IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCHES : I : NEW DELHI

BEFORE SHRI R.S. SYAL, AM & SHRI C.M. GARG, JM

ITA No.945/Del/2915
Assessment Year : 2010-11

Mitsubishi Corporation India, Private Limited, Birla Tower, 5th Floor, Barakhamba Road, New Delhi – 110 001.	vs.	DCIT, Circle 16 (2), New Delhi.
(PAN : AAACM4764G)		
(APPELLANT)		(RESPONDENT)

Assessee By : Shri M.S. Syali, Sr. Advocate
Shri Tarandeep Singh, Advocate
Shri Harkunal Singh, Advocate
Department By : Shri Sanjay Prasad, CIT DR

Date of Hearing : 22.05.2015
Date of Pronouncement : 26.05.2015

O R D E R

PER R.S. SYAL, AM :

This appeal by the assessee is directed against the order passed by the Assessing Officer under Section 143 (3) read with Section 144C of the Income-tax Act, 1961 (hereinafter also called "the Act") in relation to the assessment year 2010-11.

2. First ground of the appeal is against the addition on account of transfer pricing adjustment amounting to Rs.9,62,59,809/-.

3. Succinctly, the assessee, an Indian company, is a wholly owned subsidiary of Mitsubishi Corporation, Japan (MCJ), a general trading company headquartered in Tokyo. MCJ is one of Japanese leading sogo shosha, engaged in linking buyers and sellers of various products across the globe. The assessee reported certain international transactions in Form 3CEB. The only international transaction in dispute is "Service fee received" amounting to Rs.2,66,29,622/-. In order to demonstrate that its international transactions were at Arm's Length Price (ALP), the assessee employed the Transactional Net Margin Method (TNMM) as the most appropriate method. Certain comparables were chosen. By using the multiple-year data of the comparables, the assessee tried to show that its international transactions were at ALP. The TPO rejected the assessee's use of multiple-year data and restricted it to the current year alone. While scrutinizing the international transaction of `Service fee'

received amounting to Rs.2.66 crores, the assessee was called upon to state the cost of goods in the hands of the associated enterprises (AEs) on which such service fee was received. The assessee submitted the cost of such goods at Rs.6,65,58,05,980/- in the hands of its AE, on which it had earned the above referred Service fee. The TPO proposed to treat the `Service commission' segment as equivalent to the Trading segment. The assessee's cost base of Service Fee segment was accordingly worked out at Rs.6,82,08,06,478/-, by clubbing the cost of goods amounting to Rs.665.58 crore incurred by the AEs and expenses of Rs.16.50 crore incurred by the assessee in India under the Service fee segment. The TPO chose some comparable companies and determined the average of their OP/TC at 3.00%, which was proposed to the assessee for comments. After entertaining objections raised by the assessee as regards the selection of comparables etc., the TPO reduced the mean OP/TC of comparables and determined the arm's length margin at 2.16%. This resulted into a transfer pricing adjustment to the tune of Rs.9,62,59,809/-. The assessee objected to the addition made by the AO in the draft order on account of this transfer pricing adjustment before the Dispute Resolution Panel (DRP). Vide its Direction dated 16.12.2014, the DRP approved the action of the TPO/AO. The assessee is contesting this addition amounting to Rs.9.62 crore made by the AO.

4. We have heard the rival submissions and perused the relevant material on record. It can be observed from the international transactions reported by the assessee that apart from earning Service fee amounting to Rs. 2.66 crore, being the commission income for co-ordinating between the buyers and sellers in the capacity of an agent, it also indulged into trading activity by directly making purchases and sale of goods on principal to principal basis. Segment-wise results of the assessee from trading and service/commission segments are available at page 592 of the paper book. Thus, it is evident that the assessee did direct purchase and sale transactions with its AEs and also acted as a service provider in the sale of their goods. There is no dispute as regards the transactions undertaken by the assessee under the `Trading segment' on which operating profit was

