// Tax Review/Taxation
Daily Alert Services

Huzaima & Ikram
November 28, 2013

This special email service from Monday to Friday, part of subscription package, is aimed at keeping you informed about tax and fiscal matters. It contains news, legislative changes, case-law, in-depth articles and analyses covering all areas of taxes at domestic and international level. On every Saturday evening, we email weekly compilation of the entire material. Every month, ***Taxation*** in printed form, is sent through post and digital version of ***Tax Review International*** is made available for download at www.huzaimaikram.com.

For subscription, please visit our website or contact offices mentioned below.

This service is available *only* for paid subscribers. If you are a subscriber of *Law and Practice of Income Tax* (LPIT), *Law and Practice of Sales Tax* (LPST), *Taxation* or *Tax Review International* but not receiving this service, please send your email address at sales@huzaimaikram.com quoting subscription number.

Disclaimer:
The material contained in this publication is not intended to be advice on any particular matter. No subscriber or other reader should act on the basis of any matter contained in this publication without seeking appropriate professional advice. The publisher, the authors and editors, expressly disclaim all and any liability to any person, whether a purchaser of this publication or not, in respect of anything and of the consequences of anything done or omitted to be done by any such person in reliance upon the contents of this publication.

This issue contains:

- **ARTICLE**

  Challenges before new CJP

- **TAX NEWS**

  CII Calls on India to Stabilize Tax Regime

  Britain May Tax Foreign Property Investors

  Court asks FBR to act against smuggling

  Members given powers under various fiscal statutes: FBR

  PSEs not deducting WHT from fees paid to directors: TI Pakistan

  Salaried class tax rates:
  FBR plea accepted; SHC order suspended by SC

- **STATUTES**

  Income Tax Circular No. 13 of 2013,
  dated November 27, 2013

- **CASE LAW**

  FOREIGN

  ITA No. 7408/Mum/2010
  (Assessment year: 2002-2003) &
  ITA No.: 7641/Mum/2010
  (Assessment year: 2002-2003).

Kind regards

Mrs. Huzaima Bukhari
Editor

Lahore
Suite No. 14, Second Floor,
Sadiq Plaza, Regal Chowk, Mall Road,
Lahore 54000 Pakistan
Ph. (+9242) 36280015 & 36365582

Karachi
Ms. Sadaf Bukhari
Cell: 0301-8458701

Challenges before new CJP

by
Huzaima Bukhari & Dr. Ikramul Haq

With the appointment of Justice Tassaduq Hussain Jillani as the next Chief Justice of Pakistan from December 12, 2013, on the retirement of Chief Justice, Iftikhar Muhammad Chaudhry, there is enthusiasm in official circles that the "era of undue intervention in civil-military administrative affairs and political arena" will come to an end. It is hoped that Justice Jillani, known as "the gentleman judge" for his mild manner, would maintain focus on rights but "steer clear of intervening in government policy". It is mentioned in various reports that "Justice Tassaduq Hussain Jillani "avoided the high-profile political cases that Chief Justice Iftikhar Chaudhry revelled in". Analysts say Justice Tassaduq Hussain Jillani as Chief Justice of Pakistan would prefer "judicial vigilance" over "judicial populism". "If the courts fail to maintain this delicate balance, none else but people's confidence in the judiciary would be the worst victim", Justice Tassaduq Hussain Jillani observed in a recent ruling.

While the controversies and debates over the role and legacy of out-going Chief Justice, Iftikhar Muhammad Chaudhry, would continue, it is the time that new Chief Justice starts some fundamental reforms in the existing judicial system—'**Pride and Justice'**, *The News,* October 27, 2013. Our judicial structure, dating back to the British colonial era, has not changed except patchwork of so-called Islamic laws and establishment of Federal Shariat Court by General Ziaul Haq. Two conflicting legal systems have given undue advantage to the police alone for self-aggrandizement rather than serving any useful purpose for dispensation of justice in the real sense of the word. The maxim 'justice delayed is justice denied' most aptly describes the essence of our judicial system which desperately needs reforms at all levels.

On August 14, 1947, we inherited a strong and independent judiciary having unquestionable reputation of competence and integrity. Mian Abdul Rashid, the first Chief Justice of Pakistan, was a man of unimpeachable character, who restrained from attending government gatherings and public functions. His successor, Justice Muhammad Munir, for his judgements in Maulvi Tamizuddin case [PLD 1955 Federal Court 240] and few others did become controversial, though his critics seldom realise that it was actually the failure of the political elite that paved the way for recurrent unconstitutional rules for which judiciary could not alone be blamed. One cannot, however, forget some of his great successors like Justice Shahabuddin and Justice A.R. Cornelius, who demonstrated high standards of judicial conduct even in the earlier tumultuous years of our political history.

