

**IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH '1-1' NEW DELHI**

**BEFORE SHRI R.K. PANDA, ACCOUNTANT MEMBER
AND
SHRI K. NARASIMHA CHARY, JUDICIAL MEMBER**

**ITA No. 2745/Del/2015
Assessment Year: 2009-10**

M/s. Corbus (India) Pvt. Ltd., (Now Corbus (India) LLP), 164, Kailash Hills, East of Kailash, New Delhi. PAN : AAACM2026B (Appellant)	vs.	DCIT, Circle 3(1), New Delhi. (Respondent)
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Appellant by : Sh. Ashutosh Mohan Rastogi, Adv.
Sh. M.K. Juneja, AR
Ms. Anchal Kesari, Advocate
Respondent by: Sh. Kumar Pranav, Sr. DR

Date of hearing: 27/02/2020
Date of order : 05/03/2020

ORDER

PER K. NARASIMHA CHARY, J.M.

Challenging the order dated 25/02/2015 in appeal No. 86/2014-15/CIT(A)-44, passed by Ld. Commissioner of Income-tax (Appeals)-44, New Delhi ("Ld. CIT(A)"), for assessment year 2009-10, M/s. Corbus (India) Pvt. Ltd. ("the assessee") filed this appeal.

2. Brief facts of the case are that the assessee company was incorporated in 1994 as a subsidiary of Global Technologies International Corporation Ltd. (GTICL), which in turn was the subsidiary of Soim

International LLC. For assessment year 2009-10, the assessee filed return of income declaring total income of Rs.10,04,84,944/- and since the assessee had entered into an international transaction with its Associated Enterprises(AE) in respect of provision of Information Technology Services and related services (e-sourcing services), Ld. Assessing Officer referred the determination of Arm's Length Prices (ALP) of international transaction to the Id. TPO u/s. 92CA(1) of the Income-tax Act ("the Act"). Learned TPO did not draw any adverse inference in respect of the pricing of the international transactions but proposed to make an upward adjustment of income of the assessee on account of outstanding receivables. Ld. TPO re-characterized the debit balances, i.e., outstanding receivables in excess of 45 days as loans advanced to AE and applying an adhoc interest rate of 17.77%, proposed an addition of Rs.69,73,350/-.

3. Ld. Assessing Officer further found that the assessee had claimed dividend income of Rs.2,44,356/- and while invoking the provisions of section 14A read with Rules 8D of the Rules, disallowed a sum of Rs.26,223/-. Ld. Assessing Officer, therefore, made an addition of Rs.69,73,350/- on account of Arm's Length adjustment in respect of outstanding receivables and a sum of Rs.26,223/- by invoking section 14A read with Rule 8D of the Rules.

4. Challenging the same, the assessee preferred appeal before the CIT(A). Ld. CIT(A), after considering the submissions made on behalf of the assessee, observed that ITES segment relates to E-sourcing for procurement of goods and there was delay varying from 271 to 55 days for 10 invoices and in software development segment, the delay varied from 237 to 50 days for 27 invoices and therefore, held that such a transaction was liable for Arm's Length adjustment. Ld. CIT(A), however, directed the Assessing Officer to

charge interest @ LIBOR + 1.5% instead of interest @ 17.77% on the delayed payment from AE in both ITES and Software Development segments.

5. Ld. CIT(A) further observed that the assessee had failed to explain why the provisions of section 14A read with Rule 8D should not be applicable to the case and held that Ld. Assessing Officer correctly determined the disallowance u/s. 14A read with Rule 8D.

6. Aggrieved by both the findings of Id. CIT(A), assessee preferred this appeal before us challenging the Arm's Length adjustment in respect of outstanding receivables and also the disallowance u/s. 14A read with Rule 8D of the Rules.

7. It is the argument of the Id. AR that the receivables are not independent transactions separate from the transaction of sale; that receivables are merely an offshoot of commercial transactions and cannot be viewed on standalone basis; that the receivables is an integral part of the return on the underlying commercial transactions; and that therefore, there is no concrete reason as to why and how the outstanding receivables should be treated as loans. He further submitted that the receivables are not sham transactions, but genuinely sourced from the business operations as the amounts overdue from the customers and should be construed as such and therefore, the interest charged on such transactions is not defined and contrary to the legislative intent and judicial view expressed in a number of decisions like, the decision of Hon'ble Delhi High Court in the case of Pr. CIT vs. BC Management Services Pvt. Ltd. (ITA No. 1064/2017), decision of ITAT Delhi Bench in the case of Terradata India Ltd. Vs. ACIT (ITA No. 7885/Del/2017) and Motherson Sumi Infotech & Designs Ltd. Vs. DCIT (ITA No. 6331/Del/2016).