determined by reducing purchase and other operating costs from the sale value. The TPO has accepted such trading transactions at ALP. The controversy is only *qua* the agency segment, under which `Service fee' was received without making purchase or sale of goods as an owner. In such circumstances, the question arises as to whether the cost of goods, for which the assessee simply provided services by acting as an agent, can be considered in the hands of the assessee and the transaction of receipt of `Service fee' be treated as that of a trading nature? In our considered opinion, the answer to this question can not be in affirmative. The fact that the assessee did not purchase and sell the goods under the `Service fee' segment, has not been disputed by the TPO. There is no finding given by the Officer that the assessee actually undertook trading but wrongly gave it a colour of agency in its books of account. Once the position is that the assessee sold the goods as an agent of its AEs and simply earned commission, how the cost of such goods in the hands of the AE can be taken into consideration and the entire transaction be considered as that of sale and purchase, is anybody's guess. We do not subscribe to the view canvassed by the TPO in this regard. By equating commission business with the trading business, the TPO has ventured to recharacterize the commission transaction as a trading transaction, which is patently unacceptable. The Hon'ble jurisdictional High Court in *CIT VS. EKL Appliances Ltd. (2012) 345 ITR 241 (Delhi)* has held that the authorities should not disregard the actual transaction or substitute other transactions for them. Examination of a controlled transaction should ordinarily be based on the transaction as it has been actually undertaken. Further, their Lordships have carved out two exceptions to the aforesaid principle, viz., (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. Neither the TPO has taken recourse to any of these exceptions nor there is any material on record to justify the bringing of the instant case within their sweep. *Ex consequenti,* it is manifest that the authorities below erred in recharacterizing a commission transaction into a trading transaction.

5. One of the fundamental conditions for making a transfer pricing analysis is that the international transaction must broadly match with a comparable uncontrolled transaction. If the character of the original international transaction is tinkered with certain permutations and combinations so as to make it fit for making a comparison with an adjusted uncontrolled transactions, it will lead to incongruous results, thereby rendering the entire exercise of determining ALP, a futility. By combining the cost of goods incurred by the AE with the expenses incurred by the assessee, the TPO has embarked upon treating the foreign AE as well as the assessee as tested parties to one transaction. Such an approach has no sanction of law. The Hon'ble Delhi High Court in *Li & Fung (India) P. Ltd. Vs. CIT (2014) 361 ITR 85 (Del)* has repelled an approach similar to the one adopted in the instant case. The Mumbai bench of the tribunal in *Onward Technologies Ltd. Vs. DCIT (2013) 36 CCH 46 (Mum)* has also held that the

tested party in an international transaction can only be the assessee and not its foreign AE.

6. Adverting to the facts of the instant case, we find it as an admitted position that the assessee simply rendered agency services under this segment by co-ordinating between customers and its AEs. By no standard, the assessee can be said to have dealt with the goods of its AEs as an absolute owner. Once position is such, we fail to comprehend as to how financial results of the commission segment can be adjusted for making a comparison with trading segment. The ld. AR has drawn our attention towards the Tribunal orders passed in assessee's own case for the earlier years reversing similar stand of the Revenue authorities on the international transaction of receipt of Service fee. As such, we set aside the impugned order on this score and remit the matter to the TPO/AO for a fresh determination of ALP of the international transaction of receipt of `Service fee' as per law after allowing a reasonable opportunity of being heard to the assessee. In doing so, the assessee will initially propose comparable instances having undertaken activity similar to it

under this segment. Then it will be for the TPO to decide on their comparability or otherwise and determine the ALP of this transaction as per law. We further add that in doing so, the TPO will consider the figures of the comparables for the current year alone and not the multiple-year data as has been held by the Hon'ble jurisdictional High Court in *ChrysCapital Investment Advisors (India) P. Ltd. VS. DCIT* (Del) vide its judgment dated 27.4.2015.

7. The next ground of the appeal is against the disallowance of Rs.70,37,18,502/- made under section 40(a)(i) of the Act.

