IN THE INCOME TAX APPELLATE TRIBUNAL
ñBò BENCH : BANGALORE

BEFORE SHRI GEORGE GEORGE K., JUDICIAL MEMBER
AND SHRI A. MOHAN ALANKAMONY, ACCOUNTANT MEMBER

ITA No. 131/Bang/2010
Assessment year : 2004-05

Intel Asia Electronics Inc., India, Branch Office, C/o. Intel Technology India Pvt. Ltd., SRR2, Survey # 23-56P, Devarabeesanahalli, Outer Ring Road, Varthur Hobli, Bangalore South Taluk, Bangalore ï 560 103.	:	APPELLANT
Vs.		
The Assistant Director of Income Tax, Circle I(1), Bangalore.	:	RESPONDENT

Appellant by	:	Shri Kunj Vaidya, C.A.
Respondent by	:	Smt. Preethi Garg, CIT-III(DR)

O R D E R

Per A. Mohan Alankamony, Accountant Member

This appeal preferred by the assessee is directed against the order of the Ld. CIT(A)-IV in ITA No.174/R-19/CIT(A)-IV/06-07 dated 6.11.2009 for the assessment year 2004-05.

2. The assessee is a foreign company having a branch office in India and also has an associate enterprise (AE) - M/s. Intel Technologies India Pvt. Ltd. (ITIPL) - and primarily engaged in providing sales and marketing support service. The assessee having taken a decision to close down its branch office w.e.f. 1.4.2003 and transfer all its assets and liabilities to its AE - ITIPL as a going concern, for a consideration to be determined by the difference between the value of assets and liabilities in the books of the assessee.

3. The assessee has raised 6 grounds in its appeal, wherein ground No.6 being general in nature, it does not survive for adjudication. The cruxes of the issues addressed in ground Nos.1 to 5 are briefly condensed as follows:

ñThe ld. CIT(A) erred in confirming the armøs length price adopted by the ACIT (International Taxation), Circle 19(1), Bangalore, for the following reasons :-

(i) By adopting the written down value of assets of its office in India as it appeared in the financial statement in accordance with Company Law,

(ii) by rejecting the valuation report furnished by the assessee from a Chartered Engineer and Registered Valuer,

(iii) by holding that the assessee transferred its business (and not assets in specie) to its AE.

4. From the grounds raised by the assessee, only three moot questions arises:

(i) Whether the valuation of the assets based on the written down value as per the Company Law stated in the financial statements of the assessee should be adopted, or value determined by the Registered Valuer and Chartered Engineer should be adopted considering it to be ñComparable Uncontrolled Price methodò as proposed by the assessee?

(ii) Whether rejection of the valuation report submitted by the assessee from a registered Chartered Engineer is justifiable?

(iii) Since the Indian branch of the assessee is sold as a going concern, will it result in any consequence to determine the method to be adopted in valuing the assets of the assessee?

5. The Ld. AO referred the case to the TPO as the value of International transaction exceeded Rs. 5 crores. The Ld. TPO passed an order u/s. 92CA of the Act determining the shortfall in arms length price at Rs. 3,22,41,304/-. The Ld. TPOœ observations were as follows:-

- The assessee has preferred Comparable Uncontrolled Price as the method for determining the ALR for the sale of its business along with all Assets and Liabilities.
- As per CUP method the value of the Assets should be comparable which is not possible in this case.
- The Registered valuer had valued the Assets by depreciation method. The depreciation is worked out arbitrarily though stated to have considered various factors and the present general scenario in IT Industry.
- Since the entire business of the PE in India is also transferred to the assesseeœ AE the best method would be is to adopt the net book value.

The Ld. AO, after issuing notice to the assessee regarding the adjustments of arms length price determined by the TPO and affording the assessee an opportunity of being heard, passed an order confirming with the findings of the Ld. TPO since all objections raised by the assessee were already considered by the Ld. TPO.

6. The assessee appealed before the Ld. CIT(Appeals) who had confirmed the order passed by the Ld. Assessing Officer and out rightly rejected the valuation report certified by the Registered Valuer. The comments of the Ld. CIT(A) are listed out as under:.

- During the appellate proceedings, the assessee was not able to produce correspondence/e-mails exchanged between the parties with respect to the amendment of ñconsideration clause 2.1ò of the transfer agreement in order to prove bonafide of the transaction in spite of repeated requests.

- From the terms and conditions of the assets and liabilities transfer agreement between the parties, it is abundantly clear that the assessee had agreed to transfer the assets & liabilities of its PE along with the existing business as a going concern to the AE on the net book value. Therefore, determination of the net book value of the assesseeôs PE will be crucial for ascertaining the ALP of the transaction.

