IN THE INCOME TAX APPELLATE TRIBUNAL,
AHMEDABAD D BENCH, AHMEDABAD

[Coram: Pramod Kumar AM and S S Godara JM]

I.T.A. No.: 2873/Ahd/10
Assessment year: 2006-07

Micro Ink Limited ***………………….Appellant***
Bilakhia House , Muktanand Marg
Chala, Vapi, Gujarat [PAN: AAACH7063F]

Vs.

Additional Commissioner of Income Tax
Vapi Range, Vapi ***……………….Respondent***

Appearances by:
M K Patel, *for the appellant*
B Y Chavan *for the respondent*

Date of concluding the hearing : November 4, 2015
Date of pronouncing the order : November 27, 2015

O R D E R

Per Pramod Kumar, AM:

1. By way of this appeal, the assessee appellant has challenged correctness of the order dated 5th August 2010 passed by the Assessing Officer under section 143(3) read with section 144C of the Income Tax Act, 1961, for the assessment year 2006-07.

2. Ground no. 1 is general in nature and does not call for any specific adjudication by us.

3. In ground no. 2, the assessee is, in substance, aggrieved of an arm's length price adjustment of Rs 2,10,95,246 being notional value of excess credit period

allowed by the assessee to its US based associated enterprise, i.e. Micro Inks USA, in respect of sale of semi finished goods, ingredients and raw materials.

4. The relevant material facts, as necessary for our adjudication, are like this. The assessee before us is a leading ink manufacturer in India. The assessee has a wholly owned subsidiary in Austria, by the name of Micro Inks GmbH which, in turn, owns Micro Ink Co USA. This step down subsidiary (Micro USA, in short) manufactures printing ink by using the base material supplied by the assessee. The inks meant for US markets thus are mixed, and given finishing touches, by Micro USA. The assessee company also has trading subsidiaries in China and Hong Kong. During the relevant previous year, the assessee sold goods worth Rs 215.51 crores to Micro USA. The Transfer Pricing Officer, in the course of proceedings before the TPO, it was noted that the assessee has sold goods worth Rs 215.51 crore to Micro USA and allowed it an average credit period of 186 days as against average credit period of 130 days allowed to independent enterprises, i.e. non AEs. It was also noted that out of total exports made by the assessee, 45% exports was to Micro USA. On these facts, and the TPO being of the view that "in a third party situation, such an allowance of use of money would have been possible only upon charge of a cost", the TPO required the assessee to show cause as to why ALP adjustment in respect of excess credit period of 56 days not be made, by computing time value of money @ 6.38% on LIBOR plus basis. In response to this show cause notice, it was, inter alia, explained by the assessee that what is exported to Micro USA is semi finished material which is required to be further processed and converted into saleable product. In effect thus, export to Micro USA cannot be compared with export of finished products as was done to the independent enterprises. The assessee had also pointed out that "average credit period of third parties is 120 days whereas credit period granted to Micro USA is 135 days" though "actual highest average debtor days to third parties is 161 days whereas for Micro USA it is 186 days". It was also explained that considering the time taken in shipping the semi finished goods to Micro US, its processing in US, maintenance of inventory at US and credit realization time in US, the total cycle was about 210 days, but even

if bare minimum period to complete a sale cycle is taken account, it cannot be less than 170 days. It was thus pointed out that the average credit period to Micro USA, which was 135 days, was reasonable. On the basis of these arguments, it was submitted that no ALP adjustment is warranted in respect o, what was termed as, 'excess credit period' allowed to the Micro Ink USA. None of these submissions were accepted by the TPO. He was of the view that, taking 130 days as permissible interest free credit period, interest @6.38% should have been charged on the excess credit period of 56 (i.e. 186-130) days. An amount of Rs 2,10,95,346, computed on this basis, was proposed to be added to the income of the assessee as an arm's length price adjustment. The assessee did raise a grievance, against this ALP adjustment, before the DRP but without any success. The Assessing Officer, therefore, proceeded to make the addition of Rs 2,10,95,346, aggrieved by which the assessee is in appeal before us.

5. We find that this issue is covered, in favour of the assessee, by a decision of the coordinate bench in assessee's own case for the assessment year 2002-03 [reported as **Micro Inks Ltd Vs ACIT [(2013)144 ITD 610 (Ahd)**]. While deleting similar addition, the coordinate bench had observed as follows:

> **20. The only other ALP adjustment in appeal before us is with respect to, what the authorities below have treated as, excess credit period allowed to Micro USA. This adjustment must be deleted for the short reason that it was part of the arrangement that specified credit period was allowed and thus the cost of funds blocked in the credit period was inbuilt in the sale price. There is no dispute that similar products are not sold to any other concern, at same price or even any other price, and interest is levied on the similar credit period allowed to those independent parties but not to Micro USA. The question of excess credit period arises only when there is a standard credit period for the product sold at the same price and the credit period allowed to the associated enterprises is more than the credit period allowed to independent enterprises. That is not the case here. The credit period for finished goods cannot be compared with credit period for unfinished goods and raw materials, and in any case, when products are not the same, there cannot be any question of prices being the same. Unless the prices of the product and the product are the same, and yet extra credit period is allowed, there cannot be any occasion for making ALP adjustment on the basis of the excess credit period. None of the authorities below have even disputed that the**

> **ingredients, raw materials and semi finished goods sold to Micro USA are not sold to any other concern. The very foundation of impugned addition in arm's length price on account of excess credit period is thus devoid of any legally sustainable merits or factual basis. When all these factors were pointed out to the learned Departmental Representative, he did not have much to say except to place his bland but dutiful reliance on the orders of the authorities below. However, for the reasons set out above and in the absence of any comparative price and credit period figures on comparable product to support the case of the revenue, we uphold the grievance of the assessee and direct the Assessing Officer to delete this ALP adjustment. The assessee gets the relief accordingly**.

6. Learned counsel for the assessee submits that the issue being squarely covered, in favour of the assessee and on admittedly similar set of facts, there is no occasion to reconsider the mater. We are urged to follow the said decision and delete the impugned adjustment. On the other hand, while learned Departmental Representative does not dispute that this issue is squarely covered by the aforesaid decision, he submits that the aforesaid decision is "severely flawed" as no matter what is the goods sold, "a credit period is a credit period". It is also submitted that "the credit period for sale of raw material to an independent manufacturer would be lower as the supplier does not have to factor the lead time for the sale of finished goods by the manufacturer" and that "the supplier is entitled to receipt of payment immediately on delivery irrespective of whether the finished goods is sold in the market, get spoiled in manufacturing or is damaged". He further submits that "it is by now acknowledged that granting of excess credit period is a service rendered to the AE and needs to be benchmarked". A reference is then made to Special Bench decision in the case of **Aztec Software & Technology Services Pvt Ltd Vs ACIT [(2007) 107 ITD SB 141 (Bang)]** in support of the proposition that merely by finding fault in the work done by the TPO, the adjustments cannot be deleted and that unless the ALP submitted by the taxpayer is specifically accepted, the appellate authorities, on the basis of material available on record have to determine ALP themselves.

7. We find that, as evident from audit report on form 3CEB (pages 39 to 52 of the paper-book), the arm's length price of exports to the AEs, including Micro USA,

has been determined on the basis of the transactional net margin method (TNMM). By way of a note at page 51, it is specifically stated that "further, the said amount of Rs 2428.26 millions has also been determined/ computed by the assessee having regard to the arm's length price on application of Transactional Net Margin Method (TNMM), on aggregation of transactions, as prescribed under section 92C of the Income Tax Act, 1961". In this backdrop, we can usefully refer to the decision of Hon'ble Delhi High Court, in the case of **Sony Ericsson Mobile Corporation Pvt Ltd Vs ACIT [(2015) 374 ITR 118(Del)]** wherein Their Lordships had, inter alia, observed as follows:

> **"Where the Assessing Officer/TPO accepts the comparables adopted by the assessed, with or without making adjustments, as a bundled transaction, it would be illogical and improper to treat AMP expenses as a separate international transaction, for the simple reason that if the functions performed by the tested parties and the comparables match, with or without adjustments, AMP expenses are duly accounted for. It would be incongruous to accept the comparables and determine or accept the transfer price and still segregate AMP expenses as an international transaction,"**

8. By way of an example, this aspect of the matter was then explained by Hon'ble Delhi High Court as follows:

"An example given below would make it clear:

Particulars	*Case 1*	*Case 2*
Sales	*1000*	*1,000*
Purchase Price	*600*	*500*
Gross Margin	*400 (40%)*	*500*
Marketing Sale promotion	*50*	*150*
Overhead expense	*300*	*300*
Net profit	*50 (5%)*	*50 (5%)*

The above illustrations draw a distinction between two distributors having different marketing functions. In case 2, a distributor having significant marketing functions incurs substantial expenditure on AMP, three times more than in case 1, but the purchase price being lower, the Indian AE gets adequately compensated and, therefore, no transfer pricing adjustment is required. In case we treat the AMP expenses in case 2 as Rs.501-, i.e. identical as case 1 and AMP of Rs. 100 as a separate transaction, the position in case 2 would be:

Particulars	*Case 2*
Sales	*1,000*
Purchase Price	*500*
Gross Margin	*500*
	(50%)
Overhead expenses	*300*
Marketing expenses	*50*
Net profit	*150 (15%)*

> *It is obvious that this would not be the correct way and method to compute the arm's length price. The purchase price adjustments/set off would be mandated to arrive at the arm's length price, if the AMP expenses are segregated as an independent international transaction....."*

9. By the same logic, even making an adjustment for interest on excess credit allowed on sales to AEs will vitiate the picture, inasmuch as what has already been factored in the TNMM analysis, by taking operating profit figure which incorporate financial impact of the excess credit period allowed, will be adjusted again separately as well. Of course, in the example used by Hon'ble Delhi High Court, the AMP expenses are deductibles in computation of operating profit but that does not make any material difference because the interest levy for late realization of debtors, being inextricably connected with the sales, is also part of operating income. In the case of **Nirma Industries Limited Vs DCIT [(2006) 283 ITR 402 (Guj)],** Hon'ble High Court has dealing with the nature of interest on debtors, held it to be integral to business income. The same is the principle for the transfer pricing cases to that extent interest is to be taken as integral to sale proceeds, and, as such, includible in operating income. When such an interest is includible in operating income and the operating income itself has been accepted as reasonable under the TNMM, there cannot be an occasion to make adjustment for notional interest on delayed realization of debtors. One can understand separate adjustment for excess credit period when the arm's length price for exports has been benchmarked on the CUP basis but not in a case when the arm's length price of the exports has been benchmarked on the basis of

TNMM. The very conceptual foundation, for separate adjustment for delayed realization of debtors and on the facts of this case, is thus devoid of legally sustainable merits.

10. The other aspect of the matter is that a separate adjustment for delayed realization of debtors can, even in a fit case, can only be made only to the extent the credit period allowed to the associated enterprises is more than the credit period allowed to independent enterprise in respect of the same or materially similar transactions. In the present case, it is an undisputed position that semi finished goods, as sold to Micro USA, is not sold to any other independent enterprises. The assessee did have trading transactions in respect of the finished goods with trading subsidiaries in China and Hong Kong but it is not even the case of the TPO that excessive credit period was allowed to these AEs vis-à-vis the credit period allowed to independent enterprises, nor any ALP adjustment has been recommended in connection with the same. This fact, if anything, shows that the credit period allowed to the AEs is comparable with credit period of non AEs in respect of similar goods. To compare credit period in respect of finished goods with the credit period in respect of semi-finished goods, is, therefore, somewhat fallacious in approach and untenable in law. In our considered view, merely because there is a delay in realization of debts cannot be reason enough to make an addition as long as such a delay is peculiar to the transactions with AEs. The adjustment before us is an adjustment to arrive at an arm's length price and unless there is something, more than sweeping generalizations as implicit in the arguments before us, to at least indicate that such a delay in realization of debts in similar transactions is absent in arm's length transactions, these adjustments cannot be made even when sales are benchmarked on CUP basis. The delay in realization of debts, resulting in a continuing debit balance, is not a standalone international transaction *per se*, but is a result of the international transaction as it only reflects that the related payment has not been made by the debtor. As for the learned Departmental Representative's stand that "the supplier is entitled to receipt of payment immediately on delivery irrespective of whether the finished goods is sold in the market, get spoiled in

manufacturing or is damaged" would probably be valid in the perfect market conditions which are more of a myth than reality. The only other merit of this approach is its simplicity, or, to put it more appropriately, naivety. The real life trade and commerce is seldom so simple. It is not at all necessary that a payment is to be made as soon as goods or services are delivered. A call is to be taken by the vendor, in consultation with its client and based on the business exigencies, as to what should be the terms on which payments for the supplies is to be made. It is a harsh commercial reality that immediate payments are more of exceptions rather than rule, and more so in a complex case in which the assessee is sole vendor and the very existence of the buyer is to process the semi- finished goods and sell it to the end buyers. Many factors, such normal business practices and the commercial exigencies, influence the fact of payment in respect of a commercial transaction. Whether a payment is made immediately by the AE or is made after six months cannot, therefore, be seen in isolation with what is the position is with respect to similar payments due from non AEs. The whole exercise of ALP adjustments is to neutralize the impact of *inter se* relationships between the AEs and it is, therefore, not the delay *simplictor* in payment but delay in payment vis-à-vis similar situations with non AEs (i.e. independent enterprises) which is of crucial consideration. Such a comparison cannot be based on the hypothesis as to what would have, in the wisdom of the TPO, happened if assessee was to have similar transactions with non-AEs. The comparison has to be based on real transactions of similar nature, if at all such transactions have taken place. When no such transactions have taken place, as is the case before us, there is obviously no occasion of any comparison. The stand taken by the learned Departmental Representative, therefore, is not only quite detached from commercial reality but also wholly untenable in law. In any case, what can be examined on the touchstone of arm's length principles is the commercial transaction itself, as a result of which the debit balance has come into existence, and the terms and conditions, including terms of payment, on which the said commercial transaction has been entered into. In this view of the matter, learned Departmental Representative's reliance on Aztec decision *(supra)* is of no assistance to the case of the revenue. The international transaction is exports of goods which been benchmarked on TNMM basis and which is duly accepted by the TPO. In view of these discussions, and respectfully following the decision of the coordinate bench in assessee's own case for the earlier years, we uphold the grievance of the assessee and direct the Assessing Officer to delete the impugned ALP adjustment of Rs 2,10,95,346.