8. The facts apropos this ground are that the assessee made purchases from its AEs as under : -

S.No.	Name and Address of the AE	Description of transaction	Amount of purchases (Rs.)
1	Asia Modified Starch Co. Ltd. 130-132 Sindhorn Building, 2nd Floor, Tower 1, Wireless Road, Lumpini Pathumwan, Bangkok-10330, Thailand	Import of goods	3,506,647
2	Mitsubishi Corporation Unimetals, (Japan) 8-1, Akashicho, Chuo-Ku, Tokyo-104-6591, Japan	Import of goods	29,926,820
3	Mitsubishi Corporation Unimetals, (Japan) Head Office, 3-1, Marunouchi 2 – Chome, Chiyoda-Ku, Tokyo, Japan	Import of goods	14,758,916,057

4	Mitsubishi Corporation, Singapore 1 Temasek Avenue, #19-00 Millenia Tower, Singapore 0391921	Import of goods	6,658,981,033
5	Mitsubishi International GmbH, Germany Hamburg Brnach, Maattenwiete 5, Hamburg	Import of goods	17,610,327
6	Mitsubishi Shoji Chemical Corporation, 6-1, Kyobashi, 1-Chome, Chuo-Ku, Tokyo 104-0031	Import of goods	16,669,779
7	Petro Diamond Japan Corporation 4th Floor, Mitsubishi Corp. Building, 6-3, Marunouchi 2-Chome, Chiyoda-Ku, Tokyo 100-0005	Import of goods	2,566,470
8	Thai MC Company Limited Thailand 968, 24th Floor, U-Chuliang, Foundation Rama 4 Road Silon, Bangrak, Bangkok, Thailand	Import of goods	32,266,358
9	Total		21,520,443,490

9. The Assessing Officer observed that the assessee paid/credited the accounts of its AE suppliers without deduction of tax at source in terms of section 195 of the Act. On being show-caused as to why disallowance be not made under section 40(a)(i) of the Act towards such purchases made from non-resident group companies, the assessee stated that the Tribunal has deleted such disallowance for the assessment year 2006-07 by observing that in some cases, the group entities did not have a permanent establishment in India, while in others, the assessee

was entitled to the benefit of non-discrimination clause in the Double Taxation Avoidance Agreement between India and Japan (DTAA). The facts of the instant year were claimed to be similar to the said earlier year. Reliance was also placed on certain other tribunal decisions in support of the assessee's entitlement for making the payment of purchase price without deduction of tax at source. Not convinced, the Assessing Officer held that the assessee was required to deduct tax at source on the business profits of these companies as per the provisions of section 195 of the Act. In holding so, he followed the view taken by him for the immediately preceding year, that is, A.Y. 2009-10. He also relied on Instruction dated 26.02.2014 issued by the CBDT and thus computed the amount of disallowance under section 40(a)(i) at Rs.70,37,18,502/- by applying gross profit rate of 6.54% (as applied for the assessment year 2009-10) on total purchase transactions of Rs.2152.04 crore and attributing 50% of the same to the business operations of such companies in India. This resulted into an addition of Rs.70.37 crore, against which the assessee has come up in appeal before us.

10. We have heard the rival submissions and perused the relevant material on record. The AO has made disallowance u/s 40(a)(i) of the Act in respect of purchases made by the assessee from its seven AEs to whom payments were made without deduction of tax at source. First category consists of purchase transactions entered with its six related parties situated in Japan, Thailand and Germany. The case of the assessee is that these non-resident AEs did not have any permanent establishment during the year in India and, hence, income arising from sale of goods to India could not be charged to tax under the Act in their hands. Second category comprises of items at serial nos. 3 and 4 of the above Table which are, in fact, purchases made by the assessee from MCJ including its branch office. The ld. AR contended that the AO wrongly recorded the Mitsubishi Corporation, Singapore, at serial no. 4 as a separate entity, which is only a branch of MCJ, indicated at serial no. 3. This contention was not controverted by the ld. DR with any material/evidence to the contrary. The ld. AR argued that no deduction of tax at source was warranted from the payments made to MCJ in view of non-

discrimination clause in the DTAA. We will deal with these two categories of transactions, one by one.

11. First we espouse the category of purchases made from six foreign AEs, for which the ld. AR claimed that they did not have any PE in India and made off shore sales to the assessee, not leading to generation of any income chargeable to tax under the Act in their hands.