In post-independence years, the dilemma of our judiciary remained perpetual failure of political leadership as it was approached many a

times to determine the validity or otherwise of capturing State power by men in uniform. In *The State v Dosso* [PLD 1958 SC 533], Chief Justice Munir called it a "successful revolution", but Justice Hamoodur Rehman in *Asma Jillani v Government of Punjab* [PLD 1972 Sc 139] called it "usurpation" of people's rights. In *Begum Nusrat Bhutto v Chief of Army Staff* [PLD 1977 SC 657] came yet another endorsement of the doctrine of necessity wherein "intervention" was declared lawful "in the best and larger interest of the nation. General Musharraf not only got three years but also the right to amend the Constitution! However, defiance and an emphatic 'NO' by Iftikhar Muhammad Chaudhry to same Musharraf, many allege it was a personal affair, changed the entire judicial landscape.

For judiciary, November 3, 2007 was the beginning of a new era. A dictator imposed judiciary-specific martial law—this time the victims were not politicians but the judges. For the first time, it was issue of survival for those who always sided with men in uniform against politicians. The effectiveness of people's street power that reigned from March 9, 2007 to July 20, 2007, from November 3, 2007 to March 16, 2009—culminated in the second restitution of Iftikhar Muhammad Chaudhry as the Chief Justice of Pakistan on March 22, 2009. As March 16, 2009 brought "justice" for Iftikhar Muhammad Chaudhry, the Supreme Court as an institution conveyed a change of mind in its decision of July 31, 2009 as under:

> *"Before parting with the judgment, we would like to reiterate that to defend, protect and uphold the Constitution is the sacred function of the Supreme Court. The Constitution in its preamble, inter alia, mandates that there shall be democratic governance in the country, wherein the principles of democracy, freedom, equality, tolerance and social justice as enunciated by Islam shall be fully observed; wherein the independence of judiciary shall be fully secured. While rendering this judgment, these abiding values have weighed with us. We are sanguine that the current democratic dispensation comprising of the President, Prime Minister and the Parliament shall equally uphold these values and the mandate of their oaths".*

The above judgement highlighted the real dilemma faced by Pakistan since its existence—a daunting challenge of establishing true democratic polity based on constitutional supremacy, rule of law and equity. The long military rules—backed by foreign masters—and in between experiments of "controlled democracy" denied the people of Pakistan their sovereign right of self-governance, for which a long struggle was waged to secure independence from the British *raj*. The dictatorial rules stifled all the State organs—especially judiciary that became an approving arm for many unconstitutional rules.

Supreme Court, after restitution of Iftikhar Muhammad Chaudhry started taking up many cases, some using *suo muto* powers, causing

panic in many circles. Political polarization diluted valiant common struggle waged by all segments of society, most notably by lawyers, media, social and political activists, for restoration of an independent judiciary. The PPP government alleged that apex court was transgressing its constitutionally-defined limits. Chief Justice, Iftikhar Muhammad Chaudhry, said that if people were not getting their rights, the judiciary was bound to be proactive.

It is undeniable fact that in the post-March 16, 2009 scenario, the Judiciary under Chief Justice Iftikhar Muhammad Chaudhry failed to deliver to the people as no reform agenda was implemented to remove snags in the dispensation of justice. The justice system remained hopelessly redundant, painfully unproductive and marred with inefficiency and inordinate delays. Since March 2009 apex court is in conflict with all other state institutions. There will be a great challenge before Justice Tassaduq Hussain Jillani as the next Chief Justice of Pakistan—his will retire on July 6, 2014—to restore the “balance” he has openly spoken about. The real goal should be to make the judicial system capable of delivering justice without delays and heavy costs to litigants.

No doubt the apex court and higher courts are constitutionally obliged to curtail arbitrary exercise of powers by any organ of the State as their main role is protection of fundamental rights of citizens under all circumstances. It should remain their first and foremost duty. While maintaining the supremacy of Constitution, a sanctimonious document representing and expressing the supreme will of the people, the court should also ensure quick disposal of conflicts pending with them.