11. Ground No. 2 is thus allowed.

12. In ground no. 3, the assessee is aggrieved of an arm's length price adjustment of Rs 2,32,62,603 on account of corporate guarantees given by the assessee in respect of its associated enterprises.

13. So far as this grievance of the assessee is concerned, the relevant material facts are like this. During the course of the proceedings before the Transfer Pricing Officer, it was noted that the assessee has issue various corporate guarantees on behalf of its associated enterprises, i.e. subsidiaries. The details of these guarantees are as follows:

S.No.	***Financial Institution***	***Guarantee Amount***	***Loan o/s. as on 31.03.05***	***Loan o/s. as on 31.03.06***	***Average of o/s. Amount***
(a)	***(b)***	***(c)***	***(d)***	***(e)***	***(f)***
1.	***Bank Leumi-USA(STL)***	***$3,000,000***	***$3,000,000***	***$3,000,000***	***$3,000,000***
2.	***UTI Bank***	***$5,000,000***	***$2,449,998***	***$833,331***	***$1,641,665***
3.	***ICICI Bank***	***$5,000,000***	***$4,900,000***	***$2,940,000***	***$3,920,000***
4.	***Standard Chartered Bank***	***$10,000,000***	***$10,000,000***	***$10,000,000***	***$10,000,000***
5.	***ICICI Bank (2nd loan) May 2005***	***$5,000,000***	***-***	***$4,900,000***	***$4,900,000***
6.	***HDFC Bank-August 2005***	***$3,000,000***	***-***	***$3,000,000***	***$3,000,000***
	Total	***$31,000,000***	***$20,349,998***	***$24,673,331***	***$26,461,665***

14. It was also noted that guarantees were issued without charging the AEs any consideration for the same. The stand of the assessee was that these guarantees

did not cost assessee anything nor any charges were recovered for the same, and that the "said guarantees were in the form of corporate guarantees/ quasi capital and not in the nature of any services". The TPO, however, proceeded to compute arm's length price for these guarantees @2% on the basis of following reasoning:

> **7.2 Guarantees are chances that someone will have to pay for them, if chance is 100% i.e. in all cases one has to pay for it, guarantee fees will be simply equal to it (i.e. the guarantee amount). However, if it is only a probability and only in few cases it will have to be paid, its charges are just percentage of it. Banks normally compute guarantee charges on the basis of their experience in handling such situation.**
>
> **7.3 Guarantees given by an assessee makes its own borrowing costlier as its assets get used in guaranteeing, it has to raise costlier capital without being able to use its own those very assets. There cannot be direct link to the guarantees given for the purpose of computing cost but the fact remains that there was cost to guarantor. In view of above discussions, guarantee fees is calculated @ 2%, which is prevalent market rate for guarantee fees.**

15. It was on this basis that an ALP adjustment of Rs 2,23,62,603 was proposed on account of notional charges for corporate guarantees issued by the assessee. The assessee did raise an objection against this proposed adjustment by the TPO but without any success. While rejecting the grievance of the assessee, learned DRP referred to, and relied upon, '**OECD Transfer Pricing Guidelines for Multinational Enterprise and Tax Administrations'**, 'OECD **Report on Attribution of Profits to Permanent Establishments**' and decision of the Tax Court of Canada in the case of **G E Capital Canada Vs Her Majesty the Queen [(2009) TCC 563].** The Assessing Officer thus proceeded to make the arm's length price adjustment in respect of corporate guarantees at Rs 2,23,62,603. The assessee is aggrieved and is in further appeal before us.

16. Learned counsel for the assessee submits that the transaction of issuance of a corporate guarantee, in favour of an AE, does not constitute an 'international transaction' within the meanings of Section 92 B of the Act. Our attention is invited to

the transfer pricing report which categorically states that the “guarantees issued by the assessee are said to be in the form of corporate guarantees/ quasi capital and not in the nature of services” and that, accordingly, “these transactions are not considered as international transactions”. Learned counsel then refers to a decision of a coordinate bench of this Tribunal, in the case of **Bharti Airtel Limited Vs ACIT [(2014}63 SOT 113 (Del)]** which categorically holds that corporate guarantee issued for benefit of AE, not involving any costs to assessee and not having any bearing on profits, income, losses or assets of enterprise, are required to be kept outside ambit of 'international transaction'. Learned counsel then takes us through a number of decisions of the coordinate benches following the same proposition, including the decisions in the cases of **Redington India Limited Vs ACIT [(2014) 49 taxmann.com 146] (Chennai)],Redington India Ltd Vs JCIT [(2015) 61 taxmann.com 312 (Chennai)], Videocon Industries Ltd Vs ACIT [(2015) 55 taxmann.com 263 (Mum)].** He thus urged us to delete the impugned ALP adjustment on the short ground that the issuance of corporate guarantees, on the facts of this case, did not constitute an international transaction. Without prejudice to this argument, learned counsel submitted that even if it is assumed that post 2012 amendment in the definition of ‘international transaction’ stand specifically included in the scope of international transactions, in respect of which arm’s length price adjustments can be made, it is only elementary that such an amendment cannot have retrospective effect. He points out that the transfer pricing legislation is inherently an anti abuse legislation which seeks to ensure that the assesses behaves well within certain norms. This kind of legislation, according to the learned counsel, can never have retrospective application as assessee cannot be told today as to how should he have behaved in the past. Learned counsel submits that none can lay down the norms now and expect the assessee to have complied with these norms in the past. Learned counsel then points out that while tax legislation in general may have retrospective effect, even though presumption is in favour of the law being prospective, tax legislation in the nature of anti abuse legislation cannot be made retrospective as it would amount to an impossibility for the assesses to comply with the same. On this point also, learned counsel takes us through certain observations in **Bharti Airtel** decision *(supra)* to the effect that it is an issue to be examined whether an enhancement of scope of this anti avoidance provision can be implemented with retrospective effect. He submits that in the said case, the coordinate bench did note that "Undoubtedly, the scope of a charging provision can be enlarged with retrospective effect, but an anti-avoidance measure, that the transfer pricing legislation inherently is, is not primarily a source of revenue as it mainly seeks compliant behaviour from the assessee vis-à-vis certain norms, and these norms cannot be given effect from a date earlier than the date norms are being introduced", yet it did not adjudicate on that question for the reason that the matter has been decided "in favour of the assessee on merits and even after taking into account the amendments brought about by Finance Act 2012". In case the issue is to be held against the assessee, learned counsel submits, this aspect of the matter must be adjudicated upon now. It is his contention that any amendment in the transfer pricing law, which is more onerous in nature, cannot have retrospective effect. We are then taken through certain observations in Hon'ble Supreme Court's judgment in the case of **CIT Vs Vatika Townships Pvt Ltd [(2014) 367 ITR 466 (SC)]** and relianced is placed on the same for presumption in favour of laws being prospective in nature.

17. Learned Departmental Representative, however, vehemently relied upon the stand of the Assessing Officer which has been approved by the Dispute Resolution Panel. He begins by inviting our attention to the fact that a coordinate bench of this Tribunal, in the case of **Everest Kanto Cylinders Limited Vs DCIT [(2012) 34taxman.com 19 (Mum)]**, has observed that, "So far as the learned Senior Counsel's contention that guarantee commission is not an international transaction and there could not be any method for evaluating the ALP for the guarantee commission, we do not find any merit in the said contention in view of the amendment brought by the Finance Act, 2012 with retrospective effect from 1-4-2002 by way of Explanation added in Section 92B. Payment of guarantee fee is included in the expression 'international transaction' in view of the Explanation i(c) of Section 92B". It is then submitted that this decision of the Tribunal has been

approved by Hon'ble Bombay High Court in the judgment reported as **CIT Vs Everest Kanto Cylinders Limited [(2015) 119 DTR 394 (Bom)]**. As learned Departmental Representative puts it in his written submissions "the above decision of the ITAT has been sustained by Bombay High Court in **[(2015) 58 taxmann.com 254 (Bombay)]** wherein the High Court has not questioned the ITAT's decision with respect to the transaction being an international transaction, but has held that the comparables used by the TPO with respect to this transaction were not proper". He then invites our attention to the amendment brought about in Section 92B of the Act whereby an Explanation is inserted to the said section. It is pointed out that this Explanation, which is specifically stated to have been inserted "for the removal of doubts", it is provided that "the expression 'international transaction' shall include......capital financing, including any type of long term or short term borrowing, lending or guarantee, purchase or sale of marketable securities, or any type of advance payments or deferred payments or receivable or any other debt arising during the course of business". We are then taken through the Memorandum to the Finance Act 2012 in support of the stand that the amendment in law was introduced as (a) the definition of 'international transaction' was cryptic and needed elaboration, (b) the said definition left scope for misinterpretation, and as (c) there was a need to clarify the true scope of the term 'international transaction'. Learned Departmental Representative then refers to the decision of Hon'ble Bombay High Court in the case of **Vodafone India Services Limited Vs Union of India [(2013) 37 taxmann.com 250 (Bombay)]** which holds that effect of this amendment will have to be considered and it can not be brushed aside. Coming to Hon'ble Supreme Court's judgment in the case of **Vatika Townships** *(supra),* he submits that it is categorically stated in the said judgment that the legislative amendment modifying the accrued rights, and imposing obligations or duties or attaching a new disability have to be treated as prospective "unless the legislative amendment is clearly to give the enactment a retrospective effect and unless the amendment is for the purpose of supplying an obvious omission in a former legislation or to explain a former legislation". Our attention is also invited to the observation that "the rule against retrospective operation is a fundamental rule of law that no statute will be construed to have a retrospective operation unless such a construction appears very clearly in the terms of the Act, or arises by necessary and distinct implication". It is pointed out that Hon'ble Supreme Court, in the case of **Vatika Townships** *(supra),* were dealing with a situation in which neither the law was purported to be clarificatory nor there was any material to suggest that it was so intended by the legislature. We were thus urged to hold that the amendment in Section 92 B was retrospective in effect and in law. We were then taken through the decisions of the coordinate benches, which have decided this issue in favour of the revenue, including in the cases of **Foursoft Limited** (ITA No. 1903/Hyd/2011), **Mahindra & Mahindra Ltd Vs DCIT (54 SOT URO 146 Hyd),** and **Prolific Corporation Ltd Vs DCIT [(2015) 68 SOT 104 (Hyd)]**. Coming to **Bharti Airtel** decision *(supra),* learned Departmental Representative states that "Hon'ble Delhi ITAT was not requested by the contesting parties to decide the issue as to whether the provision of guarantee was a service or not" and added that "various Tribunal decisions have already held that provision for bank guarantee is a service and as such it needs to be benchmarked" and that "whether the service has caused any extra cost to the assessee should not be the deciding factor to determine whether it is an international transaction". He then gave an example of brand royalty to illustrate the above proposition. On the basis of this reasoning, learned Departmental Representative urged us to confirm the action of the Assessing Officer and decline to interfere in the matter.