12. Section 40 of the Act begins with a non-obstante clause *qua* sections 30 to 38 of the Act and provides that no deduction shall be allowed in computing the income chargeable under the head 'Profits and gains of business or profession' in respect of the items set out in the provision. Clause (a)(i) of section 40 provides that no deduction shall be allowed in case of any assessee, *inter alia,* on '*other sum chargeable under this Act*' which is payable outside India or in India to a non-resident, not being a company or to a foreign company on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or after deduction, has not been paid during the previous year, or in the subsequent year before the expiry of the

time prescribed under sub-section (1) of section 200. Thus, in order to invoke the provisions of section 40(a)(i), it is essential that the amount payable by the assessee to a foreign company etc. should be chargeable to tax under this Act in the hands of such foreign company etc. The AO has pressed into service the provisions of section 195 of the Act for treating the failure of the assessee in making deduction of tax at source from the payments made to the non-residents AEs. Sub-section (1) of section 195 states that any person responsible for paying to a non-resident, not being a company, or to a foreign company, any payments specified in the provision `*or any other sum chargeable under the provisions of this Act*' shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rates in force. Thus deductibility of tax at source pre-supposes the chargeability of income under the Act and disallowance u/s 40(a)(i) follows from non-deduction/payment of tax at source by the person responsible on such payments. In other words, unless income from the transaction is chargeable to tax under the Act in the hands of non-resident etc., there can be no question of deduction of tax at source and the consequential disallowance u/s 40(a)(i) of the Act cannot follow.

13. It, therefore, becomes essential to first determine if the non-resident AE sellers were liable to tax in India for the goods sold by them to the assessee in India. As against a resident chargeable under the Act in respect of his world income, a non-resident as per section 5(2) of the Act is chargeable only in respect of income from whatever source derived, which is received or is deemed to be received in India or accrues or arises or is deemed to accrue or arise to him in India. Section 9(1) of the Act provides that all income accruing or arising, whether directly or indirectly, through or from any business connection in India, etc., shall be deemed to accrue or arise in India. Explanation 1(a) to this provision states that in the case of a business of which all the operations are not carried out in India, the income of the business deemed under clause (i) to accrue or arise in India shall be only such part of the income as is reasonably attributable to the

operations carried out in India. The effect of this provision is that all income accruing or arising to a non-resident from any business connection etc. in India, to the extent of the operations of such business carried out in India, shall be deemed to accrue or arise in India and the provisions of section 5(2) shall be magnetized. Per contra, if the business operations are not carried out in India, but, still a non-resident earns income from any business connection in India, that income shall not be deemed to accrue or arise to him in India in terms of section 9(1)(i) of the Act and will get immunity from Indian taxation. The Hon'ble Supreme Court in *CIT vs. R.D. Aggarwal & Co. and Another (1965) 56 ITR 20 (SC)* considered a case in which the assessee obtained orders from dealers in Amritsar. Such orders were accepted by non-resident. Price was received and delivery was given outside India. No operations, such as, procuring of material or manufacture of finished goods, took place within India. It was held that no business connection was there and, in the absence of the non-resident having any place of business in India, the case was not covered within the provision analogous to section 9(1)(i) of the Act. Similar view has been reiterated by the Hon'ble Supreme Court in *CIT vs. T.I & M Sales Ltd. (1987) 166 ITR 93 (SC)* and more recently in *GVK Industries Ltd. And Another vs. ITO and Another (2015) 371 ITR 453 (SC).* It, therefore, follows that when a non-resident makes offshore supply of goods to an Indian enterprise, without performing any activity in India, no income accrues or arises to him in India. If, however, some activity is done in India or some operations are performed in India, then, the income attributable to such operations is chargeable to tax under the Act. The absence of a Permanent Establishment of a non-resident in India ordinarily implies that no business operations were carried out by him in India. The existence of a PE in India may require examination as to whether such PE was involved in specific transactions between non-resident and an unrelated Indian enterprise. In case there is no PE of the foreign enterprise in India and the goods are directly sold offshore by such non-resident enterprise without performing any operations in India, then, no income can accrue or arise or deemed to accrue or arise to him in terms of section 9(1)(i) of the Act.