- The fair market value computed by the registered valuer is purely based on arbitrary rates and unreasonable assumptions rather than on any sound basis. The registered valuer has adopted unduly high rates of depreciation without any scientific or rational basis. These assumptions of the registered valuer are highly general and subjective and not based on statistical data, empirical evidence or comparable instances.

- The fair market value of resold improvements have been worked out by the registered valuer at Rs.72,27,677 while its WDV as per the Act was 1,29,40,455. It could be seen from the depreciation schedule worked out as per the Act itself that there was an addition of Rs.74,29,821 under ñleasehold improvementsò during financial year 2002-03. From the perusal of the valuation report, it could be noted that the registered valuer had not determined any value for ñleasehold improvementsò made in earlier years, which are shown at Rs.80,30,752 in the books of accounts and at Rs.69,48,462 in the depreciation chart worked out as per the Act.

7. Before us, the Ld. AR made the following submissions.

- The assessee has determined the value of the assets sold in accordance with the certificate issued by the Chartered Engineer and Registered Valuer.

- The Chartered Engineer and Registered Valuer had valued the assets considering all the facts like nature of the asset, sale ability in the open market, price change due to technological development in the field and price increase in respect of certain assets. The Registered Valuer and Chartered Engineer had evaluated the assets on scientific basis with justifiable reasoning in his report. Therefore, there should not be any reason to doubt the certificate issued by the valuer.

- The concept of fair market value and book value are totally different. The Accounting Standards also recognize the fact that it is necessary to revalue the assets to arrive at the fair market value.

- The net book values of the assets are determined by reducing the depreciation computed at the rates specified by the Companies Act from the historical cost of acquisition. In reality, it is not necessary that the assets can always be sold at such book value computed. There could be instances where an asset could be at a value more or less than of the book value. The Accounting Standards also recognize the concept of profit & loss on sale of assets.

- Different Acts have adopted different rates for depreciation according to their perceptions. For instance, the rate of depreciation prescribed under the Income-tax Act is different from the rate prescribed under the Companies Act. In the instant case, majority of assets sold by the assessee were computers and accessories. The rate of depreciation prescribed for computers and accessories as per Companies Act is 40% whereas the rate adopted under the Income-tax Act is 60%.

- In the recent past, there have been extremely fast technological developments in the field of computer and its accessories. A computer available in the market today becomes obsolete within a year on an average. Price levels also drop drastically within a period of a year. In such a situation, second-hand computers do not fetch much resale value.
- Evaluating the value of assets by registered Chartered Engineers is acceptable in law. The Valuer engaged by the appellant is one amongst the most reputed valuers in the city, whose reports are generally accepted by the tax department. He is also not related to the assessee in any manner. Therefore, there is no reason to doubt his integrity or bonafide of his valuation report.
- The Revenue has not found any specific defects in the Registered Valuer's report, but has passed only generalized comments to reject it. In fact, the figures worked out by the Registered Valuer are on the higher side.
- The Revenue's action of treating the book value of the asset as ALP is not justifiable. The rates prescribed under the Companies Act have remained static over a long period. This clearly shows that such rate of depreciation does not reflect the correct diminution in the value of the assets in the challenging, highly volatile and unpredictable market conditions of the present day. In these circumstances, the valuer's report which has taken into consideration of all factors affecting the marketability of the assets is more appropriate to rely upon. It is also a settled law as per principles laid down by the Hon'ble Apex Court that accounting principles cannot be the basis for determination of tax liabilities. Tax liabilities have to be mandatory determined as per the tax laws.

8. The Ld. DR strongly supported the order of the Ld. AO and Ld. CIT(Appeals) and argued that the valuation report has to be rejected

outrightly since it did not have a sound scientific footing. The Ld. DR further argued that changing the terms with respect to consideration in the transfer agreement was purely an afterthought and the change was brought in, in order to avoid levy of tax. The Ld. DR vehemently prayed that the order of the Ld. CIT(A) requires to be upheld.