18. In rejoinder, learned counsel for the assessee submitted that it is wholly incorrect to suggest that in Everst Kanto's case Hon'ble Bombay High Court has held the corporate guarantee to be an international transaction. It is pointed out that this issue was never before the Hon'ble High Court. Learned counsel submits that this issue was in principle decided against the assessee by the Tribunal but the reported decision by Hon'ble Bombay High Court was on the appeal filed before Hon'ble Bombay High Court which was confined to the question as to the correctness of comparables adopted on the facts of this case. The question before us now was not even raised before, much less adjudicated by, Hon'ble Bombay High Court. We are taken through the text of the judgment to demonstrate this point. A reference is then

made to Hon'ble Bombay High Court's judgment in the case of **CIT vs. Sudhir Jayantilal Mulji [(1995) 214 ITR 154 (Bom)]**, in support of the proposition that a judicial precedent is only an authority for what it actually decides and not what may come to follow from some observations which find place therein. It is pointed out that the propositions which are assumed by the Court to be correct for the purpose of deciding the same are, according to this judgment of the Hon'ble jurisdictional High Court, lack precedence value and are not binding in nature.Turning to Hon'ble Bombay High Court's decision in the case of **Vodafone India Services Pvt Ltd** *(supra),* learned counsel submits that this decision was in altogether a different context. Learned counsel points out that it was in the context of Section 2(47) but even then it was added that "We do not find it either necessary or proper to indicate the application of section 2(47) as amended to the present proceedings. The application would depend upon the facts on record or those may be permitted to be brought on record" . It was also pointed out that all issues were left open as evident from the observation to the effect "The petitioner may well contend that the amended definition makes no difference it being clarificatory in nature. The provisions thereof must, therefore, be deemed always to have been in existence. We will presume that it would be open to the petitioner to contend, therefore, that the judgment of the Supreme Court would remain entirely unaffected for the Supreme Court must be deemed to have considered the term as per its true ambit, as always intended by the Parliament" and, as such, there was no finding regarding application of amended definition. In these circumstances, according to the learned counsel, Hon'ble High Court's observation that the effect of the amendment would have to be considered is to be taken in the wider context and not simply meaning that the effect of the amendment is to be implemented in its literal sense. We are thus urged to consider the impact of the amendment in accordance with the law as has been done in the case of **Bharti Airtel** *(supra).* Learned counsel once again taken us through Hon'ble Supreme Court's decision in the case of **Vatika Township** *(supra)* and highlights certain observations made therein which, according to the learned counsel show that the stand of the Departmental Representative with regard to the amendment in Section 92 B is clearly contrary to the scheme of law as laid down by a constitutional bench of Hon'ble Supreme Court. A reference is also made to the oft quoted book 'The Principles of Statutory Interpretation (13^{th} Edition 2012)' by Justice G P Singh. It was also submitted that the transfer pricing provisions are set out in the 'special provisions relating to avoidance of tax' under chapter X. These provisions, according to the learned counsel, are normally deeming provisions to check and control the avoidance of tax. A reference is then made to the introduction of General Anti Avoidance Rules in Chapter XA of the Act, and the circumstances leading to its deferral were highlighted. It was submitted that transfer pricing provisions belong to the same genus and what holds good for GAAR also applies to the transfer pricing. Elaborate arguments are then made on the Tribunal decisions cited by the learned Departmental Representative and an effort is made to demonstrate that there is no contrary findings even in these decisions. As for our question as to why issuance of corporate guarantees not be treated as intra group services in the light of OECD guidance on the issue, learned counsel submitted that in the light of the Indian legal position, which is what is material for our adjudication, the issuance of corporate guarantee cannot be treated as a service and even if it is treated as a service, in order to come within the ambit of international transaction, the service should be such that it has "a bearing on profits, incomes, losses or assets of the enterprise". That condition, according to the learned counsel, is admittedly not satisfied on the facts of this case. Without prejudice to this argument, learned counsel invites our attention to information furnished by the Central Board of Direct Taxes, in response to a requisition made under the Right to Information Act, 2005, which is published by the website www.itatonline.org at http://www.itatonline.org/info/index.php/relevance-of-oecd-guidelines-departments-view. On the strength of this information, it is submitted that the revenue authorities cannot lean on the OECD guidelines to make out a case against the assessee when the plain words of statute are in favour of the assessee. We are once again urged to delete the impugned addition in respect of notional charges for the issuance of corporate guarantee.

19. When we put it to the parties as to why this issue should not be sent to a larger bench, none of the parties before us favoured this idea. Learned counsel

submits that there is only decision on the issue is Bharti Airtel decision (supra) which holds that the issuance of corporate guarantee in a situation in which no costs are involved, and this decision has been followed in a number of other cases as well, such as **Redington India Ltd** *(supra),* **Videocon Industries Limited** *(supra).* According to the learned counsel, there are no decisions pointing out anything incorrect, or holding to the contrary, to the said decision. He submits that **Everest Kanto Cylinder Ltd Vs ACIT [(2014) 52 taxmann.com 395 (Mumbai)]**, **Bharti Airtel** *(supra)* decision is distinguished on the ground that guarantee commission has been paid to the bank which is not the case before us. The same was the position with respect to **Aditya Birla Minacs Worldwide Ltd vs DCIT [(2015) 56 taxmann.317 (Mumbi)].** In **Prolific Corporation Ltd Vs DCIT [(2015) 55 taxmann.com 226 (Hyd)]**, according to the learned counsel, the bench has accepted that "there may not be any charge to the P&L account but inherent risk cannot be ruled out in providing guarantees". As for **Hindalco Industries Ltd vs ACIT [(2015) 62 taxmann.com 181 (Mumbai)]**, learned counsel submits that the bench had not held anything to the contrary to what has been decided in Bharti's case even though it has mentioned that the relevant observations were mere obiter dicta. When there is no contrary view expressed by any coordinate bench, according to the learned counsel, there cannot be any occasion to refer it to a larger bench. We are urged to maintain consistency and follow the decision in the case of **Bharti Airtel** *(supra).* Learned Departmental Representative, on the other hand, submits that the law is quite clear, it admits no ambiguity and the matter is now covered, in favour of the assessee, by two binding precedents of Hon'ble Bombay High Court- in cases of **Vodafone India Services** *(supra)* and **Everest Kanto** *(supra).* No useful purpose will be served, according to the learned Departmental Representative, by referring an issue, on which higher judicial forums have adjudicated, to a larger bench of this Tribunal. We are thus urged to follow the decisions of Hon'ble Courts above as also subsequent decisions, following these precedents, of the coordinate benches.

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

21. It is only elementary that the determination of arm's length price, under the scheme of the international transfer pricing set out in the Income Tax Act, 1961, can only be done in respect of an 'international transaction'. Section 92(1) provides that, "(**a)ny income arising from an international transaction shall be computed having regard to the arm's length price**". In order to attract the arm's length price adjustment, therefore, a transaction has to be an 'international transaction' first. The expression 'international transaction' is a defined expression. Section 92 B defines the expression 'international transaction' as follows:

92 B - Meaning of international transaction

(1) For the purposes of this section and sections 92, 92C, 92D and 92E, "international transaction'' means a transaction between two or more associated enterprise s, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises.

(2) A transaction entered into by an enterprise with a person other than an associated enterprise shall, for the purposes of sub-section (1), be deemed to be a transaction entered into between two associated enterprises, if there exists a prior agreement in relation to the relevant transaction between such other person and the associated enterprise, or the terms of the relevant transaction are determined in substance between such other person and the associated enterprise.

Explanation*: - **For the removal of doubts, it is hereby clarified that —**
*(*inserted by the Finance Act 2012, though with retrospective effect from 1st April 2002*)

(i) the expression "international transaction" shall include —

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

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

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

(d) provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service;

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

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

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

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

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

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

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

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

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

(h) human capital related intangible assets, such as, trained and organised work force, employment agreements, union contracts;

(i) location related intangible assets, such as, leasehold interest, mineral exploitation rights, easements, air rights, water rights;

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

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

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

22. As analyzed by a coordinate bench, in the case of **Bharti Airtel** *(supra)* and speaking through one us, the legal position with respect to the above definition is as follows:

25. An analysis of this definition of 'international transaction' under Section 92 B, as it stood at the relevant point of time, and its break up in plain words, shows the following:

An international transaction can be between two or more AEs, at least one of which should be a non-resident.

An international transaction can be a transaction of the following types:

in the nature of purchase, sale or lease of tangible or intangible property,

in the nature of provision of services,

in the nature of lending or borrowing money, or

in the nature of any other transaction having a bearing on the profits, income, losses or assets of such enterprises

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

Section 92B (2), covering a deeming fiction, provides that even a transaction with non AE in a situation in which such a transaction is de facto controlled by prior agreement with AE or by the terms agreed with the AE.

26. Let us now deal with the Explanation, inserted with retrospective effect from 1st April 2002 i.e. right from the time of the inception of transfer pricing legislation in India, which was brought on the statute vide Finance Act, 2012.

27. This Explanation states that it is merely clarificatory in nature inasmuch as it is 'for the removal of doubts', and, therefore, one has to proceed on the basis that it does not alter the basic character of definition of 'international transaction' under Section 92 B. Clearly, therefore, this Explanation is to be read in conjunction with the main provisions, and in harmony with the scheme of the provisions, under Section 92 B. Under this Explanation, five categories of transactions have been clarified to have been included in the definition of 'international transactions'.

28. The first two categories of transactions, which are stated to be included in the scope of expression 'international transactions' by the virtue of clause (a) and (b) of Explanation to Section 92 B, are transactions with regard to purchase, sale, transfer, lease or use of tangible and intangible properties. These transactions were anyway covered by 2 (a) above which covered transactions 'in the nature of purchase, sale or lease of tangible or intangible property'. The only additional expression in the clarification is 'use' as also illustrative and inclusive descriptions of tangible and intangible assets. Similarly, clause (d) deals with the " provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service" which are anyway covered by 2(b) and 3 above in "provision for services" and "mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises ". That leaves us with two clauses in the Explanation to Sect ion 92 B which are not covered by any of the three categories discussed above or by other specific segments covered by Section 92 B, namely borrowing or lending money.

29. The remaining two items in the Explanation to Section 92 B are set out in clause (c) and (e) thereto, dealing with (a) capital financing and (b) business restructuring or reorganization. These items can only be covered in the residual clause of definition in international transactions, as in Section 92B(1), which covers "any other transaction having a bearing on profits, incomes, losses, or assets of such enterprises".

30. It is, therefore, essential that in order to be covered by clause (c) and (e) of Explanation to Section 92 B, the transactions should be such as to have *beating on profits, incomes, losses or assets of such enterprise. In other words, in a situation in which a transaction has no bearing on profits, incomes, losses or assets of such enterprise, the transaction will be outside the ambit of expression 'international transaction'. This aspect of the matter is further highlighted in clause (e) of the Explanation dealing with restructuring and reorganization, wherein it is acknowledged that such an impact could be immediate or in future as evident from the words "irrespective of the fact that it (i.e. restructuring or reorganization) has bearing on the profit, income, losses or assets of such enterprise at the time of transaction or on a future date". What is implicit in this statutory provision is that while impact on " profit, income, losses or assets" is sine qua non , the mere fact that impact is not immediate, but on a future date, would not take the transaction outside the ambit of 'international transaction'. It is also important to bear in mind that, as it appears on a plain reading of the provision, this exclusion clause is not for "contingent" impact on profit, income, losses or assets but on "future" impact on profit, income, losses or assets of the enterprise. The important distinction between these two categories is that while latter is a certainty, and only its crystallization may take place on a future date, there is no such certainty in the former case. In the case before us, it is an undisputed position that corporate guarantees issued by the assessee to the Deutsche Bank did not even have any such implication because no borrowings were resorted to by the subsidiary from this bank.*

*31. In this light now, let us revert to the provisions of clause (c) of Explanation to Section 92B which provides that the expression 'international transaction' shall include "**capital financing, including any type of long -term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business**". In view of the discussions above, the scope of these transactions, as could be covered under Explanation to Section 92 B read with Section 92B(1), is restricted to such capital financing transactions, including inter alia any guarantee, deferred payment or receivable or any other debt during the course of business, as will have "a bearing on the profits, income, losses or assets or such enterprise". This pre-condition about impact on profits, income, losses or assets of such enterprises is a pre-condition embedded in Section 92B(1) and the only relaxation from this condition precedent is set out in clause (e) of the Explanation which provides that the bearing on profits, income, losses or assets could be immediate or on a future date. The contents of the Explanation fortifies, rather than mitigates, the significance of expression 'having a bearing on profits, income, losses or assets' appearing in Section 92B(1).*

32. There can be number of situations in which an item may fall within the description set out in clause (c) of Explanation to Section 92B, and yet it may not constitute an international transaction as the condition precedent with regard to the 'bearing on profit, income, losses or assets' set out in Section

> *92B(1) may not be fulfilled. For example, an enterprise may extend guarantees for performance of financial obligations by its associated enterprises. These guarantees donot cost anything to the enterprise issuing the guarantees and yet they provide certain comfort levels to the parties doing dealings with the associated enterprise. These guarantees thus donot have any impact on income, profits, losses or assets of the assessee. There can be a hypothetical situation in which a guarantee default takes place and, therefore, the enterprise may have to pay the guarantee amounts but such a situation, even if that be so, is only a hypothetical situation, which are, as discussed above, excluded. One may have also have a situation in which there is a receivable or any other debt during the course of business and yet these receivables may not have any bearing on its profits, income, losses or assets, for example, when these receivables are out of cost free funds and these debit balances donot cos t anything to the person allowing such use of funds. The situations can be endless, but the common thread is that when an assessee extends an assistance to the associated enterprise, which does not cost anything to the assessee and particularly for which the assessee could not have realized money by giving it to someone else during the course of its normal business, such an assistance or accommodation does not have any bearing on its profits, income, losses or assets, and, therefore, it is outside the ambit of international transaction under section 92B (1) of the Act.*
>
> *33. In any event, the onus is on the revenue authorities to demonstrate that the transaction is of such a nature as to have "bearing on profits, income, losses or assets" of the enterprise, and there was not even an effort to discharge this onus. Such an impact on profits, income, losses or assets has to be on real basis, even if in present or in future, and not on contingent or hypothetical basis, and there has to be some material on record to indicate, even if not to establish it to hilt, that an intra AE international transaction has some impact on profits, income, losses or assets. Clearly, these conditions are not satisfied on the facts of this case.*

23. Learned Departmental Representative submits that this decision is no longer good law in the light of Everest Kanto decision *(supra)* and Vodafone India Services decision (supra) by Hon'ble Bombay High Court.