14. Reverting to the facts of the instant case, we find that out of the assessee's import transactions with six AEs, three are with Mitsubishi Shoji Light Metal, Japan, Thai MC Company Ltd., Thailand and Petro Diamond Corporation, Japan. The assessee made purchases from these three AEs in the immediately preceding assessment year and the Tribunal was pleased to hold that in the absence of any PE of these three enterprises in India, the provisions of section 40(a)(i) were not attracted. The AO, while finalising the assessment for the current year, has noticed on pages 52 and 54 of his order that the assessee made identical reply which was made during the course of assessment proceedings for the assessment year 2009-10. In rejecting the assessee's contention put forth for the instant year and making disallowance u/s 40(a)(i) of the Act, he relied on the view taken by him for the said assessment year 2009-10. Since the assessment order for the assessment year 2009-10 has been overturned by the Tribunal on this issue by holding that there was

no evidence of such enterprises having any PE in India and as such no disallowance was called for, we are unable to countenance the contrary view canvassed by the ld. DR on this count. In so far as the purchase transactions with the other three AEs are concerned, namely, Mitsubishi Corporation, Unimetals, Japan, Asia Modified Strach, Thailand and Mitsubishi International, GmbH, Germany, we find that the AO has dealt with the purchase transactions with all the six AEs in a common manner without separately adjudicating upon these three parties which were not involved in the preceding year. This shows that the facts and circumstances in respect of these AEs are similar to those of the three AEs from whom the assessee purchased goods in the preceding year as well. Apart from relying on his order for the AY 2009-10, the AO also noticed that the Tribunal order in the case of Metalone Corporation, in favour of the assessee, has not been accepted by the Department and appeal is pending against it before the High Court. The case of Metalone Corporation was originally taken cognizance of by him in an earlier year for holding that all the foreign AEs would be deemed to have PE in India because of some common activity carried out in India on behalf of all of them. This contention of the Revenue came to be turned down by the Tribunal in its order of Metalone Corporation by holding that the existence of PE cannot be inferred in such circumstances. In view of the fact that the AO has not drawn any line of distinction between the three new AEs from which the assessee made purchases in the current year alone *vis-a-vis* the remaining three from which imports were made in earlier years as well, and, further, on the failure of the ld. DR to point out any difference in the factual or legal position existing in respect of these three new entities, we are inclined to follow the same conclusion as given for the three parties coming from the earlier year for which the Tribunal has held that they did not have any PE in India. The crux of the matter is that since these six AEs did not have any PE in India, the off-shore sales made by them to the assessee in India would not generate any income chargeable under the Act to the AEs from such sale transactions.

15. Now we take up the second category of purchases made from MCJ, for which the ld. AR claimed the benefit of non-discrimination clause of the DTAA to bolster his submission of non-applicability of the provisions of section 40(a)(i) of the Act. The sum and substance of his arguments is that total purchases amounting to Rs.2141.78 crore were made by the assessee from MCJ including its overseas branch office and non-discrimination clause under Article 24 of the DTAA applies warranting non-deduction of tax at source. *Au contraire*, the ld. DR put forth that the case of the assessee is covered under Article 9 of the DTAA and for that reason, the application of Article 24 is ousted.

16. In order to appreciate the above rival contentions, it would be apposite to consider the mandate of Article 24, the relevant part of which, is as under:-

> `ARTICLE 24 - 1. Nationals of a Contracting State shall be subjected in the other Contracting State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which nationals of that other Contracting State in the same circumstances are or may be subjected. This provision shall, notwithstanding the provisions of article 1, also apply to persons who are not residents of one or both of the Contracting States.

2. The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favourably levied in that other Contracting State than the taxation levied on enterprises of that other Contracting State carrying on the same activities.

This provision shall not be construed as obliging a Contracting State to grant to residents of the other Contracting State any personal allowances, reliefs and reductions for taxation purposes on account of civil status or family responsibilities which it grants to its own residents.

3. *Except where the provisions of article 9,* paragraph 8 of article 11, or paragraph 7 of article 12 *apply*, interest, royalties and other disbursements paid by an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable profits of such enterprise, be deductible under the same conditions as if they had been paid to a resident of the first mentioned Contracting State.........'.

17 It is equally important to consider the prescription of Article 9, the relevant part of which runs as under :-

`ARTICLE 9 - 1. Where :

(a) an enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State, or

(b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State,

and in either case conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be

> included in the profits of that enterprise and taxed accordingly.....'.