9. We have heard the rival submissions and perused the records minutely. From the arguments of both the parties, we find that there is no dispute with regard to the method adopted for determining the Arm's length price (ALP) relating to the international transaction i.e. Comparable Uncontrolled Price Method (CUPM). However, the objection of the Revenue is that the valuation of assets by the Registered Valuer and Chartered Engineer is arbitrary, without any reasonable basis and therefore, erroneous ;,hence, the same cannot be considered for arriving at the ALP. The Revenue is of the opinion that the Registered Valuer has arbitrarily adopted the depreciation rate for every item in order to arrive at a figure convenient to the assessee. The Registered Valuer had not explained with proper reasoning as to why such depreciation rate was being considered while depreciating the value of asset. On our perusal of the valuation report, we also came at instances where the valuation was done without any reasoned footing. For instance, depreciation for furniture and fixtures was provided at the rate of 30%/40%/50%/60%/75% and 90% (Source page 17 to 40 of the paper book furnished by the assessee) which included items like chairs, tables, Godrej filing cabinets, racks, etc. Further, we noted that Godrej safes were depreciated at 90% which is not at all reasonable. For most of the computers and accessories, depreciation was

worked out at 100%/90% and thereby assuming the value of the equipments to be nil or at 10% of its cost. Considering these factors, we are in total agreement with the Revenue for rejecting the Valuer's Report.

10. As per the guidelines Note issued by the Institute of Chartered Accountants of India, CUP method may be determined by adopting the following steps for transfer of goods:

i) identify the price charged to the items sold in comparable uncontrolled transaction or in a number of such transactions.

ii) Adjust such price to account for the differences if any, between the International transaction and the comparable uncontrolled transaction or between enterprises entering into such transactions which could materially affect the price in the open market. The presence or absence of any special feature in the uncontrolled transaction as compared to the International transactions is to be adjusted for in mathematical terms or absolute numbers.

iii) Such adjusted price is the ALP.

iv) The ALP is now to be compared with the price charged in the international transaction.

v) If price charged in the international transaction is lower than the ALP or higher than the ALP, then an adjustment is to be made for the price charged in the international transaction by the amount of such variance.

This method is suitable when an independent enterprise sells the same product as is sold between two associate enterprises. The uncontrolled transaction should reflect goods of a similar type, quantity and quality as between the associate enterprises and relate to transactions taking place at a similar time and stage with similar conditions applying.

11. In the instant case, this is an isolated transaction of sale of the assesseeøs permanent establishment (PE) as a ógoing concernö to the assesseeøs AE and, therefore, there are no similar transactions in an uncontrolled situation to compare with the controlled situation. However, the contentions of the assessee are justifiable that the actual market value of the asset has to be determined in an uncontrolled situation to determine the ALP in this case. In order to determine the actual market value, in the absence any such identical transaction/transactions, as opted by the assessee, the valuation determined by the registered valuer could be the most appropriate means under CUP method. However, in this given case, the valuation report relied upon by the appellant is held to be erroneous due to various reasons as discussed above. In such a situation, the only option available to the Revenue is to adopt the value of the assets sold as per the written down value arrived at by following the provisions of the Company law or Income-tax Law. We do agree with the argument of the appellant that the depreciation rates prescribed by the company law is static and, therefore, the WDV of the assets so arrived at will not be at par with the net present market value and, therefore, the valuation of the assets based on the book value as determined by the Ld. AO is not justifiable.

12. To break the ice in such a situation, the only reasonable approach would be to value the assets by applying the depreciation rates as provided by the Income Tax Act for it is more dynamic and so schemed to bring in a notional charge on the profit and loss account to arrive at the actual income of an assessee keeping in view of the depletion of the assets.

13. To sum up; with regard to the questions framed by us in Para 4, we hold as under:

(i) In the present case since the valuation based on the WDV worked out as per the Income Tax Act will be most appropriate since the valuation report of the Registered Valuer and Chartered Engineer is rejected.

(ii) In the present case the valuation report of the Registered Valuer and Chartered Engineer requires to be rejected is justified due to the reasons discussed hereinabove.

(iii) The Indian Branch of the assessee is sold as a going concern. We are of the opinion that this fact will also have some consequences in determining the ALP because factors like profitability of the branch office, goodwill, and various other commercial and technical aspects will have a bearing when the AE takes over the branch office of the appellant. However, neither the Ld. AO nor the Ld. CIT(A) have made any reference on any factors on this regard in this given case and, therefore, we refrain from making any comments with regard to this aspect in this case.

Accordingly, the matter is remitted back on the file of the Ld. AO with a specific direction to the AO to determine the ALP by adopting the value of assets by WDV method as per the Income

Tax Act, of course, after providing a reasonable opportunity to the assessee of being heard. It is ordered accordingly.

14. In the result, the appeal of the assessee is treated as allowed for statistical purpose.

Pronounced in the open court on this 21st day of January, 2011.

Sd/-	Sd/-
(GEORGE GEORGE K.) Judicial Member	(A. MOHAN ALANKAMONY) Accountant Member

Bangalore,
Dated, the 21st January, 2011.

Ds/-

Copy to:

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

By order

Assistant Registrar

ITAT, Bangalore.