24. As for Hon'ble High Court's judgment in the case of Everest Kanto *(supra),* it is necessary to appreciate the fact the assessee was charging a .5% commission on issuance of corporate guarantees, on behalf of the AEs, and it could not, therefore, be said that the transaction will have no impact on "profits, incomes, losses or assets of such enterprise". This aspect of the matter is clear from an observations in the related Tribunal order, which is reported as **Everest Kanto Cylinders Limited Vs**

DCIT [(2012) 34taxman.com 19 (Mum)], to the effect that **"However, in this case, the assessee has itself charged 0.5% guarantee commission from its AE and, therefore, it is not a case of not charging any kind of commission from its AE".** The Tribunal did note, in the immediately following sentence in paragraph 23 itself, that **"the only point to be seen in this case is whether the same is at ALP or not".** The very fact of charging this guarantee commission brings the issuance of corporate guarantees to the net of transfer pricing. Nevertheless, the ALP adjustment made by the TPO was deleted by the Tribunal. Aggrieved by the relief so given by the Tribunal, the matter was carried in further appeal, by the Commissioner, before the Hon'ble Bombay High Court which eventually upheld the relief granted by the Tribunal. The appeal before the Hon'ble High Court was by the Commissioner, and not by the assessee, and, therefore, the grievance against the issuance of corporate guarantee being held to be an international transaction could not have come up for consideration. Of course, the assessee had no occasion to challenge the stand of the Tribunal on this aspect since the addition, on merits, was deleted anyway making revenue's success in this respect hollow and of no damage to the interests of the assessee. It was in this backdrop that the action of the Tribunal was upheld in granting relief to the assessee on merits. It is difficult to understand as to how this decision is taken as supporting the proposition that the issuance of corporate guarantee, even in a case in which neither any guarantee commission is charged nor any costs are incurred, is an international transaction. In any case, there is nothing in the operative portion which even remotely suggests that Their Lordships had any occasion to address themselves to the question as to whether the issuance of corporate guarantee amounts to international transaction. The operative portion of the judgment is reproduced below for ready reference:

> …………In the matter of guarantee commission, the adjustment made by the TPO were based on instances restricted to the commercial banks providing guarantees and did not contemplate the issue of a Corporate Guarantee. No doubt these are contracts of guarantee, however, when they are Commercial banks that issue bank guarantees which are treated as the blood of commerce being easily encashable in the event of default, and if the bank guarantee had to be obtained from Commercial Banks, the higher commission could have been justified. In the present case, it is assessee company that is

issuing Corporate Guarantee to the effect that if the subsidiary AE does not repay loan availed of it from ICICI, then in such event, the assessee would make good the amount and repay the loan. The considerations which applied for issuance of a Corporate guarantee are distinct and separate from that of bank guarantee and accordingly we are of the view that commission charged cannot be called in question, in the manner TPO has done. In our view the comparison is not as between like transactions but the comparisons are between guarantees issued by the commercial banks as against a Corporate Guarantee issued by holding company for the benefit of its AE, a subsidiary company. In view of the above discussion we are of the view that the appeal does not raise any substantial question of law and it is dismissed

25. We are unable to see, in the judgment of Hon'ble Bombay High Court, any support to the proposition that issuance of corporate guarantees is inherently within the ambit of definition of 'international transaction' under section 92B irrespective of whether or not such transactions have any "bearing on profits, incomes, losses, or assets of such enterprises". Revenue, therefore, does not derive any help from the said decision.

26. Coming to Hon'ble Bombay High Court in the case of **Vodafone India Services** *(supra),* which has been relied upon by the learned Departmental Representative, we find that the operative portion of this judgment, so far as relevant to this discussion, is as follows:

213. The amendment to section 2(47) raises several important questions of fact and of law. Whether or not it affects the proceedings which were the subject matter before the Supreme Court is not relevant for the purpose of this Writ Petition. But, whether it is relevant or not for the purpose of the assessment proceedings in respect of the petitioner which are the subject matter of this Writ Petition, is relevant. The effect of the amendment would have to be considered. It cannot be brushed aside.

*214. Section 2(47), as amended, even on a cursory glance raises various issues. It is necessary to note four preliminary aspects of Explanation 2 to section 2(47). Firstly, as the opening words, "**For the removal of doubts it is hereby clarified that ……**", indicate it is a clarificatory amendment. Secondly, it is an inclusive definition as is evident from the words " **"transfer" includes.....**". Thirdly, the amendment is with retrospective effect from 1st April, 1962. Fourthly, the Finance Act 2012 which introduced,* ***inter-alia****, the* *amendment to section 2(47) and section 92CA(2B) is a validating act in view of section 119 thereof.*

215. Explanation 2 to section 247 broadly has four elements.

Disposal or parting with or creating any interest in an asset.

The asset or any interest in the asset.

The disposing of or parting with the asset or creating any interest therein may be:

(a) Direct or indirect.
(b) Absolute or conditional.
(c) Voluntary or involuntarily.
(d) By amendment or otherwise.

(iv) A non-obstante provision regarding the nature of a transfer. If an act, arrangement, transaction etc. constitutes a transfer as defined in the section it would be so notwithstanding the transfer of rights having been categorised as being effected or dependent upon or flowing from the transfer of a share or shares of a company registered or incorporated outside India.

216. Two aspects of a transfer are clarified - the asset itself and the manner in which it is dealt with. The asset is no longer restricted to the asset ***per se*** *or a right therein, but also extends to "****any interest therein****". Prior to the amendment, the words "****any interest therein****" were absent. Further, the nature of the disposal is also expanded. It now includes the creation of any interest in any asset. Moreover, the disposal of or creation of any interest in the asset may be direct or indirect, absolute or conditional, voluntary or involuntary. It may be by way of an agreement or otherwise. Further, the concluding words constitute a non-obstante provision. It provides that the transfer contemplated therein would be notwithstanding that it has been characterised as being effected or dependent upon or flowing from the transfer of a share or shares of a company registered or incorporated outside India.*

It would be evident, therefore, that a lot more must now be seen and considered than before while arriving at a conclusion whether the terms and conditions of the Framework agreement constituted a transfer or assignment of the call options by one party to another.

217. ***At the cost of repetition, we are not concerned here with whether the amendment is valid or not. One of the issues, however, that does arise is whether the amendment, albeit clarificatory, would make a difference in the construction of the provisions*** *of the Framework agreements themselves, to wit as regards the construction of the clauses* *thereof without the aid of any other material for interpreting them. Vodafone's case obviously considered the ambit of the term "transfer" prior to the amendment.* ***In the present assessment proceedings, it is the amended definition which would have to be considered.***

218. We do not find it either necessary or proper to indicate the application of section 2(47) as amended to the present proceedings. ***The application would depend upon the facts on record or those may be permitted to be brought on record.***

219. There is another aspect. ***The petitioner may well contend that the amended definition makes no difference it being clarificatory in nature****. The provisions thereof must, therefore, be deemed always to have been in existence.* ***We will presume that it would be open to the petitioner to contend, therefore,*** *that the judgment of the Supreme Court would remain entirely unaffected for the Supreme Court must be deemed to have considered the term as per its true ambit, as always intended by the Parliament. On the other hand, it may be equally open to the Revenue to contend that certain ingredients of a transfer were not considered by the Revenue itself in the proceedings relating to Vodafone's case on account of the Revenue itself not having appreciated or realized the actual ambit of the term "transfer" which are now clarified by the amendment. Even assuming that the Revenue cannot re-open the Vodafone case, it cannot be barred from relying upon the true ambit of the term "transfer" in future cases, including the proceedings in respect of the petitioner. Thus, even assuming that the judgment of the Supreme Court remains unaffected by the clarificatory amendment, the Revenue would be entitled hereafter in other cases, at least, to appreciate, analyze and construe the transactions relating to call options, including the Framework agreements in a proper perspective which it may not have done earlier.*

*220****. These are important issues. There is no justification for withdrawing the proceedings from the channel provided by the Income Tax Act, bypassing the Tribunal and considering all these questions in exercise of the High Court's extra-ordinary jurisdiction under Article 226***

(Emphasis, by underlining, supplied by us)

27. Revenue's emphasis is on the last two sentences in paragraph no 213 which state that "**The effect of the amendment would have to be considered. It cannot be brushed aside"** but in doing so what it overlooks is the subsequent observations highlighted above which recognize the fact that merely because a subsequent Explanation is introduced by the legislature, it is not an open and shut case against the assessee or the revenue, and that all these observations are in the context that

"**there is no justification for withdrawing the proceedings from the channel provided by the Income Tax Act, bypassing the Tribunal and considering all these questions in exercise of the High Court's extra-ordinary jurisdiction under Article 226".** When Their Lordships have made it clear that they would not like to bypass the channels under the Income Tax Act and proceed to decide these issues in writ jurisdiction under article 226, there cannot obviously be any question of Their Lordships deciding the matter one way or the other. Any observations made by Their Lordships, while declining to decide the matter in writ jurisdiction, cannot be treated as decisive of the issue on merits. While it is true that Hon'ble Bombay High Court has observed that the effect of amendment will have to be considered, Hon'ble Bombay High Court has also observed that even after taking into account the amendments, the legal implications of this amendment is still an open issue which will have to be adjudicated in the light of pleadings of the parties. Even in these observations, which donot anyway decide anything on merits, effect of a retrospective amendment was not in the context of the precise issue before us, or on the scope of the international transaction, but in respect of connotations of 'transfer'. As learned counsel rightly contends, in the light of Hon'ble Bombay High Court's judgment in the case of **Sudhir Jayantilal Mulji** *(supra) "*ratio of a decision alone is binding, because a case is only an authority for what it actually decides and not what may come to follow from some observations which find place therein"**.** In view of these discussions, the reliance placed on **Vodafone India Services** *(supra)* is also equally misplaced and devoid of legally sustainable merits. In any case, as is noted by Hon'ble Supreme Court in the case of **CIT Vs Sun Engineering Works Pvt Ltd (1992) 198 ITR 297 (SC)],** "It is neither desirable nor permissible to pick out a word or a sentence from the judgment of this Court, divorced from the context of the question under consideration and treat it to be the complete "law" declared by this Court. The judgment must be read as a whole and the observations from the judgment have to be considered in the light of the questions which were before this Court" Their Lordships further noted that "A decision of this Court takes its colour from the questions involved in the case in which it is rendered and, while applying the decision to a later case, the Courts must carefully try to ascertain the true principle laid down by the decision of this Court and not to pick out words or sentences from the judgment, divorced from the context of the questions under consideration by this Court, to support their reasoning**"** It was also recalled that in **Madhav Rao Jivaji Rao Scindia Bahadur vs. Union of India (1971) 3 SCR 9 : AIR 1971 SC 530,** Hon'ble Supreme Court had cautioned that "It is not proper to regard a word, clause or a sentence occurring in a judgment of the Supreme Court, divorced from its context, as containing a full exposition of the law on a question when the question did not even fall to be answered in that judgment." That precisely, however, has been the approach of the revenue authorities in placing reliance on **Vodafone India Services** *(supra)* decision. We reject this approach.

28. For the reasons set out above, learned Departmental Representative's reliance on Hon'ble Bombay High Court's judgments in the cases of Everest Kanto (supra) and Vodafone India Services (supra) is wholly misplaced and devoid of any merits. As for co-ordinate bench decision in the case of Hindalco Industries (supra), all it does is to follow the Everest Kanto decision by Hon'ble Bombay High Court, but then, as we have seen earlier, that was a case in which Their Lordships were *in seisin* of a situation in which guarantee commission was actually charged by the assessee. That is not the case before us. The coordinate bench decisions dealing with the situations in which the guarantee commission was actually charged, and as such there was indeed a bearing on the profits of the assessee, clearly donot apply on this case. We, therefore, reject the reliance on these decisions as devoid of legally sustainable merits.

29. Let us now deal with the reliance placed by the revenue authorities on GE Capital's case by the Tax Court of Canada. In the DRP's order, a reference is made to well known Canadian decision in the case of **GE Capital Canada** *(supra).* The said case, to quote the words of the DRP, "also shows that the group company issuing the guarantee (i.e. guarantor) would, in principle, at least need to cover the cost that it incurs with respect to providing the guarantee" and that "these costs may include administrative expenses as well as the costs of maintaining an appropriate

level of cash equivalents, capital, subsidiary credit lines or more expensive external funding conditions on other debt finance". The DRP had also noted that "in addition, the guarantor would want to receive appropriate compensation for the risk it incurs" and concluded that "following the above discussions, an arm's length guarantee fees is typically required to be determined by establishing a range of fees that the guarantor would, at least, want to receive and the fees that the guaranteed group company would be willing to pay depending on the prevailing conditions within financial markets in practice".