18. The case of the ld. AR is that the assessee is entitled to the benefit of Article 24 in terms of para 3. A perusal of this para transpires that except where the provisions of Article 9 etc. apply, interest, royalties and other disbursements paid by an Indian enterprise to a Japanese enterprise, shall, be deductible in determining the taxable profits of the Indian enterprise under the same conditions as if they had been paid to an Indian resident. Simply stated, para 3 of Article 24 provides that any payment made by an Indian enterprise to a Japanese enterprise shall, for the purposes of determining the taxable profit of an Indian enterprise, be taken up under the same conditions as if the payment had been made to an Indian resident and not to a non-resident. In simple words, for the purpose of computing the taxable profit of an Indian enterprise, the provisions of the Act shall apply on a transaction with a Japanese enterprise as if it is a transaction with an Indian enterprise. If the transaction with a

Japanese enterprise entails some adverse consequences in comparison with if such transaction had been made with an Indian enterprise, then such adverse consequences will be remedied under this clause by presuming, for computing the total income of an Indian enterprise, as if it was a transaction with an Indian enterprise and not a Japanese enterprise. Thus, Article 24 provides in unequivocal terms that for the purposes of determining the taxable profits of an Indian enterprise, any disbursements made to a Japanese enterprise shall be deductible in the same manner as if it had been made to an Indian resident. When we examine the TDS provisions, it is noticed that no provision under the Chapter XVII of the Act stipulates for deduction of tax at source from payment made for the purchases made from an Indian resident. This position when contrasted with purchases made from a non-resident, imposes liability on the purchaser for deducting tax at source under section 195, subject to the fulfilment of other conditions. When we compare an Indian enterprise purchasing goods from an Indian party *vis-a-vis* from a Japanese party, there is possibility of an obvious discrimination in terms of disallowance of purchase consideration under section 40(a)(i) in so far as the purchases from a Japanese enterprise are concerned. It is this discrimination which is sought to be remedied by para 3 of Article 24. The effect of this Article is that in determining the taxable profits of an Indian enterprise, the provisions of the Act, including disallowance u/s 40(a)(i), shall apply as if the purchases made from a Japanese enterprise are made from an Indian enterprise. Once purchases are construed to have been made by an Indian enterprise from another Indian enterprise, not requiring any deduction of tax at source from the purchase consideration and consequently ousting the application of section 40(a)(i), the non-discrimination clause shall operate to stop the making of disallowance in case of purchases actually made from a Japanese enterprise, which would have otherwise attracted the disallowance. Thus, it is evident that para 3 of Article 24, without considering the effect of Article 9 and other Articles referred to in the beginning of this para, rules out the making of disallowance u/s 40(a)(i) of the Act.

19. Now let us examine Article 9 of the DTAA and its setting in Article 24(3), which in the opinion of the ld. DR, comes to the rescue of the Revenue in making inoperative the otherwise applicability of para 3 of Article 24. The opening part of para 3 provides that `*Except where the provisions of article 9 .... apply*'. Then it talks about the application of non-discrimination as discussed above. This shows that the provisions of Article 24(3) shall be restricted to the extent of applicability of Article 9. In other words, whatever has been provided in Article 9 shall remain intact and will have superseding effect over the mandate of Article 24(3). The contention of the ld. DR that once Article 9 applies, then the application of Article 24(3) is thrown out, is not wholly correct. The writ of Article 9 does not stop the application of Article 24(3) in entirety. The overriding effect of Article 9 over para 3 of Article 24 is limited to its content alone. In other words, the mandate of Article 24 applies save and except as provided in Article 9 etc. It does not render Article 24(3) redundant in totality. A conjoint reading of these two Articles brings out that if there is some discrimination in computing the

taxable income as regards the substance of Article 9, then such discrimination will continue as such. But, in so far as rest of the discriminations covered under para 3 of Article 24 are concerned, those will be removed to the extent as provided.