8. Next contention of the assessee is that the operating profit margin from services rendered to AEs is 45.88% which is significantly higher than the working capital adjusted results for comparables, i.e., 22.07% and therefore, the working capital adjustment if appropriately taken into account, the return that was earned by assessee would adequately compensate it for outstanding receivables and since the pricing – profitability of the assessee is more than the working capital adjusted, the arm's length adjustment on the outstanding receivables is not warranted.

9. Ld. AR while drawing our attention to the statement on the company's credit policy submitted that the assessee follows uniform policy of not charging any interest on outstanding receivables both from AEs and non-AEs and therefore, a comparison of the case of AEs and Non-AEs clearly suggests that according to such credit policy, no adjustment is warranted on the outstanding receivables.

10. The next limb of arguments of Id. AR is that the assessee is a debt free company as it has neither received any interest from any creditors nor paid interest to any debtor, as is reflected in the profit and loss account showing a surplus of Rs.9.6 crores with a meagre interest charge of Rs.30,278/- and therefore, in view of the decision of Hon'ble Delhi High Court in the case of PCIT vs. BC Management Services Pvt. Ltd. (supra) and number of decisions of co-ordinate Benches of Delhi Tribunal, the delayed payments made by AE cannot be treated as part of assessee's income.

11. In respect of disallowance u/s. 14A, the case of the assessee has been that the investment in mutual funds was made in earlier years and by way of the policy of automatic reinvestment of dividend without any efforts of the assessee, such investments accrue further dividends and therefore, there is

neither any direct expenses nor interest expense nor any administrative expense involved in earning of dividend. He further submitted that a similar question had arisen in immediately preceding year 2008-09 under identical circumstances and the CIT(A), considering the submissions of the assessee, deleted the addition.

12. Per contra, Ld. DR places heavy reliance on the orders of the authorities below and drew our attention to the relevant observations of the authorities in such orders.

13. We have gone through the records in the light of submissions made on either side. There is no denial of the fact that operating profit margin earned by the assessee from the services rendered to AEs is 45.88% and the same is significantly higher than the working capital adjusted results for comparables at 22.07%. Working capital adjustment is an adjustment for the opportunity cost of capital for investments made in working capital, which require capital and operating assets and an uncontrolled entity is expected to earn a market rate of return on that required capital independent of the services that it provides. The amount of capital required to support the services is dependent upon the level of inventory, debtors and creditors measured at a particular percentage of the total cost and had impact on the profits from investing at different levels of working capital due to the differences in the cash collection cycle which imply differences in credits granted to the customers which activity is similar to an additional service for which the markets would pay.

14. In Kusum Healthcare Private Ltd. Vs. ACIT (2015)170 TJJ-411, the coordinate Bench of Tribunal held -

“7 . We have heard rival submissions and perused the material on record. An uncontrolled entity will expect to earn a market rate of return on its working capital investment independent of the functions it performs or products it provides. However, the amount of capital required to support these functions varies greatly, because the level of inventories, debtors and creditors varies. High levels of working capital create costs either in the form of incurred interest or in the form of opportunity costs. Working capital yields a return resulting from a) higher sales price or b) lower cost of goods sold which would have a positive impact on the operational result. Higher sales prices acts as a return for the longer credit period granted to customers. Similarly in return for longer credit period granted, a firm should be willing to pay higher purchase price which adds to the cost of goods sold. Therefore, high levels accounts receivable and inventory tend to overstate the operating results while high levels of accounts payable tend to understate them thereby necessitating appropriate adjustment. The appropriate adjustments need to be considered to bring parity in the working capital investment of the assessee and the comparables rather than looking at the receivable independently. Such working capital adjustment takes into account the impact of outstanding receivables on the profitability.”

15. This order of Tribunal was affirmed by Hon’ble jurisdictional High Court in ITA No. 765/2016 (Revenue’s appeal) vide order dated 25.04.2017 and the Hon’ble High Court unequivocally held that working capital adjustment takes into account the impact of outstanding receivables on the profitability.