30. However, while dealing with this aspect of the matter, it is necessary to bear in mind the fact that this judicial precedent, whatever be its worth in the hierarchy of binding judicial precedents in India, does not even deal with the fundamental question as to whether issuance of a corporate guarantee is an international transaction at all- which is what we are concerned with at present. This TCC decision dealt with a situation in which the assessee was denied, in computation of its business income, tax deduction for payment of guarantee fees on the ground that there was no effective benefit to the assessee, in obtaining the said guarantee. Aggrieved by denial of deduction, assessee carried the matter in appeal before the Canadian Tax Court, and the plea of the assessee was eventually upheld. It is also interesting to note that as a sequel to this Tax Court of Canada decision, the transfer pricing legislation was amended, to bring greater clarity on the issue and as a measure of abundant caution, and section 247 (7.1), granting specific exemption to guarantee fees, was introduced. This amendment is as follows:

> (7.1) Subsection (2) does not apply to adjust an amount of consideration paid, payable or accruing to a corporation resident in Canada (in this subsection referred to as the "parent") in a taxation year of the parent for the provision of a guarantee to a person or partnership (in this subsection referred to as the "lender") for the repayment, in whole or in part, of a particular amount owing to the lender by a non-resident person, if (a) the non-resident person is a controlled foreign affiliate of the parent for the purposes of section 17 throughout the period in the year during which the particular amount is owing; and (b) it is established that the particular amount would be an amount owing described in paragraph 17(8)(a) or (b) if it were owed to the parent.
> (http://www.fin.gc.ca/drleg-apl/ita-lrir-dec12-l-eng.pdf)

31. It is also important to bear in mind the fact that, under the Canadian law, the definition of 'international transaction', unlike an exhaustive definition under section 92B of the Indian Income Tax Act, 1961, is a very brief but inclusive and broad definition to the effect that **"'transaction' includes a series of transactions, an arrangement or an event"** [See Section 247(1) of the Canadian Income Tax Act, 1985; http://laws-lois.justice.gc.ca/eng/acts/I-3.3/page-419.html#h-156] coupled with the legal position that arm's length adjustment to the prices of such transaction come into play "**Where a taxpayer or a partnership and a non-resident person with whom the taxpayer or the partnership, or a member of the partnership, does not deal at arm's length**" [See Section 247(2) *ibid*]. When one takes into account these variations in the statutory provisions, it will become very obvious that the provisions of the Indian Income Tax Act, 1961 and the Canadian Income Tax Act, 1985 are so radically different that just because a particular transaction is to be examined on arm's length principle in Canada cannot be a reason enough to hold that it must meet the same in India as well. While the Canadian transfer pricing legislation, as indeed the transfer pricing legislation in many other jurisdictions, does not put any fetters on the nature of transactions between the AEs, so as to be covered by the arm's length price adjustment, and, therefore, covers all transactions between the related enterprises, Indian transfer pricing legislation covers only such transactions as are **"in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises".** Our transfer pricing provisions, perhaps being in the quest of comprehensive coverage, have ended up in a limited scope of the transactions being covered by the arm's length price adjustments for transfer pricing. In any event, as emphasized earlier as well, the decision was in the context of the deduction, and, post this decision, a specific amendment was introduced in the Canadian transfer pricing law to clarify the position that all corporate guarantees issued by the assessee, in support of its subsidiaries, are not necessarily international transactions. Revenue, therefore, does not derive any advantage from the Tax Court of Canada's decision in the case of GE Capital Canada. There are

many more aspects which make this decision wholly irrelevant in the present context but suffice to say that relevant legal provisions and context being radically different, the reliance of this decision must be rejected for this short reason alone.

32. As we take note of the above legal position in Canada, it is appropriate to take note of the concept of '**shareholder activities'** in the context of corporate guarantees which provides conceptual justification for exclusion of corporate guarantees, under certain conditions, from the scope of transfer pricing adjustments. Taking note of these proposed amendments, **'Transfer Pricing and Intra Group Financing – by Bakker & Levvy, IBFD publication (ISBN- 978-90-8722-153-9)'** observes that **"Proposed subsection 247(7.1) of the ITA provides that the transfer pricing rules will not apply to guarantees provided by Canadian parent corporations in respect of certain financial commitments of their Canadian controlled foreign affiliates to support the active business operations of those affiliates"**. As to what could be conceptual support for such an exclusion, we find interesting references in a discussion paper issued by the Australian Tax Officer in June 2008 and titled as "**Intra-group finance guarantees and loans**" (http://www.transferpricing.com/pdf/Australia_Thin%20Capitalisation.pdf). The fact that this discussion paper did not travel beyond the stage of the discussion paper is not really relevant for the present purposes because all that we are concerned with right now is understanding the conceptual basis on which, contrary to popular but apparently erroneous belief, the issuance of corporate guarantees can indeed be kept outside the ambit of services. The relevant extracts from this document are as follows:

> 102. An independent company that is unable to borrow the funds it needs on a stand-alone basis is unlikely to be in a position to obtain a guarantee from an independent party to support the borrowings it needs. Where such a guarantee is given it compensates for the inadequacies in the financial position of the borrower; specifically, the fact that the subsidiary does not have enough shareholders' funds. .....
>
> 103. It would not be expected that a company pay for the acquisition of the equity it needs for its formation and continued viability. Equity is generally supplied by the shareholders at their own cost and risk.

> 104. Accordingly to the extent that a guarantee substitutes for the investment of the equity needed to allow a subsidiary to be self-sufficient and raise the debt funding it needs, the costs of the guarantee (and the associated risk) should remain with the parent company providing the guarantee.

33. On a conceptual note, thus, there is a valid school of thought that the corporate guarantees can indeed be a mode of ownership contribution, particularly when, as is often the case, **"where such a guarantee is given it compensates for the inadequacies in the financial position of the borrower; specifically, the fact that the subsidiary does not have enough shareholders' funds".** There can be number of reasons, including regulatory issues and market conditions in the related jurisdictions, in which such a contribution, by way of a guarantee, would justify to be a more appropriate and preferred mode of contribution vis-a-vis equity contribution. It is significant, in this context, that the case of the assessee has all along been, as noted in the assessment order itself, that "**said guarantees were in the form of corporate guarantees/ quasi capital and not in the nature of any services**". In other words, these guarantees were specifically stated to be in the nature of shareholder activities. The assessee's claim of the guarantees being in the nature of quasi capital, and thus being in the nature of a shareholder's activity, is not rejected either. The concept of issuance of corporate guarantees as a shareholder activity is not alien to the transfer pricing literature in general. On the contrary, it is recognized in international transfer pricing literature as also in the official documentation and legislation of several transfer pricing jurisdictions. The '**OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations**' itself recognizes the distinction between a shareholder activity and a provision for services, when, contrasting the shareholder activity with broader term "stewardship activity" and thus highlighting narrow scope of shareholder activity, it states that "**Stewardship activities <u>covered a range of activities by a shareholder that may *include* provision for services to other group members</u>, for example services that would be provided by a coordinating centre**". It proceeded to add, in the immediately following sentence at page 207 of 2010 Guidelines, that "**These latter type of non-shareholder activities could include detailed planning services for**

particular operations, management or technical advice (trouble shooting) or in some cases assistance in day to day management". The shareholder activities are thus seen as conceptually distinct from the provision of services. The issuance of corporate guarantee, as long as it is in the nature of shareholder activity, can not, therefore, amount to a "provision for services".

34. Undoubtedly, pioneering work done by the OECD, in the field of international taxation, has been judicially recognized worldwide by various judicial forums, including, most notably by Hon'ble Andhra Pradesh High Court in the case of **CIT VS Visakhapatnam Port Trust [(1983) 144 ITR 146 (AP)].** Their Lordships also referred to Lord Radcliffe's observations in **Ostime vs. Australian Mutual Provident Society [(1960) 39 ITR 210 (HL)]**, which has described the language employed in the models developed by the OECD as the "international tax language". The work done by OECD in the field of transfer pricing is no less significant. No matter which part of the world we live in, and irrespective of whether or not that tax jurisdiction is an OECD member jurisdiction, the immense contribution of the OECD, in the field of the transfer pricing as well, is admired and respected. However, the relevance of this work, so far as interpretation to transfer pricing legislation is concerned, must remain confined to the areas which have remained intact from legislative or judicial guidance. There is no scope for parallel or conflicting guidance by such forums. Legislation is an exclusive domain of the sovereign, and, therefore, as long as an area is adequately covered by the work of legislation, things like guidance of the OECD, or for that purpose any other multilateral forum, are not decisive. While we are alive to the school of thought that when the domestic transfer pricing regulations do not provide any guidelines, it may have to be decided having regard to international best practices, we donot quite agree with it inasmuch as, in our considered view, Revenue cannot seek to widen the net of transfer pricing legislation by taking refuge of the best practices recognized by the OECD work.

35. While dealing with "special consideration for intra group services", the 'OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax

Administrations' has noted that there are two fundamental issues with respect to the intra group services- first, whether intra group services have indeed been provided, and, second- if the answer to the first question is in positive, that charge to these services should be at an arm's length price. Dealing with the first question, which is relevant for the present purposes, these Guidelines (2010 version) state as follows:

> 7.6 Under the arm's length principle, the question whether an intra-group service has been rendered when an activity is performed for one or more group members by another group member should depend on whether the activity provides a respective group member with economic or commercial value to enhance its commercial position. This can be determined by considering whether an independent enterprise in comparable circumstances would have been willing to pay for the activity if performed for it by an independent enterprise or would have performed the activity in-house for itself. If the activity is not one for which the independent enterprise would have been willing to pay or perform for itself, the activity ordinarily should not be considered as an intra-group service under the arm's length principle.
>
> 7.7 The analysis described above quite clearly depends on the actual facts and circumstances, and it is not possible in the abstract to set forth categorically the activities that do or do not constitute the rendering of intra-group services. However, some guidance may be given to elucidate how the analysis would be applied for some common types of activities undertaken in MNE groups.
>
> 7.8 Some intra-group services are performed by one member of an MNE group to meet an identified need of one or more specific members of the group. In such a case, it is relatively straightforward to determine whether a service has been provided. Ordinarily an independent enterprise in comparable circumstances would have satisfied the identified need either by performing the activity in-house or by having the activity performed by a third party. Thus, in such a case, an intra-group service ordinarily would be found to exist. For example, an intra-group service would normally be found where an associated enterprise repairs equipment used in manufacturing by another member of the MNE group.
>
> 7.9 A more complex analysis is necessary where an associated enterprise undertakes activities that relate to more than one member of the group or to the group as a whole. In a narrow range of such cases, an intra-group activity may be performed relating to group members even though those group members do not need the activity (and would not be willing to pay for it were they independent enterprises). Such an activity would be one that a group member (usually the parent company or a regional holding company) performs solely because of its ownership interest in one or more other group

members, i.e. in its capacity as shareholder. This type of activity would not justify a charge to the recipient companies. It may be referred to as a "shareholder activity", distinguishable from the broader term "stewardship activity" used in the 1979 Report. Stewardship activities covered a range of activities by a shareholder that may include the provision of services to other group members, for example services that would be provided by a coordinating centre. These latter types of non-shareholder activities could include detailed planning services for particular operations, emergency management or technical advice (trouble shooting), or in some cases assistance in day-to-day management.

7.10 The following examples (which were described in the 1984 Report) will constitute shareholder activities, under the standard set forth in paragraph 7.6:

a) Costs of activities relating to the juridical structure of the parent company itself, such as meetings of shareholders of the parent, issuing of shares in the parent company and costs of the supervisory board;

b) Costs relating to reporting requirements of the parent company including the consolidation of reports;

c) Costs of raising funds for the acquisition of its participations.

In contrast, if for example a parent company raises funds on behalf of another group member which uses them to acquire a new company, the parent company would generally be regarded as providing a service to the group member. The 1984 Report also mentioned "costs of managerial and control (monitoring) activities related to the management and protection of the investment as such in participations". Whether these activities fall within the definition of shareholder activities as defined in these Guidelines would be determined according to whether under comparable facts and circumstances the activity is one that an independent enterprise would have been willing to pay for or to perform for itself.

(Emphasis, by underlining, supplied by us)

36. We have noticed that the 'OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations' specifically recognizes that an activity in the nature of shareholder activity, which is solely because of ownership interest in one or more of the group members, i.e. in the capacity as shareholder **"would not justify a charge to the recipient companies"**. It is thus clear that a shareholder activity, in issuance of corporate guarantees, is taken out of ambit of the group services. Clearly, therefore, as long as a guarantee is on account of, what can be termed as

'shareholder's activities', even on the first principles, it is outside the ambit of transfer pricing adjustment in respect of arm's length price. It is essential to appreciate, at this stage, the distinction in a service and a benefit. One may be benefited even when no services are rendered, and, therefore, in many a situation it's a 'benefit test' which is crucial for transfer pricing legislation, such as in US Regulations 1.482-9(1)(3)(i) which defines 'benefit', form a US Transfer Pricing perspective, as "**an activity is considered to be provide a benefit to the recipient if the activity directly results in a reasonably identifiable increment of economic or commercial value that enhances the recipient's commercial position, or that may be reasonably anticipated to do so**". The expression "**activity**", in turn is defined, as "**including the performance of functions; the assumption of risks; the use by a rendered of tangible or intangible property or other resources capabilities or knowledge (including knowledge of and ability to take advantage of a particularly advantageous situation or circumstances); and making available to the recipient any property or other resources of the rendered**" [Regulation 1.482-9(1)(2)]. The issuance of guarantees is not within the ambit of transfer pricing in United States because it is a service but because it is covered by the specific definition discussed above. As a matter of fact, David S Miller, in a paper titled '**Federal Income Tax Consequences of Guarantees; A Comprehensive Framework for Analysis'** published in the 'The American Lawyer Vol. 48, No. 1 (Fall 1994), pp. 103-165 (http://www.jstor.org/stable/20771688), has stated that a guarantee is not a service. The following observations, at pages 114, are important:

> **The position that guarantees are services has been discredited by the courts with good reason[38]. Guarantee fees do not represent payments for services any more than payments with respect to other financial instruments constitute payment for services[39]. A guarantor does not arrange financing for the debtor, but merely executes a financial instrument in its favour.**
>
> *[38]See. e.g., Centel Communications Co. V. Commissioner, 92 T.C. 612, 632 (1989), aff d, 920 F2d 1335 (7th Cir. 1990); Bank of Am. V. United States, 680 F.2d 142, 150 (Cl. Ct. 1982). The Service's current position on the characterization of guarantee*

fees as payment for services under section 482 is inconsistent with its treatment of guarantee fees under other provisions. See P.L.R. 9410008 (Dec. 13, 1993).

