therefore, transfer pricing norms require separate benchmarking of each transaction and therefore the TPO was justified in examining the royalty transaction by using CUP. As regards, the comparable transactions chosen by the TPO which are in agriculture sector, Ld. CIT(DR) submitted that even though these transactions involve companies with different product profile, the technology for which royalty is paid by these companies is highly sophisticated similar to the technology availed by the appellant from its AE. Therefore, the transactions chosen by the TPO are good comparables and should not be rejected merely because they have a different product profile.

63. We have considered the rival contentions and examined the material on record. We find considerable merit in the contention of the assessee that the comparable transactions chosen under CUP are devoid of any meaningful comparability. Of all the methods prescribed, CUP is the most rigorous as it compares prices at transactional level. It requires highest level of similarity in

terms of subject matter of agreements and transactions in respect of products/services, salient contractual terms, tenure and several other economically relevant characteristics. We find that the TPO's selection of comparable transactions is vitiated as wholly incomparable technologies, products and contracts have been picked up in an arbitrary manner. Such an approach is inimical to the accuracy demanded under CUP. We have perused the royalty transactions chosen by the TPO and we note the following glaring dissimilarities that render the entire process untenable:

- (a) ROSETTA INPHARMATICS INC (LICENSOR) AND MONSANTO CO (LICENSEE) - This agreement pertains to payment of royalty in lieu of the right to use technical knowledge (algorithms and methods) for developing and selling species of animals, plants, plant or animal products, animal progeny, seeds containing a gene lead. It not valid for the relevant year since this agreement started in November 2000 for a period of 3 years and there is no material on record to show that it was in currency for the current year. The Licensor is a laboratory based in Washington which is engaged in provision of genomics services such as genotyping, gene sequencing, and gene expression profiling. The licensee is an agricultural company engaged in developing products and tools to including seeds to help farmers grow crops while using energy, water, and land more efficiently. The licensee uses biotechnology and other advanced methodologies including gene editing to make improvements in the plant's DNA to ensure a productive harvest.
- (b) MONSANTO CO (LICENSOR) AND CALGENE II, INC (LICENSEE)- The agreement does not even state the date of commencement nor the date of termination of the license. The Licensor is an agricultural company engaged in developing products and tools to including seeds to help fanners grow crops while using energy, water, and land more efficiently and Licensee is a biotechnology research

and development firm.

- (c) PARADIGM GENETICS INC (LICENSOR) AND MONSATO CO. (LICENSEE) - This agreement was entered on 17 November 1999 and valid for 6 years. Renewal agreement has not been produced. The Licensor is engaged in medical biotechnology and makes use of genomics information obtained from Arabidopsis, for extensions into crop plants via agricultural biotechnology while Licensee is an agricultural company engaged in developing products and tools to including seeds to help farmers grow crops.

64. These transactions are ex-facie disparate and do not have even a modicum of similarity at transactional level. We have no hesitation in holding that the approach adopted by the TPO is unsustainable and should be deleted. The adjustment made to the royalty transaction is therefore, held to be invalid and unsustainable in law.

65. Since we have held that on merits this adjustment is sustainable, we need not get into the issue of jurisdiction and other ancillary aspects raised by the assessee. These are academic in view of our aforesaid conclusion. As regards the issue of adoption of TNMM versus CUP, it is fair to conclude that if relevant data of comparable transactions (in terms of material aspects like nature of goods and services, geographical markets, contract terms etc) is not available CUP should be eschewed and TNMM can be an appropriate method to determine the arm's length. In the instant case, we have held that the data chosen by the TPO for CUP is wholly inappropriate. Secondly, the TPO has already accepted TNMM for the Manufacturing segment as a whole. There are numerous international transactions in this segment - all these transactions like royalty, purchase of raw materials etc. have been aggregated under TNMM and benchmarked against independent third party comparables. In these circumstances, cherry-picking of one particular transaction like royalty and subjecting the same to a separate benchmarking and adjustment under CUP results in an impermissible double adjustment - once under TNMM and another CUP. This is contrary to the provisions which mandate adoption of only one method as the most appropriate method. A licensing arrangement where technical know-how is used for manufacturing is an inextricable part of

the entire segment and we do not find any infirmity in bundling the same with the other transactions of this segment. At the end of the day, if the segment is generating arm's length level of operating profits which is equivalent or more than profit margin of the comparables, there can be no cause for the Revenue to carry out an exercise of the present kind. Grounds 29-32 are disposed of in terms of the aforesaid observations.