Tragically, our courts are still following the outdated procedures and methods whereas many countries have adopted e-system for filing of cases and their quick disposal through fast-track follow up using the offices of magistrates at grass root levels. The main aim of judicial reforms should be elimination of unnecessary litigation and facilitating smooth running of affairs between the State and its citizens. Once both learn to act within the four corners of law, there would be no need for enormous litigation. It is shameful that presently the government is the main litigant. It usurps the rights of people and then drags the poor citizens in courts. First of all, the apex court under new Chief Justice should establish a commission to determine the reasons for this morbid state of affairs. The principles underlying reforms should not mean forcing unnecessary litigation and then its quick disposal but to help reduce its occurrence in the first instance.

India

CII Calls on India to Stabilize Tax Regime

The Confederation of Indian Industry (CII) has called on the Government to offer greater clarity in its taxation of multinational companies, with the aim of addressing concerns and repairing investor confidence.

A new CII white paper, released in conjunction with accountancy firm Ernst & Young, surveys the emerging trends in global taxation and considers how they are impacting on India's tax policy.

CII Director General Chandrajit Banerjee said of the document: "Our country presently needs a tax system which is simple, broad-based, less litigious, and transparent, and ensures international competitiveness. We need to benchmark our systems with international best practices."

The paper focuses to a large extent on the international crackdown on tax avoidance. It notes both the publication in July of the Organization for Economic Cooperation and Development's (OECD) Action Plan on base erosion and profit shifting (BEPS), and the determination of the G20 group of nations to prevent "double non-taxation."

The CII stresses that India is actively working with the OECD on its BEPS project, but warns that tackling the problem "requires a multi-dimensional approach, especially as the apprehension is about whether companies follow the spirit of the law or whether they pay [a] fair share of taxes as per the law of the land."

The Confederation recommends that India's proposed new General Anti-Avoidance Regulations (GAAR) should be applied as an exception, rather than a rule. They should not be used in cases where Specified Anti-Avoidance Rules are already in place.

The white paper also recognizes the growing tension between multinational corporations and revenue authorities over the enforcement of transfer pricing rules. It argues that taxpayers must consider their "options of dispute resolution and determine the comparative benefits of adopting safe harbour rules, continuing with the litigation, or applying for APAs."

Finally, the CII urges the early implementation of the much-delayed goods and services tax (GST) in India. The GST should "simplify and rationalize the current indirect tax regime in the

centre and states, eliminate tax cascading and put the Indian economy on a higher growth trajectory." – *Courtesy tax-news.com*

United Kingdom

Britain May Tax Foreign Property Investors

British Deputy Prime Minister Nick Clegg said on November 18, 2013 that the government is planning to impose a capital gains tax (CGT) on sales of British houses by foreign owners.

The measure is a response to fears of a housing bubble, particularly in London, where prices rose more than 10 percent in a year, largely due to demand from Russian and Middle Eastern investors.

The government is reviewing the proposal ahead of Chancellor George Osborne's Autumn Statement on December 05, but no decision has yet been reached, Clegg told a news conference.

"We certainly need to make sure that people who invest very large amounts of money into property in central London locations...pay their fair share of tax in those transactions. That is why we are looking at options like a differential application of capital gains tax to those kind[s] of transactions," he said.

Currently foreign investors are exempt from the CGT which Britons have to pay (usually at 28 percent) on any profit from the sale of property which is not their primary residence.

Mr Osborne has been hesitant about imposing CGT on foreign property owners, fearing that it might deter investors from coming to the United Kingdom. However, this concern has been somewhat allayed by the way in which London's property market has continued to grow despite the imposition of a new 7 percent top rate of stamp duty on homes worth over GBP2m. – *Courtesy tax-news.com*

Court asks FBR to act against smuggling

The Supreme Court directed the federal authorities on Wednesday to devise a mechanism to beat the menace of duty evasion on imported goods and smuggling of arms and drugs “with zero tolerance” for sustainable peace in Karachi.

The court rejected a report submitted by the Customs authorities on duty collection and directed the chairman of the Federal Board of Revenue to appear in court to explain the measures taken in this regard.

The bench, headed by Chief Justice Iftikhar Muhammad Chaudhry and comprising Justices Jawwad S. Khawaja, Mian Saqib Nisar, Amir Hani Muslim and Ejaz Afzal Khan, was seized with the implementation proceedings of the Karachi suo motu judgment case.

The court was utterly disappointed and dissatisfied with three different reports filed by the customs authorities, one of them on behalf of the FBR chief, and termed them “eyewash”.

Justice Chaudhry observed that the black money generated through duty evasion and smuggling of weapons and drugs was used in criminal activities not only in Karachi but also across the country.

The judges asked the customs officials whether black money generated by evading taxes and levies was being controlled at Karachi Port and Port Qasim.