[39]But cf Federal Nat'l Mortgage Ass'n v. Commissioner, 100 T.C. 541, 579 (1993) (Fannie Mae provided services by buying mortgages).

37. We are in agreement with these views. There can thus be activities which benefit the group entities but these activities need not necessarily be 'provision for services'. The fact that the OECD considers such activities in the services segment does not alter the character of the activities. While the group entity is thus indeed benefited by the shareholder activities, these activities do not necessarily constitute services. There is no such express reference to the benefit test, or to the concept of benefit attached to the activity, in relevant definition clause of 'international transaction' under the domestic transfer pricing legislation. As we take note of these things, it is also essential to take note of the legal position, in India, in this regard. No matter how desirable is it to read such a test in the definition of the international transaction' under our domestic transfer pricing legislation, as is the settled legal position, it is not open to us to infer the same. Hon'ble Supreme Court, in the case of **Tarulata Shyam Vs CIT [(1977) 108 ITR 351 (SC)]**, took note of the situation before Their Lordships in these words: "We have given anxious thoughts to the persuasive arguments of Mr Sharma. His arguments, if accepted, will certainly soften the rigour of this extremely drastic provision and bring it more in conformity with logic and equity". However, Their Lordships declined to do so on the ground that "There is no scope for importing into the statute the words which are not there. Such importation would be not to construe but to amend the statue". Their Lordships noted that "Even if there be *casus omissus*, the defect can be remedied only by legislation and not by judicial interpretation". The benefit test, which is set out in the OECD Guidance and which finds its place in the international best practices, does not find its place in the main definition of international transaction, even though there is a reference to the expression 'benefit' in the context of cost or expense sharing arrangements but that is a different aspect of the matter altogether. In the absence of benefit test being mentioned in the definition for the present purposes, we cannot infer the same.

38. One more thing which is clearly discernable from the above discussions is that the tests recognized by these guidelines are interwoven twin tests of benefit and arm's length. Benefit test implies the recipient group member should get "economic or commercial value to enhance its commercial position". The benefit test is interlinked with the an arm's length test in the sense that it seeks an answer to the question whether under a similar situation an independent enterprise would have been willing to pay for the activity concerned, or would have performed the activity in-house for itself. So far as the benefit test is concerned, as we have noted earlier, it is alien to the definition of international transaction' under the Indian transfer pricing legislation. So far as arm's length test is concerned, it presupposes that such a transaction is possible in arm's length situation. However, in a situation in which the subsidiary does not have adequate financial standing of its own and is inadequately capitalized, none will guarantee financial obligations of such a subsidiary.

39. The issuance of financial guarantee in favour of an entity, which does not have adequate strength of its own to meet such obligations, will rarely be done. The very comparison, between the consideration for which banks issue financial guarantees on behalf of its clients with the consideration for which the corporates issue guarantees for their subsidiaries, is ill conceived because while banks seek to be compensated, even for the secured guarantees, for the financial risk of liquidating the underlying securities and meeting the financial commitments under the guarantee, the guarantees issued by the corporates for their subsidiaries are rarely, if at all, backed by any underlying security and the risk is entirely entrepreneurial in the sense that it seeks to maximize profitability through and by the subsidiaries. It is inherently impossible to decide arm's length price of a transaction which cannot take place in arm's length situation. The motivation or trigger for issuance of such guarantees is not the kind for consideration for which a banker, for example, issue the guarantees, but it is maximization of gains for the recipient entity and thus the MNE group as a whole. In general, thus, the consideration for issuance of corporate guarantees are of a different character altogether.

40. At this stage, it would appropriate to analyze the business model of bank guarantees, with which corporate guarantees are sometimes compared, in the context of benchmarking the arm's length price of corporate guarantees. A bank guarantee is a surety that that the bank, or the financial institution issuing the guarantee, will pay off the debts and liabilities incurred by an individual or a business entity in case they are unable to do so. By providing a guarantee, a bank offers to honor related payment to the creditors upon receiving a request. This requires that bank has to be very sure of the business or individual to whom the bank guarantee is being issued. So, banks run risk assessments to ensure that the guaranteed sum can be retrieved back from the business. This may require the business to furnish a security in the shape of cash or capital assets. Any entity that can pass the risk assessment and provide security may obtain a bank guarantee. The consideration for the issuance of bank guarantee, so far as a banker is concerned, is this. When the client is not able to honour the financial commitments and when client is not able to meet his financial commitments and the bank is called upon to make the payments, the bank will seek a compensation for the action of issuing the bank guarantee, and for the risk it runs inherent in the process of making the payment first and realizing it from the underlying security and the client. Even when such guarantees are backed by one hundred percent deposits, the bank charges a guarantee fees. In a situation in which there is no underlying assets which can be realized by the bank or there are no deposits with the bank which can be appropriated for payment of guarantee obligations, the banks will rarely, if at all, issue the guarantees. Of course, when a client is so well placed in his credit rating that banks can issue him clean and unsecured guarantees, he gets no further economic value by a corporate guarantee either. Let us now compare this kind of a guarantee with a corporate guarantee. The guarantees are issued without any security or underlying assets. When these guarantees are invoked, there is no occasion for the guarantor to seek recourse to any assets of the guaranteed entity for recovering payment of defaulted guarantees. The guarantees are not based on the credit assessment of the entity, in respect of which the guarantees are issued, but are based on the business needs of the entity in question. Even in a situation in

which the group entity is sure that the beneficiary of guarantee has no financial means to reimburse it for the defaulted guarantee amounts, when invoked, the group entity will issue the guarantee nevertheless because these are compulsions of his group synergy rather than the assurance that his future obligations will be met. We see no meeting ground in these two types of guarantees, so far their economic triggers and business considerations are concerned, and just because these instruments share a common surname, i.e. 'guarantee', these instruments cannot be said to be belong to the same economic genus. Of course, there can be situations in which there may be economic similarities, in this respect, may be present, but these are more of an exception than the rule. In general, therefore, bank guarantees are not comparable with corporate guarantees.

41. As evident from the OECD observation to the effect "**In contrast, if for example a parent company raises funds on behalf of another group member which uses them to acquire a new company, the parent company would generally be regarded as providing a service to the group member",** it is also to be clear that when the corporate guarantees are issued for the purpose of subsidiaries raising funds for acquisitions by such subsidiaries, these guarantees will be deemed to be services to the subsidiaries, and, as a corollary thereto, when corporate guarantees are issued for the subsidiaries to raise funds for their own needs, the corporate guarantees are to be treated as shareholder activity. The use of borrowed funds for own use is a reasonable presumption as it is a matter of course rather than exception. There has to be something on record to indicate or suggest that the funds raised by the subsidiary, with the help of the guarantee given by the assessee, are not for its own business purposes. As a plain look at the details of corporate guarantees would show, these guarantees were issued to various banks in respect of the credit facilities availed by the subsidiaries from these banks. The guarantees were *prima facie* in the nature of shareholder activity as it was to provide, or compensate for lack of, core strength for raising the finances from banks. No material, indicating to the contrary, is brought on record in this case. Going by the OECD Guidance also, it is not really possible to hold that the corporate guarantees

issued by the assessee were in the nature of 'provision for service' and not a shareholder activity which are mutually exclusive in nature. In the light of these discussions, we are of the considered view, and are fully supported by the OECD Guidance in this, that the issuance of corporate guarantees, in the nature of quasi capital or shareholder activity- as is the uncontroverted position on the facts of this case, does not amount to a service in which respect of which arm's length adjustment can be done.

42. As observed by Hon'ble Delhi High Court in the case of **CIT Vs EKL Appliances Ltd [(2012) 345 ITR 241 (Del)],** a re-characterization of a transaction is indeed permissible, inter alia, in a situation "(i) where the economic substance of a transaction differs from its form and (ii) where the form and substance of the transaction are the same but arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner". The case of a corporate guarantee clearly falls in the second category as no independent enterprise would issue a guarantee without an underlying security as has been done by the assessee. We may, in this regard, refer to the observations made by Hon'ble High Court, speaking through Hon'ble Justice Easwar (as he then was), as follows:

> *16. The Organization for Economic Co-operation and Development ('OECD', for short) has laid down "transfer pricing guidelines" for Multi-National Enterprises and Tax Administrations. These guidelines give an introduction to the arm's length price principle and explains article 9 of the OECD Model Tax Convention. This article provides that when conditions are made or imposed between two associated enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises then any profit which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, if not so accrued, may be included in the profits of that enterprise and taxed accordingly. By seeking to adjust the profits in the above manner, the arm's length principle of pricing follows the approach of treating the members of a multi-national enterprise group as operating as separate entities rather than as inseparable parts of a single unified business. After referring to article 9 of the model convention and stating the arm's length principle, the guidelines provide for "recognition of the actual transactions undertaken" in paragraphs*

1.36 to 1.41. Paragraphs 1.36 to 1.38 are important and are relevant to our purpose. These paragraphs are re-produced below: -

> *"1.36 A tax administration's examination of a controlled transaction ordinarily should be based on the transaction actually undertaken by the associated enterprises as it has been structured by them, using the methods applied by the taxpayer insofar as these are consistent with the methods described in Chapters II and III. In other than exceptional cases, the tax administration should not disregard the actual transactions or substitute other transactions for them. Restructuring of legitimate business transactions would be a wholly arbitrary exercise the inequity of which could be compounded by double taxation created where the other tax administration does not share the same views as to how the transaction should be structured.*
>
> *1.37 However, there are two particular circumstances in which it may, exceptionally, be both appropriate and legitimate for a tax administration to consider disregarding the structure adopted by a taxpayer in entering into a controlled transaction. The first circumstance arises where the economic substance of a transaction differs from its form. In such a case the tax administration may disregard the parties' characterization of the transaction and re-characterise it in accordance with its substance. An example of this circumstance would be an investment in an associated enterprise in the form of interest-bearing debt when, at arm's length, having regard to the economic circumstances of the borrowing company, the investment would not be expected to be structured in this way. In this case it might be appropriate for a tax administration to characterize the investment in accordance with its economic substance with the result that the loan may be treated as a subscription of capital. The second circumstance arises where, while the form and substance of the transaction are the same, the arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner and the actual structure practically impedes the tax administration from determining an appropriate transfer price. An example of this circumstance would be a sale under a long-term contract, for a lump sum payment, of unlimited entitlement to the intellectual property rights arising as a result of future research for the term of the contract (as previously indicated in paragraph 1.10). While in this case it may be proper to respect the transaction as a transfer of commercial property, it would nevertheless be appropriate for a tax administration to conform the terms of that transfer in their entirety (and not simply by reference to pricing) to those that might reasonably have been expected had the transfer of property been the subject of a transaction involving independent enterprises. Thus, in the case described above it might be appropriate for the tax administration, for*

> > *example, to adjust the conditions of the agreement in a commercially rational manner as a continuing research agreement.*
> >
> > *1.38 In both sets of circumstances described above, the character of the transaction may derive from the relationship between the parties rather than be determined by normal commercial conditions as may have been structured by the taxpayer to avoid or minimize tax. In such cases, the totality of its termswould be the result of a condition that would not have been made if the parties had been engaged in arm's length dealings. Article 9 would thus allow an adjustment of conditions to reflect those which the parties would have attained had the transaction been structured in accordance with the economic and commercial reality of parties dealing at arm's length."*
>
> *17. The significance of the aforesaid guidelines lies in the fact that they recognise that barring exceptional cases, the tax administration should not disregard the actual transaction or substitute other transactions for them and the examination of a controlled transaction should ordinarily be based on the transaction as it has been actually undertaken and structured by the associated enterprises. It is of further significance that the guidelines discourage re-structuring of legitimate business transactions. The reason for characterisation of such re-structuring as an arbitrary exercise, as given in the guidelines, is that it has the potential to create double taxation if the other tax administration does not share the same view as to how the transaction should be structured.*
>
> *18. Two exceptions have been allowed to the aforesaid principle and they are (i) where the economic substance of a transaction differs from its form and (ii) where the form and substance of the transaction are the same but arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner.*

43. It is thus clear that even if we accept the contention of the learned Departmental Representative that issuance of a corporate guarantee amounts to a 'provision for service', such a service needs to be re-characterized to bring it in tune with commercial reality as "arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner". No bank would be willing to issue a clean guarantee, i.e. without underlying asset, to assessee's subsidiaries when the banks are not willing to extend those subsidiaries loans on the same terms as without a guarantee. Such a guarantee transaction can only be, and is, motivated

by the shareholder, or ownership considerations. No doubt, under the OECD Guidance on the issue, an explicit support, such as corporate guarantee, is to be benchmarked and, for that purpose, it is in the service category but that occasion comes only when it is covered by the scope of 'international transaction' under the transfer pricing legislation of respective jurisdiction. The expression 'provision for services' in its normal or legal connotations, as we have seen earlier, does not cover issuance of corporate guarantees, even though once a corporate guarantee is covered by the definition of international transaction', it is benchmarked in the service segment. In view of the above discussions, OECD Guidelines, as a matter of fact, strengthen the claim of the assessee that the corporate guarantees issued by the assessee were in the nature of quasi capital or shareholder activity and, for this reason alone, the issuance of these guarantees should be excluded from the scope of services and thus from the scope of 'international transactions' under section 92B. Of course, once a transaction is held to be covered by the definition of international transaction, whether in the nature of the shareholder activity or quasi capital or not, ALP determination must depend on what an independent enterprise would have charged for such a transaction. In this light of these discussions, we hold that the issuance of corporate guarantees in question was not in the nature of 'provision for services' and these corporate guarantees were required to be treated as shareholder participation in the subsidiaries.