### **DISALLOWANCE OF SALARY PAID TO EXPATRIATE EMPLOYEES**

66. The last issue in this appeal pertains to Grounds 33, 34 and 35 - these are in respect of disallowance of salary amounting to Rs. 192,45,41,190/- paid to expatriate employees on secondment made u/s 37 of the Act by the AO. The AO has held that the employees on secondment from Korea are primarily working for the Korean parent and therefore, their salaries being paid by the appellant are not allowable as deductible expenses. This conclusion is based on legacy assessments carried out by the AO of the parent entity, Samsung Electronics Co. Ltd. Korea wherein the AO had concluded that on account of the presence of these secondees expatriates in India at the premises of the appellant, the Korean company had a fixed place permanent establishment in India. It was concluded that since the expatriate employees on secondment from Korea to India are regularly providing information to the parent company, they were in effect carrying out the business of the foreign company.

67. Before the Ld. DRP, the assessee submitted that in the case of Samsung Korea the issue of existence of permanent establishment on account of the activities of the secondees expatriates, the Tribunal has deleted the addition and negated the conclusion drawn by the AO. The DRP, while acknowledging the same directed the AO to verify whether any appeal has been filed by the department against the Tribunal order before the High Court. It was held that the addition would be sustained only if the matter was pending before the High Court under an appeal and if it was found that no appeal had been preferred by the department, the addition would have to be deleted. The AO after having ascertained that appeals have been filed for several years where the Tribunal had ruled in favour of Samsung Korea, he made the addition in his final assessment order.

68. Ld. AR, at the outset, submitted that this addition has been made for the second successive assessment year and was first made in prior A.Yr. 2014-15 on identical grounds. The appellant had carried the matter in appeal before this forum and the Tribunal has deleted the addition based on coordinate bench decision in the case of Samsung Korea wherein it has been held that the presence and activities of the secondees from Korea at the premises of the appellant does not lead to creation of any permanent establishment of the Korean company. He contends that the situation during the present year is similar as in prior year and the order of the Tribunal for the prior assessment year be followed.

69. As regards the facts it has been pointed out that the secondees from Samsung Korea are taken on the payroll of the appellant by way of local employment contracts and during the period of secondment they work under the sole control of the appellant. Their salary is borne solely by the appellant and the Korean parent is not liable for any of their actions and omissions. Their functions are wholly towards the business of the appellant and though they may be required to interact closely and regularly with the personnel of the parent entity, their functions and responsibilities are solely towards the appellant. He has cited numerous decisions to support the view that secondees were the employees of the assessee and no permanent establishment can be created for such activities. Ld. CIT(DR), while accepting, that the prior year's Tribunal order on this issue squarely covers the issue, submits that res-judicata does not apply to income tax proceedings and every year needs to be seen separately. He would submit that the seconded employees are furthering the objectives of the Korean company and are in effect the employees of the Korean company. We do not find any merit in his contention. The AO has not brought any evidence on record to show that the seconded employees were furthering the business objectives of the foreign parent. He has merely relied on the assessment order passed in the Korean company's case where it was held by the AO of the Korean company that it had a permanent establishment in India on account of the functions of the secondees. The entire approach is based on surmises and conjectures. The Coordinate Bench in the case of the Korean company has already deleted the additions and negated the existence of permanent establishment. Based on

these orders, in A.Yr. 2014-15, another Coordinate Bench has deleted the disallowance of salary made on this account. We accordingly direct the deletion of this disallowance. Grounds 33, 34 and 35 are, accordingly, allowed in favour of the assessee.

70. In the result, the appeal of the assessee is partly allowed in the aforesaid manner.

Order pronounced in the Open Court on 29/07/2024.

**Sd/-**  
**( G. S. PANNU )**  
**VICE PRESIDENT**

**Sd/-**  
**(YOGESH KUMAR U.S.)**  
**JUDICIAL MEMBER**

Dated : 29/07/2024  
R.N, Sr. PS  
Copy forwarded to :

1. Appellant;
2. Respondent;
3. CIT,
4. CIT (Appeals)
5. DR: ITAT

ASSISTANT REGISTRAR  
ITAT NEW DELHI