The court observed that the customs authorities had failed to satisfy it “by making a statement that 100 per cent recovery of taxes is being made and there is no evasion”.

The bench directed the FBR chief to put up a concise statement showing daily clearance of goods separately from ports along with a complete record, manifest correspondence, a clearance of the customs department with a certificate that there was no evasion, particularly of goods which were cleared on Wednesday.

The court ordered the customs authorities to deliver copies of their reports/statements in the offices of Attorney General Munir A. Malik. The attorney general, along with Sindh Advocate General Khalid Javed, would go through them and give their opinion in respect of transparency in making evaluation and recovery of taxes.

The judges also inquired of the customs authorities about the flow of arms and ammunition into the country through vessels or launches. They directed the FBR chief and the director general of the Pakistan Coast Guards to place on record documents to show the process of smuggling.

The customs officials conceded that the department was unable to recover 100pc duty.

They also referred to a customs intelligence report and said that there were dens of smuggled arms and ammunition in the Sohrab Goth area. Smuggled weapons were stored in certain residential projects, including Al Asif Square. However, he said, customs alone was unable to clean the area.

"Tax evasion and illegal weapons and drugs have brought the country to the brink of destruction," the chief justice observed, directing the customs to ensure eradication of smuggling and duty evasion.

The bench issued notices to chairmen of the Pakistan Telecommunication Authority and the Frequency Allocation Board, along with six cellular companies, for issuing unauthorised SIMs and SIMs of other countries, including Afghanistan.

The court observed that illegal arms and SIM cards were key elements in creating a law and order situation.

It was informed that activated SIM cards of Afghan companies were being sold and operated in the country for use in anti-social activities.

The attorney general informed the bench that he had taken up the matter of Afghan SIMs with higher authorities. He said there existed a roaming agreement between two companies, by which a local company provided roaming facility to the company of a foreign country. He said the PTA and any local company could not block the SIM cards of foreign companies, including those of Afghanistan.

The bench issued a notice to Ramzan Bhatti, who was appointed as head of one-man commission to make findings on duty evasion and weapons and drug smuggling, to appear in court to explain why he incorporated into his findings observations which had found mention in a report submitted by the Federal Tax Ombudsman.

Earlier, at the outset the advocate general submitted a performance and progress report regarding targeted operations conducted by police and Rangers.

Expressing satisfaction over the performance of law-enforcement agencies, the court expressed apprehension that achievement made by them might not sustain if those arrested were not put on trial.

The hearing was adjourned to Thursday.

Balochistan missing persons' case

Meanwhile, a three-member bench headed by the chief justice observed that the Frontier Constabulary had to play a role in the missing persons' case, but no remarkable progress had so far been made.

The bench was hearing a petition of the president of Balochistan High Court Bar Association and other human rights cases regarding missing persons.

Advocate Shahid Hamid, appearing on behalf of the Balochistan government, submitted a report about progress in the cases of missing persons.

The bench noted with concern that relatives of missing persons had travelled on foot from Quetta to Karachi, facing harsh winter weather to launch a protest for recovery of their near and dear ones.

The court directed the deputy attorney general to procure the attendance of a responsible person so that, if need be, appropriate directions could be made to ensure the recovery of missing persons in light of the report submitted by the provincial government.

The court will continue the hearing on Thursday. – *Courtesy Dawn*

Members given powers under various fiscal statutes: FBR

The Federal Board of Revenue has delegated powers and functions of the Board under various fiscal statutes administered by the FBR to the Members of the Board for smooth functioning and administration of the tax machinery and effective implementation of income tax, sales tax, federal excise duty and customs duty.

Sources told on Wednesday that the proper delegation of powers and functions from the FBR to its members under various statutes and the FBR Act, 2007 was imperative for smooth functioning of the Board and for effective implementation of fiscal statutes.

Accordingly, in exercise of powers conferred by Section 8 of the Federal Board of Revenue Act, 2007 read with Rule 3(1) of FBR Rules, 2007, the Board-in-Council has delegated the powers and functions of the Board under various fiscal statutes administered by the FBR to the Members of the Board and prescribed their job descriptions.

Under FBR Act 2007, Board has delectated its powers to the Members to give legal backing to certain functions of the existing FBR Members, sources said.

It has also been decided that any power exercised or any job done by a FBR Member mistakenly or inadvertently or in case of exigency, which falls outside the powers delegated or job prescribed, shall not be void due to such mistakes or inadvertence. However, the same shall be subject to ratification by the Board-in-Council. Resultantly, Member (Admn) FBR shall issue a notification of delegation of powers effective from 08-11-2013 in line with minutes of the Board-in-Council.