20. Now let us decipher the instruction of the relevant part of Article 9 of the DTAA as extracted above. Para 1 of this Article can be viewed in two parts, viz., clause (a) or clause (b) as one part and the portion starting with `and' as the second part. Such first part sets out the basic condition for the applicability of the second part. The first part provides for the one enterprise directly or indirectly controlling or contributing to the capital of the other or the existence of common persons managing or contributing to the capital of both the enterprises. The existence of the conditions set out in the first part in the case of the assessee has not been disputed by the ld. AR. The second part of para 1 of Article 9 provides that when the stipulations of the first part of para 1 of Article 9 are satisfied AND the conditions between the two enterprises in their commercial or financial relations differ from those which would have been between two independent

enterprises, then, any profit which has not accrued to one of the enterprises due to such conditions, may be included in the profits of that enterprise and taxed accordingly. The effect of the second part is that the transactions between the two enterprises should be viewed at arm's length notwithstanding their commercial or financial relations. And if the profit accruing to an enterprise has been understated due to such commercial or financial relations, then, such understated profits should also be taxed. On circumspection of Article 9 read with Article 24, the position which emerges is that the enhancement of income made by virtue of Article 9 in treating the inhibited transactions between two enterprises as at arm's length price, cannot be neutralised by the application of Article 24. In other words, Article 24 applies on all discriminations as set out in it except those specifically excluded including Article 9. Reverting to the facts of the instant case, we find that the assessee is seeking the benefit of article 24 *qua* the disallowance u/s 40(a)(i) and not in respect of any transfer pricing adjustment made by bringing transactions between two AEs at arm's length price. Disallowance u/s 40(a)(i) is an independent component of the computation of total income which is distinct from any transfer pricing adjustment. Article 24 read with Article 9 albeit prohibits the deletion of enhancement of income due to the making of transactions at ALP, but permits the deletion of enhancement of income due to disallowance u/s 40(a)(i) of the Act. Be that as it may, we find that the TPO has not proposed any transfer pricing adjustment in respect of `Trading segment' of the assessee under which the purchases in question were made. The addition on account of TP adjustment is in respect of `Service fee received', which was earned by the assessee without making purchases of the goods from its AEs. As disallowance u/s 40(a)(i) is in respect of purchases made from the AEs, which is in no manner connected with the Commission segment, we hold that the assessee is entitled to the benefit provided by article 24 of the DTAA and cannot be visited with the disallowance u/s 40(a)(i) of the Act.

21. The foregoing discussion divulges that there existed no liability on the assessee to deduct tax at source from the

payments made by it to the above listed seven foreign AEs, either because of non-chargeability of income under the Act from sale of such goods to the assessee or because of the application of non-discrimination clause. The natural corollary which follows is that the provision of section 195 cannot apply and, resultantly, there can be no disallowance u/s 40(a)(i) of the Act. We, therefore, order for the deletion of this disallowance. This ground is allowed.

22. The only other ground is against the disallowance of Rs.1,38,410/- made by the AO u/s 14A of the Act. The AO has recorded in para 4 of his order that even if no exempt income was earned by the assessee in the year in question, still it was liable to offer disallowance u/s 14A of the Act. He, therefore, computed disallowance under this provision at Rs.1,38,410/-.

23. After considering the rival submissions and perusing the relevant material on record, we find it as an admitted position that the assessee did not earn any exempt income during the year. The Hon'ble jurisdictional High Court in *CIT vs. Holcim India*

Pvt. Ltd. (2014) 90 CCH 081 Del-HC, has held that no disallowance u/s 14A can be made in the absence of any exempt income. In *Joint Investments Pvt. Ltd. Vs. CIT (2015) 372 ITR 694 (Del),* it has been held that disallowance u/s 14A cannot exceed the exempt income. Since the assessee admittedly did not earn any exempt income during the relevant year, respectfully following the precedents, we hold that no disallowance u/s 14A can be made. This ground is allowed.

24. In the result, the appeal is partly allowed.

Order pronounced in open court on this 26th day of May, 2015.

Sd/-	**Sd/-**
(C.M. GARG)	**(R.S. SYAL)**
JUDICIAL MEMBER	**ACCOUTNANT MEMBER**

Dated the 26th May, 2015

dk

Copy forwarded to:

1.Appellant
2.Respondent
3.CIT
4.CIT(A)-III, New Delhi.
5.CIT(ITAT), New Delhi.

AR, ITAT, NEW DELHI.