44. As for the words 'provision for services" appearing in Section 92 B, and connotations thereof, our humble understanding is that this expression, in its natural connotations, is restricted to services rendered and it does not extend to the benefits of activities *per se*. Whether we look at the examples given in the OECD material or even in Explanation to Section 92 B, the thrust is on the services like market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, and scientific research, legal or accounting service or coordination services. As a matter of fact, even in the Explanation to Section 92 B- which we will deal with a little later, guarantees have been grouped in item 'c' dealing with capital financing, rather than in item 'd' which

specifically deals with 'provision for services'. When the legislature itself does not group 'guarantees' in the 'provision for services' and includes it in the 'capital financing', it is reasonable to proceed on the basis that issuance of guarantees is not to be treated as within the scope of normal connotations of expression 'provision for services'. Of course, the global best practices seem to be that guarantees are sometimes included in 'services' but that is because of the extended definition of 'international transaction' in most of the tax jurisdictions. Such a wide definition of services, which can be subject to arm's length price adjustment, apart, "Transfer Pricing and Intra Group Financing – by Bakker & Levvy" *(ibid)* notes that "the IRS has issued a non binding Field Service Advice (FSA 1995 WL 1918236, 1 May 1995) stating that, <u>in certain circumstances</u> *(emphasis, by underling, supplied by us),* a guarantee may be treated as a service". If the natural connotations of a 'service' were to cover issuance of guarantee in general, there could not have been an occasion to give such hedged advice. This will be stretching the things too far to suggest that just because when guarantees are included in the international transactions, these guarantees are included in service segment in contradistinction with other heads under which international transactions are grouped, the guarantees should be treated as services, and, for that reason, included in the definition of international transactions. That is, in our considered view, purely fallacious logic. In our considered view, under Section 92 B, corporate guarantees can be covered only under the residuary head i.e. "**any other transaction having a bearing on the profits, income, losses or assets of such enterprise".** It is for this reason that Section 92 B, in a way, expands the scope of international transaction in the sense that even when guarantees are issued as a shareholder activity but costs are incurred for the same or, as a measure of abundant caution, recoveries are made for this non chargeable activity, these guarantees will fall in the residuary clause of definition of international transactions under section 92B. As for the learned Departmental Representative's argument that "whether the service has caused any extra cost to the assessee should not be the deciding factor to determine whether it is an international and then gives an example of brand royalty to make his point. What, in the process, he overlooks is that is that Section 92B(1) specifically covers

sale or lease of tangible or intangible property". The expression **"bearing on the profits, income, losses or assets of such enterprises"** is relevant only for residuary clause i.e. any other services not specifically covered by Section 92 B. It was also contended that, while rendering Bharti Airtel decision, the Delhi Tribunal did go overboard in deciding something which was not even raised before us. In the written submission, it was stated that "Hon'ble Delhi ITAT was not requested by the contesting parties to decide the issue as to whether the provision of guarantee was a service or not". That's not factually correct. We are unable to see any merits in learned Departmental Representative's contention, particularly as decision categorically noted that not only before the Tribunal, but this issue was also raised before the DRP- as evident from the text of DRP decision. We now take up the issue with respect to specific mention of the words in Explanation to Section 92B which states that "**For the removal of doubts, it is hereby clarified that (i) the expression "international transaction" shall include…….. (c) capital financing, including any type of long -term or short -term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business.**" There is no dispute that this Explanation states that it is merely clarificatory in nature inasmuch as it is 'for the removal of doubts', and, therefore, one has to proceed on the basis that it does not alter the basic character of definition of 'international transaction' under Section 92 B. Accordingly, this Explanation is to be read in conjunction with the main provisions, and in harmony with the scheme of the provisions, under Section 92 B. Under this Explanation, five categories of transactions have been clarified to have been included in the definition of 'international transactions'. The first two categories of transactions, which are stated to be included in the scope of expression 'international transactions' by the virtue of clause (a) and (b) of Explanation to Section 92 B, are transactions with regard to purchase, sale, transfer, lease or use of tangible and intangible properties. These transactions were anyway covered by transactions 'in the nature of purchase, sale or lease of tangible or intangible property'. The only additional expression in the clarification is 'use' as also illustrative and inclusive descriptions of tangible and intangible assets. Similarly, clause (d) deals with the " provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service" which are anyway covered in "provision for services" and "mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises ". That leaves us with two clauses in the Explanation to Sect ion 92 B which are not covered by any of the three categories discussed above or by other specific segments covered by Section 92 B, namely borrowing or lending money. The remaining two items in the Explanation to Section 92 B are set out in clause (c) and (e) thereto, dealing with (a) capital financing and (b) business restructuring or reorganization. These items can only be covered in the residual clause of definition in international transactions, as in Section 92B (1), which covers "any other transaction having a bearing on profits, incomes, losses, or assets of such enterprises". It is, therefore, essential that in order to be covered by clause (c) and (e) of Explanation to Section 92 B, the transactions should be such as to have beating on profits, incomes, losses or assets of such enterprise. In other words, in a situation in which a transaction has no bearing on profits, incomes, losses or assets of such enterprise, the transaction will be outside the ambit of expression 'international transaction'. This aspect of the matter is further highlighted in clause (e) of the Explanation dealing with restructuring and reorganization, wherein it is acknowledged that such an impact could be immediate or in future as evident from the words "irrespective of the fact that it *(i.e. restructuring or reorganization)* has bearing on the profit, income, losses or assets of such enterprise at the time of transaction or on a future date". What is implicit in this statutory provision is that while impact on " profit, income, losses or assets" is *sine qua non* , the mere fact that impact is not immediate, but on a future date, would not take the transaction outside the ambit of 'international transaction'. It is also important to bear in mind that, as it appears on a plain reading of the provision, this exclusion clause is not for “contingent” impact on profit, income, losses or assets but on “future” impact on profit, income, losses or assets of the enterprise. The important distinction between these two categories is that while latter is a certainty, and only its crystallization may take place on a future date, there is no such certainty in the former case. In the case before us, it is an undisputed position that corporate guarantees issued by the assessee to the various banks and crystallization of liability under these guarantees, though a possibility, is not a certainty. In view of the discussions above, the scope of the capital financing transactions, as could be covered under Explanation to Section 92 B read with Section 92B(1), is restricted to such capital financing transactions, including *inter alia* any guarantee, deferred payment or receivable or any other debt during the course of business, as will have “a bearing on the profits, income, losses or assets or such enterprise”. This pre-condition about impact on profits, income, losses or assets of such enterprises is a pre-condition embedded in Section 92B(1) and the only relaxation from this condition precedent is set out in clause (e) of the Explanation which provides that the bearing on profits, income, losses or assets could be immediate or on a future date. These guarantees do not have any impact on income, profits, losses or assets of the assessee. There can be a hypothetical situation in which a guarantee default takes place and, therefore, the enterprise may have to pay the guarantee amounts but such a situation, even if that be so, is only a hypothetical situation, which are, as discussed above, excluded. When an assessee extends an assistance to the associated enterprise, which does not cost anything to the assessee and particularly for which the assessee could not have realized money by giving it to someone else during the course of its normal business, such an assistance or accommodation does not have any bearing on its profits, income, losses or assets, and, therefore, it is outside the ambit of international transaction under section 92B (1) of the Act.

45. Before we part with this issue, there are a couple of things that we would like to briefly deal with.

46. The first issue is this. We find that in the case of **Four Soft Ltd Vs DCIT [(2011) 142 TTJ 358 (Hyd)]**, a co-ordinate bench had, vide order dated 9th September 2011, observed as follows:

> "We find that the TP legislation provides for computation of income from international transaction as per Section 92B of the Act. The corporate guarantee provided by the assessee company does not fall within the definition of international transaction. The TP legislation does not stipulate any guidelines in respect to guarantee transactions. In the absence of any charging provision, the lower authorities are not correct in bringing aforesaid transaction in the TP study. In our considered view, the corporate guarantee is very much incidental to the business of the assessee and hence, the same cannot be compared to a bank guarantee transaction of the Bank or financial institution."

47. However, within less than four months of this decision having been rendered, the Finance Act 2012 came up with an Explanation to Section 92B stating that "**for the removal of doubts**", as we have noted earlier in this decision, "**clarified**" that international transactions include, *inter alia*, capital financing by way of guarantee. This legislative clarification did indeed go well beyond what a coordinate bench of this Tribunal held to be the legal position and we are bound by the esteemed views of the coordinate bench. We are, therefore, of the opinion that the Explanation to Section 92 B did indeed enlarge the scope of definition of 'international transaction' under section 92B, and it did so with retrospective effect. If, for argument sake, it is assumed that the insertion of Explanation to Section 92B did not enlarge the scope of definition, there cannot obviously be any occasion to deviate from the decision that the coordinate bench took in Four Soft case *(supra),* but if the scope of the provision was indeed enlarged, as is our opinion, the question that really needs to be addressed whether, given the peculiar nature and purpose of transfer pricing provision, is it at all a workable idea to enlarge the scope of transfer pricing provisions with retrospective effect There can be little doubt about the legislative competence to amend tax laws with retrospective effect, and, in any case, we are not inclined to be drawn into that controversy either. On the issue of implementing the amendment in transfer pricing law with retrospective effect, in the case of Bharti Airtel *(supra),* a coordinate bench had observed as follows:

> 34. There is one more aspect of the matter. The Explanation to Section 92 B has been brought on the statute by the Finance Act 2012. If one is to proceed on the basis that the provisions of Explanation to Section 92 B enlarges the scope of Section 92 B itself, even as it is modestly describe d as 'clarificatory' in nature, it is an issue to be examined whether an enhancement of scope of this anti avoidance provision can be implemented with retrospective effect. Undoubtedly, the scope of a charging provision can be enlarged with retrospective effect, but an anti-avoidance measure, that the transfer pricing legislation inherently is, is not primarily a source of revenue as it mainly seeks compliant behaviour from the assessee vis-à-vis certain norms, and these norms cannot be given effect from a date earlier than the date norms are being introduced. However, as we have decided the issue in favour of the assessee on merits and even after taking into account the amendments brought about by Finance Act 2012, we need not deal with this aspect of the matter in greater detail

48. In the present case, we have held that the issuance of corporate guarantees were in the nature of shareholder activities- as was the uncontroverted claim of the assessee, and, as such, could not be included in the 'provision for services' under the definition of 'international transaction' under section 92 B of the Act. We have also held, taking note of the insertion of Explanation to Section 92B of the Act, that the issuance of corporate guarantees is covered by the residuary clause of the definition under section 92 B of the Act but since such issuance of corporate guarantees, on the facts of the present case, did not have "bearing on profits, income, losses or assets", it did not constitute an international transaction, under section 92B, in respect of which an arm's length price adjustment can be made. In this view of the matter, and for both these independent reasons, we have to delete the impugned ALP adjustment. The question, which was raised in Bharti Airtel's case (supra) but left unanswered as the assessee had succeeded on merits, reamins unanswered here as well. However, we may add that in the case of **Krishnaswamy S PD Vs Union of India [(2006) 281 ITR 305 (SC)],** wherein Their Lordships had, inter alia, observed that "**the law does not compel a man to do what he cannot possibly perform. The law itself and its administration is understood to disclaim as it does in its general aphorisms, all intention of compelling impossibilities, and the administration of law must adopt that general exception in the consideration of particular cases**. It was for this reason that a

coordinate bench of this Tribunal, in the case of **Channel Guide India Ltd Vs ACIT [(2012) 139 ITD 49 (Mum**)], held that even though the assessee had not deducted the applicable tax at source under section 195, the disallowance could not be made under section 40(a)(i) since the taxability was under the provisions which were amended, post the payment having been made by the assessee, with retrospective effect. All this only shows that even when law is specifically stated to have effect from a particular date, its being implemented in a fair and reasonable manner, within the framework of judge made law, may require that date to be tinkered with. When a proviso is introduced with effect from a particular date specified by the legislature, the judicial forums, including this Tribunal, at times read it as being effect from a date much earlier than that too. One such case, for example, is **CIT Vs Ansal Landmark Township Pvt Ltd [(2015) 377 ITR 635 (Delhi)]** wherein Hon'ble Delhi High Court confirmed the action of the Tribunal in holding that the provision, though stated to be effective from 1st April 2013 must be held to be effective from 1st April 2005. Whether such an exercise can be done in the present case is, of course, something to be examined and our observations should not be construed as an expression on merits of that aspect of matter. Given the fact that the assessee has succeeded on merits in this case, it would not really be necessary to deal with that aspect of the matter.