FBR Chairman Tariq Bajwa highly appreciated the efforts of Chaudhry Safdar Hussain FBR Member (Legal) and Dr Muhammad Iqbal Special Assistant to Chairman for their valuable contribution in chalking out delegations of powers and job descriptions in consultation with other Members of the Board.

According to the FBR's delegation of powers to the Members, the FBR has delegated following powers to its Members under FBR Act, 2007:

The FBR Member (Customs) will exercise powers and perform functions of the Board under the following provisions of Customs Act, 1969: Sections 2 (ai), 4 with approval of Chairman, 5,6,8,9,10,11, 18E, 20, 21, 21A(1), 21A(2), 22A, 25C, 25(12), 26(3), 26A, 27A, 32B, 35(2), 37, 38, 43, 45, 45(2), 50, 53, 54, 65, 67, 68(5), 71, 76(1)(a), 78, 79(I))(a), 79(3), 82 (after approval of FG), 85, 86 (I)(b), 90(2), 90(3), 98(1), 98(2), 99(2), 100(2), 107(1), 110, 121 (2) & (3), 125, 129 (A), 131 (a), 131(2), 131(2) proviso, 147, 155 (G), 174 [2nd Proviso], 177(1), 179(2), 179(4), 181 [1st Proviso], 181 [2nd Proviso], 182, 185(F), 193(2), 194 A, 195, 195 C (2), 195 C (3A), 195C (4), 195C (7), 201(1) (1A), 202 (5), 202B(2) with approval of Chairman, 203 (A), 211 (2), 217, 219 and 224.

He will also exercise powers and perform functions of the Board under the following provisions of Customs Notifications; S.R.O.71(1)/95, S.R.O.554(I)/98 , S.R.O. 678(1)/2004, S.R.O. 575(1)/2006, S. R.O. 41(1)/2009, S.R.O.809(l)/2009, SRO

565(1)/2006, SRO 576(1)/2006, SRO 655(1)/2006, SRO 656(1)/2006, SRO 450(1)/2001, S.R.O.75(l)/2006, S.R.O.327(I)/2008, S.R.O. 559(I)/2008, S.R.O. 492(1)/2009 and S.R.O. 413(1)/2012.

The FBR Member (Inland Revenue-Policy) will exercise powers and perform functions of the Board under the following provisions of Sales Tax Act, 1990: Sections 2(46)(g), 3 (1B), 3(6), 4(d), 8B Proviso, 9, 10(1) Provisos, 14, 22(1)(f), 22(2), 23(1), 23(3), 23(4), 26 (1) 1st & 2nd provisos, 26(5), 50(1), 61, 61A, 63, 72C with approval of Chairman and Clause 48 of 6th Schedule.

He will also exercise powers and perform functions of the Board under the following provisions of Income Tax Ordinance, 2001: Sections 2(29C)(b), 27(c), 28(3) to the extent of formulating criteria of approval of leasing companies etc, 32(3), 46(d), 59AA(6), 61(5), 67(2), 74(2A), 76(11), 77(6), 100B(2)(e), 111(5), 114(2A) in consultation with Member(IT), 148(2), 155(3)(vii), 159(3) to the extent of exempting persons, class of persons. goods or class of goods from withholding tax, 181(3), 181(3) Proviso, 183, 206, 206A, 227A with approval of Chairman, 237(1), Clause 12 of Part l of 2nd Schedule, Clause 1 3(iii) of Part I of 2nd Schedule, Clause 53A of Part I of 2nd Schedule and Clause 57 of Part I of 2nd Schedule. He can also exercise powers and perform functions of the Board under the following provisions of Federal Excise Act, 2005; Sections 3(3), 4(2) proviso, 4(5), 4(8), 5(2), 5(3), 6(3), 7(1), 12(5), 17(1)(g), 18(3), 18(4), 18(5), 40(1) and 42C with approval of Chairman.

He will also exercise powers and perform functions of the Board under following provisions of Income Tax Rules, 2002: Rules 19A, 19B, 19C, 19D, 19E, 19F and 231A. He can also exercise powers and perform functions of the Board under the following provisions of Federal Excise Rules, 2005: Rules 31(2), 32(2), 33(1), 33(2), 33(3), 40(7), 41A (15), 43(6) and 79.

He can also exercise and perform functions of the Board under the following provisions of Sales Tax Rules, 2006: Rules 18 and 150.