16. It is also not in dispute that the assessee is a debt free company as is reflected in the profit and loss account wherein the interest charges are only Rs.30,278/-. It is, therefore, clear that the assessee does not have any interest where borrowed funds were utilized for extending any kind of loan to its AEs, so that transfer pricing adjustment could be made. In the case of

BC Management Services Pvt. Ltd. (supra), Hon'ble jurisdictional High Court held that notional income on account of delayed payment cannot be treated as part of income and be made subject matter of adjustment.

17. In Indo American Jewellery Limited (ITA No. 5872/Mum/2009), the Mumbai Tribunal held –

“A close reading of section 92B transpires that the transactions of ‘sale’ and lending...money’ have been distinctly set out. Transaction of ‘sale’ results into profit and that of ‘lending money’ gives interest income. Thus it is evident that interest income is associated only with the lending or borrowing of money and not with sale. So if the international transaction is that of ‘sale’, the arm’s length price is determined qua the ‘sale price’. Of course, while determining the ALP in a sale transaction, all the relevant aspects including the credit period allowed are taken into view. On the other hand, if the international transaction is that of ‘lending or borrowing money’, the arm’s length price is gauged qua the ‘interest’. When the international transaction is that of ‘sale’, the interest aspect is embedded in it. There can be no separate international transaction of ‘interest’ in the international transaction of ‘sale’. Early or late realization of sale proceeds is only incidental to the transaction of sale, but not a separate transaction in itself. If the ALP in respect of an international transaction of ‘sale’ is determined, then there can be no question of treating the non-receipt of interest in such sale transaction as a separate international transaction warranting any further adjustment. One may also contend that the expression ‘any other transaction having a bearing on the profits, income, losses’ as employed in sec. 92B defining international transaction would encompass such interest from sale as the non-receipt of due interest would have the effect on profits or income. This contention also does not merit acceptance because when ‘sale’ and ‘lending money’ have been specifically included in definition of ‘international transaction’ u/s 92B, then the expression ‘any other transaction’ used in the later part of this

provision will exclude all the items separately covered. In this view of the matter, it becomes manifest that there can be no separate international transaction of interest income which is part of the transaction of sale. Once ALP is determined in respect of the sale transaction, it would be deemed to be covering all the elements and consequences of the transaction of sale. Having determined ALP in a sale transaction, it cannot be accepted that separate adjustment de hors such determination is required in respect of interest.”

18. Similar view is taken in Nimbus Communication in ITA No. 6597/Mum/2009 and Bharti Airtel Limited vs. ACIT (ITA No. 5816/Del/2012. It is, therefore, clear that re-characterisation of the outstanding receivables as loan is impermissible unless the transactions are found to be substantially at variance with the stated form.

19. Lastly, there is no denial of the fact that in the assessment year 2012-13, this question of adjustment on account of receivables was dealt by the CIT(A) and by referring to the decision of Hon'ble jurisdictional High Court in the case of Kusum Healthcare Private Ltd.(supra), deleted the entire adjustment suggested by Id. TPO on account of interest on outstanding receivables. We, agree with the submission of the Id. AR that because the Id. CIT(A) did not have the benefit of decision of Hon'ble jurisdictional High Court in the case of Kusum Healthcare Pvt. Ltd. (supra), the issue was held otherwise for the assessment year 2009-10.

20. Viewing from any angle, we are of the considered opinion that the addition made on account of arm's length price adjustment in respect of outstanding receivables cannot be sustained and we, therefore, while allowing grounds Nos. 1 to 3, direct the Id. Assessing Officer to delete the addition.

21. Grounds Nos. 1, 4 & 5 are academic in nature in view of our findings in ground Nos. 1 to 3.

22. Now, turning to ground No. 6 in respect of disallowance of expenditure u/s. 14A. On a reading of the order dated 17.07.2019 in ITA No. 5723/Del/2016 for assessment year 2011-12 in assessee's own case, we find that this issue stands covered and in the absence of any reason to show why the view taken by the Tribunal in assessee's own case on identical facts and circumstances should not be followed, we find that mechanical application of Rule 8D is not tenable and the addition made on this account has to be deleted. We order so.

23. In the result, appeal of the assessee is allowed.

Order pronounced in the open court on 5th March, 2020

Sd/-

(R.K. PANDA)
ACCOUNTANT MEMBER

Sd/-

(K. NARASIMHA CHARY)
JUDICIAL MEMBER

Dated: 05/03/2020

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