49. The second issue is this. We must deal with the question whether in this case the matter should have been referred to a larger bench. The parties before us were opposed to the matter being sent for consideration by the special bench, and at least one of the reasons for which the grievance of the assessee is upheld, i.e. guarantees being in the nature of shareholder activity and excludible from the scope of services for that reason alone, is an area which had come up for consideration for the first time. In effect, therefore, there was no conflict on this issue of and the other issues, given decision on the said issue, were wholly academic. It cannot be open to refer the academic questions to the special bench. No doubt, some decisions of the coordinate benches which have reached the different conclusions. There is, however, no conflict in the reasoning. Four Soft decision *(supra)* had decided the

issue in favour of the assessee but that was with respect to the law prior to insertion to Explanation to Section 92B. As for the post amendment law and the impact of amendment in the definition of 'international transaction', the matter was again decided in favour of the assessee by Bharti Airtel decision *(supra)* on the peculiar facts of that case. The decisions like Everest Kento *(supra) and* Aditya Birla Minacs Worldwide *(supra)* were decisions in which the assessee had charged the fees and, for that reason, such cases are completely distinguishable as discussed above. In Prolific's case *(supra),* as indeed in any other case so far, it was case not the case of the assessee that corporate guarantees are quasi capital, or shareholder activity, in nature, and, for that reason, excludible from chargeable services, even if these are held to be services in nature. That plea has been specifically accepted in the present case. Therefore, the question whether issuance of corporate guarantee *per se* in general constitutes a 'international transaction' under section 92B would have been somewhat academic question on the facts of this case. In any event, in Prolific's case *(supra),* an earlier considered decision on the same issue by coordinate bench of equal strength was simply disregarded and that fact takes this decision out of the ambit of binding judicial precedents. We have also noted that in view of the decision a coordinate bench, in the case of **JKT Fabrics Vs DCIT [(2005) 4 SOT 84 (Mum)]** and following the Full bench decision of Hon'ble AP High Court in the case of CIT Vs **BR Constructions [(1993) 202 ITR 222 (AP)],** a decision disregarding an earlier binding precedent on the issue is *per incurium*. Such decisions cannot be basis for sending the matters to special bench since occasion for reference to special bench arises when binding and conflicting judicial precedents from coordinate benches come up for consideration. That was not the case here. All these factors taken together, in our considered view, it was not possible in this case to refer the matter for constitution of a special bench. In any case, whatever we decide is, and shall always remain, subject to the judicial scrutiny by Hon'ble Courts above and our endeavor is to facilitate and expedite, within our inherent limitations, that process of such a judicial scrutiny, if and when occasion comes, by analyzing the issues in a comprehensive and holistic manner.

50. In the light of the detailed discussions above, and for the detailed reasons set out above, we uphold the grievance raised by the assessee. The impugned ALP adjustment of Rs 2,23,62,603, thus stands deleted. As we do so, however, we must add that, in our considered view, the way forward, to avoid such issues being litigated and to ensure satisfactorily resolution of these disputes, must include a clear and unambiguous legislative guidance on the transfer pricing implications of the corporate guarantees as also on the methodology of determining its ALP, if necessary. Of course, no matter how good is the legislative framework, the importance of a very comprehensive analysis, in the transfer pricing study, of the nature of corporate guarantees issued by the assesses, can never be overemphasized. The sweeping generalizations, vague statements and evasive approach in the transfer pricing study reports, which are quite common in most of the transfer pricing reports, cannot do good to a reasonable cause. When judicial calls on the complex transfer pricing issues are to be taken, utmost clarity in the legislative framework and a comprehensive analysis of relevant facts, in the transfer pricing documentation, are basic inputs. Unfortunately, both of these things leave a lot to be desired. We can only hope, and we do hope, that things will change for better.

51. Ground no. 3 is thus also allowed.

52. In ground no.4, the assessee has raised the grievance that the Assessing Officer has erred in not accepting the profits of various units as declared by the appellant company by reducing certain items as adjustments for inter division transfer and adjusting the same to the business income of various units as under while granting deduction u/s. 80IB and 10B.

53. Learned Representatives fairly agree that the issue is covered in favour of the assessee, by the orders of the co-ordinate bench in assessee's own cases for the assessment years 2002-2003 and 2005-06, to the extent that the matter is required to be remitted to the file of Assessing Officer for fresh adjudication in the light of the directions set out in those orders. We are, thus, urged to remit the matter to the file

of the Assessing Officer for fresh adjudication in the light of Tribunal's order for the assessment years 2002-03 and 2005-06, even as learned. Departmental Representative dutifully relied upon the stand of the Assessing Officer.

54. We see no reasons to take any other view of the matter than the view taken by the co-ordinate benches. Respectfully following these views, we remit the matter to the file of the Assessing Officer with the direction to adjudicate the matter afresh in the light of, inter alia, the directions given for the assessment years 2002-03 which has been followed in Assessment Year 2005-06 as well. Ordered, accordingly.

55. Ground no.4 is thus allowed for statistical purposes in the terms indicated above.

56. In ground no.5, the assessee has raised the following grievance against the Assessing Officer's including excise duty, sales tax, insurance and freight while calculating the amount of total turnover for the purpose of working out deduction u/s. 10B of the Act.

57. With the consent of the parties, this issue is remitted to the file of the Assessing Officer for fresh adjudication on merits by way of a speaking order, in accordance with the law and after giving yet another opportunity of hearing to the assessee. The assessee will be at liberty to raise all such factual and legal aspects, as he may be advised to.

58. Ground no. 5 is also thus allowed for statistical purpose.

59. In ground no.6, the assessee has raised the following grievance:

On appreciation of the facts and circumstances of the case and law, the Learned Addl. Commissioner of Income Tax has erred in excluding the following items of income while granting deduction u/s. 80IB

Amount Rs.

	Silvassa-I	Silvassa-I-I
Other Income:-		
Income from sale of scrap	48,01,099	26,89,679
Discount on purchase of DEPB	1,33,662	1,42,902
Gain on sale of DFRC	1,81,694	5,209
Insurance Claim	2,55,382	4,41,751
Other Operating Income:-		
Income from DEPB/DFRC	5,82,963	3,68,68,545

60. So far as this ground is concerned, learned representatives fairly agree that as far as income from sale of scrap is concerned, the issue is covered in favour of the assessee by the order of co-ordinate bench in assessee's own case for the Assessment Year 2005-06. As regards discount on purchase of DEPB, Gain on sale of DFRC, Insurance claim, Income from DEPB/DFRC, following order of another coordinate bench in assessee's own case for assessment year 2005-06, the matter is required to be sent back to the file of Assessing Officer for fresh adjudication. Learned Departmental Representative does not seriously oppose the matter being remitted to the file of Assessing Officer but relies on the stand of the Assessing Officer.

61. We see no reasons to take any other view of the matter than the view taken by the Co-ordinate bench. Respectfully following the same, as far as the income from sale of scrap to the tune of Rs.48,01,099/- for Silvassa-I and Rs.26,89,679/- for Silvassa-II Units, we direct the Assessing Officer to include the same in computation of deduction under section 80IB. As regards remaining items, on the line of orders for the earlier years, we direct the Assessing Officer to adjudicate the mater fresh in the light of directions of the coordinate benches in accordance with law and by way of a speaking order.

62. Ground no.6 is also thus allowed for statistical purposes.

63. In ground no.7 the assessee has raised the following grievance :-

"On appreciation of the facts and circumstances of the case, the learned Addl. Commissioner of Income Tax has erred in making addition to the tune of Rs.1,03,272/- and Rs.8,83,622/- pertaining to telephone and electricity expenses of Managing Director respectively, claimed by the appellant company as revenue expenditure. The action of the Learned Addl. Commissioner of Income Tax is contrary to the facts and law and deserves to be deleted."

64. On this issue also, the learned representatives fairly agree that the issue is covered by the order of co-ordinate bench for the assessment year 2005-06 in the sense that, on the same lines, while disallowance in respect of electricity expenses of Rs.8,83,622/- is to be confirmed, the disallowance of telephone expenses to the tune of Rs.1,03,272/- is to be deleted. In this issue also, we see no reasons to deviate from the stand taken by the co-ordinate bench in the earlier year and respectfully following the same, we delete the disallowance of telephone expenses and confirm the disallowance of electricity expenses as above. To the limited extent of deleting the disallowance of telephone expenses of Rs.1,03,272, the assessee gets the relief.

65. Ground no.7 is thus partly allowed in the terms indicated above.

66. In ground no.8, the assessee has raised the following grievance:-

"On appreciation of the facts and circumstances of the case, the Learned Addl. Commissioner of Income Tax has erred in making addition out of software expenses to the tune of Rs.51,22,143/- claimed as revenue expenditure by the appellant company. The action of the Learned Addl. Commissioner of Income Tax is contrary to the facts and law and deserves to be deleted."

67. So far as this grievance of the assessee is concerned, the material facts are like this. During the course of assessment proceedings, the Assessing Officer noted that the assessee had debited Rs.11,86,371 towards professional fees for implementation of SAP software, user license (for SAP software) and user license for other software. When the Assessing Officer required the assessee to show cause as to why this expenditure not be treated as capital expenditure, the assessee

submitted that the expenses incurred on implementing the SAP software is mainly increasing the efficiency of the assessee- company so far as the financial results are concerned. It was also submission that these expenses do not give enduring benefit and frequent updating of software required. The Assessing Officer, however, did not agree with any of the arguments and proceeded to treat the same as capital expenditure. The benefit of the additional depreciation was, nonetheless, allowed. The total deprecation thus allowed was Rs.67,41,569/-. In effect, a disallowance of Rs.51,22,143/- was made to the total income of the assessee. Aggrieved, the assessee did raise grievance before the DRP but without any success. The DRP rejected the grievance of the assessee by, *inter alia,* observing as follows:-

> The various submissions made by the assessee in this regard have been carefully considered by us and are not found acceptable. With effect from 01.04.2003, computer software has been classified as tangible asset under heading “Plant” in Appendix-I to the Rules which is entitled to deprecation @ 60%. In the various decisions relied upon by the assessee, the aforesaid change brought with effect from 01.04.2003 in the I.T. Rules has not been considered by the Hon’ble Courts and the same are therefore distinguishable from the facts of the assessee’s case.
>
> The decision of Hon’ble ITAT Pune ‘B’ Bench in the case of Sudarshan Chemical Industries Ltd. vs. Assistant Commissioner of Income-tax, 110 ITD 171 (Pune) is directly on this issue and the Hon’ble Tribunal in the said decision has held as under :
>
>> The expression “a know-how, a patent, a copy right and a trademark”, are examples of ‘intellectual property’, or a license acquired in respect of such a property, are all ‘intangible assets’ under clause (ii) of Section 32(1). In view of the discussion made above, explaining the nature and scope of the ERP implementation and the software used for this purpose, there is no doubt that the R/3 software and a license to use this software were both ‘intangible assets’ within the meaning of clause (ii) of Section 32(1)”
>
> In view of the above, the disallowance of Rs.51,22,143/- proposed by the AO as a result of treating the said amount of Rs.1,18,63,712/- as capital expenditure and allowing depreciation @ 60% there on is hereby confirmed.

68. The assessee is aggrieved and is in appeal before us.

69. Having heard the rival contentions and having perused the material on record, we see no reasons to interfere in the matter. The reason is this. Learned counsel for the assessee has primarily relied upon the decision of Hon'ble jurisdictional High Court in the case of **CIT Vs NJ India Invest Pvt Ltd [(2013) 32 taxmann.com 367 (Guj)]** but then that is hardly of any assistance because that was a case in which the expenditure was incurred in the "nature of maintenance, back up and support service to the existing hardware and software already installed by the company for the purpose of its business" and not on the new software per se. The situation before us is materially different. This is a case when ERP has been introduced for the first time and the expenditure is not in the support or maintenance of the existing software.We, therefore, approve the stand of the authorities below on this point and decline to interfere in the matter.

70. Ground no 8 is thus dismissed.

71. In the result, the appeal is partly allowed in the terms indicated above. Pronounced in the open court today on 27th day of November, 2015.

Sd/xx	Sd/xx
S S Godara	**Pramod Kumar**
(Judicial Member)	**(Accountant Member)**

Dated: the 27th day of November, 2015.

Copies to:	*(1)*	*The appellant*	*(2)*	*The respondent*
	(3)	*DIT*	*(4)*	*DRP*
	(5)	*DR*	*(6)*	*Guard File*

By order etc

Assistant Registrar
Income Tax Appellate Tribunal
Ahmedabad benches, Ahmedabad