FBR Member (Inland Revenue-Operations) will exercise powers and perform functions of the Board under the following provisions of Sales Tax Act, 1990: Sections 2[5AA(f)], 2(9), 6(2), 8A, 10(3), 13(2)(b), 21(1), 21(4), 22(IA), 26(1), 27(a), 31, 32(1)(a) &(b), 37A, 37B(13), 371, 38(1), 38B(3), 40B, 40C, 45A, 47A, 47A(4), 48(IA), 55, 62 and 74.

He can exercise powers and perform functions of the Board under the following provisions of Income Tax Ordinance, 2001: Sections 26(2), 28(3) to the extent of granting approvals in the light of

criteria of leasing companies, etc, 74(11), 80(2)(b)(vi), 134A(2), 134A(4), 165(3), 180, 181A, 202, 209(1) except for CIR (A), 209(2), 212 to the extent of powers conferred on him by this distribution/delegation of powers order, 214A except for appellate body and 217(1) in consultation with Member (IT).

He will exercise powers and perform functions of the Board under the following provisions of Federal Excise Act, 2005: Sections 16(3), 22(1), 23(1), 29(3), 35(1), 38(1) to (4), 43, 45(2), 45(3), 45A and 46(1).

He can exercise powers and perform functions of the Board under the following provisions of Income Tax Rules, 2002: Rules 90, 94, 109, 220B and 231C.

He will exercise powers and perform functions of the Board under the following provisions of Federal Excise Rules, 2005: Rules 2(b), 2(g), 3(5), 5(1), 5(4), 25, 26, 28, 31(1), 33(4) in consultation with Member (IR-Policy), 36(4), 40A(3), 41A(2), 53, 54, 55, 56, 57, 58, 64, 74(3), 76, 77 and 78.

He can exercise powers and perform functions of the Board under the following provisions of Sales Tax Rules, 2006: Rules 5, 6, 10, 12, 27, 28, 30, 41, 44, 52, 62, 64, 65, 66, 67, 68, 69 and 150F.

FBR Member (Legal) can exercise powers and functions under the following provisions of Customs Act, 1969: Sections 185G (2) and 193 A (3) [1st Proviso].

He can exercise powers and perform functions of the Board under the following provisions of Sales Tax Act, 1990: 45A (to the extent of orders by CIR (A) and 74 to the extent of granting condonation to CIR(A) in respect of appellate matters.

He will exercise powers and perform functions of the Board under the following provisions of Income Tax Ordinance, 2001: Sections 209(1) to the extent of CIR (A), 214A in respect of orders by CIR (A) and 223(7).

He can exercise powers and functions under the following provisions of Federal Excise Act, 2005: Sections 35(1) and 43 - to the extent of appellate orders.

The FBR Member (Administration) will exercise powers and perform functions of the Board under the following provisions of Customs Act, 1969: Sections 3, 3A, 3AA, 3B, 3BB, 3C, 3CC, 3D, 3DD and 3DDD (all with the approval of chairman).

He can exercise powers and perform functions of the Board under the following provisions of Sales Tax Act, 1990: Sections 30 with approval of Chairman and 30(1) with approval of Chairman.

He will exercise powers and perform functions of the Board under the following provisions of Income Tax Ordinance, 2001: Section 208(1) with the approval of Chairman. He can exercise powers and perform functions of the Board under the following provisions of Federal Excise Act, 2005: Section 29(1) with approval of Chairman.

The FBR Member (FATE) can exercise powers and perform functions of the Board under the following provisions of Income Tax Ordinance, 2001: 181B and 216(5).

The FBR Member (Taxpayers Audit) can exercise powers and perform functions of the Board under the following provisions of Sales Tax Act, 1990: Sections 32A and 72B to the extent of actual selection on the basis of criteria approved by Board-in-Council.

He can also exercise powers and perform functions of the Board under the following provisions of Income Tax Ordinance, 2001: Sections 177(8) and 214C to the extent of actual selection on the basis of criteria approved by Board-in-Council. He can also exercise powers and perform functions of the Board under the following provisions of Federal Excise Act, 2005: Sections 42B (1) to the extent of actual selection on the basis of criteria approved by Board-in-Council and 45(4).

The FBR Member (Information Technology) can exercise powers and perform functions of the Board under the following provisions of Sales Tax Act, 1990: Sections 2(5AAA) in consultation with Member (IR-Operations), 22(2A) in consultation with Member (IR-Operations), 22(3) in consultation with Member (IR-Operations), 26(1) 3rd Proviso in consultation with Member (IR-Operations), 50A in consultation with Member (IR-Operations) and 52A in consultation with Member (IR-Operations). He can exercise powers and perform functions of the Board under the following provisions of Income Tax Ordinance, 2001: Section 237A in consultation with Member (IR-Operations).

He can exercise powers and perform functions of the Board under the following provisions of Federal Excise Act, 2005: Sections 4(6) in consultation with Member (IR-Operations) and 17(2) (b) in consultation with Member (IR-Operations). He will exercise powers and perform functions of the Board under the following provisions of Income Tax Rules, 2002: Rules 73(2), 73(6) and 229.

He can also exercise powers and perform functions of the Board under the following provisions of Federal Excise Rules, 2005: The electronic Filing of Federal Excise Rules, 2005. He can also exercise powers and perform functions of the Board under the following provisions of Sales Tax Rules, 2006: Rules 150B, 150D, 150G, 150I, 150J, 150K, 150L and 150O. – *Courtesy Business Recorder*

PSEs not deducting WHT from fees paid to directors: TI Pakistan

Public Sector Enterprises (PSEs) are acting illegally by not deducting WHT from the fees paid to directors of the boards as well as attending committee meetings, which is against the IT Ordinance 2001, according to Transparency International Pakistan.

In a letter sent to Federal Board of Revenue Chairman Tariq Bajwa on November 26, Advisor, TI-Pakistan, Syed Adil Gilani, has cited Pak Oman Investment Company, Sui Southern Gas Company Ltd, Sui Northern Gas Pipelines Limited, and several other companies who have reportedly not deducted WHT since last ten years or so, causing loss to the exchequer which may run into billions of rupees.

This act of the Board of Directors of such PSEs is defined as corruption and corrupt practices in the National Accountability Ordinance, 1999, the letter says.

Section 9 (a)(vi) and 10 (a) of the National Accountability Ordinance, 1999 [as amended by National Accountability Bureau (Amendment) Ordinance, 2002] quoted below are punishable for rigorous imprisonment which may extend up to 14 years.

Corruption and corrupt practices: 9 (a) A holder of a public office, or any other person, is said to commit or to have committed the offence of corruption and corrupt practices-(vi) 2[if he misuses his authority so as to gain any benefit or favour for himself or any other person, or 3[renders or attempts to render] 4[or wilfully fails to exercise his authority to prevent the grant, or rendition of any undue benefit or favour which he could have prevented by exercising his authority].

Adil Gilani has requested the FBR Chairman to look into the matter and get the accounts of all PSEs checked for non-deduction of WHT from the fees paid to the respective directors. In case of

violation of law, action may be taken to re-characterise the income, and recover the WHT from all the directors of such companies for the past years, and also penalise PSEs as per provisions of IT Ordinance 2001, he said.

Copies of the letter have been forwarded for the information and action under their mandate to: Secretary to Prime Minister, Islamabad, Senator Ishaq Dar, Minister of Finance, with request to take immediate action, Chairman, NAB, Islamabad, this may be act of undue favour under NAO 1999, Article 9(a) (vi), Federal Tax Ombudsman, Islamabad, and Registrar, Supreme Court of Pakistan, Islamabad. – *Courtesy Business Recorder*

Salaried class tax rates: FBR plea accepted; SHC order suspended by SC

An appeal filed by the FBR has been accepted by the Supreme Court and the order passed by Sindh High Court on tax rates prescribed for salaried individuals through Finance Act, 2012, has been suspended by the apex court. To avoid default surcharge, salaried individuals are required to pay the tax as per Finance Act, 2012. In this regard, the Federal Board of Revenue has made an announcement here on Tuesday.

Sources told that the FBR has filed a CPLA in the Supreme Court against the judgment of Sindh High Court (SHC) and the Supreme Court of Pakistan has suspended the judgment of the SHC that was announced in C.P No D-2342/2013 dated 25.10.2013. Earlier, SHC while deciding a constitutional petition has declared tax rates prescribed for salaried individuals in the First Schedule to the Income Tax Ordinance, 2001 through Finance Act, 2012 illegal, ultra vires of the Constitution and Income Tax Ordinance, 2001.

The SHC had also directed the tax department to issue tax refund to all the salaried individuals whose tax has been withheld and deposited in the treasury pursuant to incorrect amount of tax under Finance Act 2012, within a period of one month from the date of filing such return. Sources said the SHC has declared that the anomaly in the calculation and quantification of tax at S.No 4, 5 and 6 of the Table-B has crept due to incorrect arithmetic calculation as there is no rational basis or reasonableness whatsoever in such determination of the tax liability. The amount of tax as calculated under slabs of taxable income at S.No 4, 5 and 6 of table “B” is without any conscious application of mind. It also lacks certainty of charge and is devoid of any rationale basis and

has resulted in creation of additional burden of tax upon a particular group of salaried individuals without legal sanction.

The FBR has issued a press release on Tuesday which says, "The salaried individuals are informed that on 25.11.2013 the honourable Supreme Court of Pakistan has suspended the judgment of the honourable Sindh High Court that was announced in C.P NO.D-2342/2013 dated 25.10.2013. The FBR has filed a CPLA before the honourable Supreme Court against the judgment of the Sindh High Court.

The effect of the suspension of the Sindh High Court judgment referred above is that now the rates of tax as already provided in clause (1A) of Division I of Part I of the First Schedule to the Income Tax Ordinance 2001 shall apply to all salaried individuals. Those persons who have paid less tax in view of the judgment of the Sindh High Court (above) and have filed the returns, may calculate the short paid tax and deposit the same upto 30.11.2013 to avoid default surcharge, etc," the FBR added. – *Courtesy Business Recorder*

C.No.4(25)ITP/2013(Pt-1)-158795-R

Islamabad, the 27th November, 2013

INCOME TAX CIRCULAR NO. 13/2013

Subject: **Clarification regarding business capital for payment of Income Support Levy.**

Clarification has been sought from the Board as to what would constitute business capital for the purposes of calculating net moveable assets for payment of Income Support Levy. Queries have been raised whether business capital would comprise entire business assets. The matter has been considered and I is clarified that valuation of moveable assets has been explained in Rule (5) of the Income Support Levy Rules, 2013. As per sub rule (2) of rule (5) of the ISL Rules, 2013, the value of any movable asset shall, for the purposes of computing Levy, be the value as declared by the person in the wealth statement.

2. Business capital is distinct and separate from business assets. Business capital is the difference between entire business assets and entire business liabilities. Entire business assets as such, are not subject to Income Support Levy and business capital is calculated by deducting liabilities of business from assets of the business.

2013 TRI 1908 (Trib. Ind.)

INCOME TAX APPELLATE TRIBUNAL
MUMBAI "K" BENCH, MUMBAI

D. Karunakara Rao, Accountant Member and Vivek Varma, Judicial Member

FACTS/HELD

Transfer Pricing: ALP of royalty for trademark usage and technical know-how fee can be determined as per TNMM. Approval of RBI & Govt. means payment is as at arms length

1. The assessee entered into an agreement with its parent company, Cadbury Schweppes, pursuant to which it agreed to pay royalty for the use of trademarks and royalty for the use of technical know-how at 1.25% each of the net sales. This was approved by the RBI and the SIA (Government). The assessee adopted the Transaction Net Margin Method ("TNMM") for computing the ALP of the international transactions by comparing the net margin of the company at entity level with that of companies engaged in food products, beverages and tobacco business. The TPO held that the transactions pertaining to payment of royalty for trademarks and technical know-how fee had to be separately and independently bench-marked using the Comparable Uncontrolled Prices ("CUP") method. He held that the ALP of royalty and technical know-how fee should be computed at 1% of sales the instead of at 1.25% of the sales. This was reversed by the CIT(A) who held that the royalty and technical know-how fee paid by the assessee were at ALP. On appeal by the department to the Tribunal HELD dismissing the appeal:

    The assessee has been paying royalty on technical know-how to its parent AE since 1993. Other group companies across the Globe are also paying the same royalty. Also, the payment is as per the approval given by the RBI and the SIA. Hence there cannot be any scope of doubt that the royalty payment on technical know-how is at arms length. As regards the royalty on trademark usage, the assessee is in fact paying a lesser amount if the payment is

compared with the payment towards trademark usage by other group companies using the brand "Cadbury" in other parts of the world. Accordingly, the royalty payment on trademark usage is also within the arms' length and does not call for any adjustment (Lumax Industries (ITAT Del) (attached) followed). The Department's request for a remand to the TPO to examine the AMP expenses in the light of Maruti Suzuki 328 ITR 210 (Del) (and L. G. Electronics 140 ITD 41 (Del)(SB)) rejected.

Order accordingly.

ITA No.: 7408/Mum/2010 (Assessment year: 2002-2003) & ITA No.: 7641/Mum/2010 (Assessment year: 2002-2003).

Heard on: 22nd October, 2013.

Decided on: 13th November, 2013.

Present at hearing: J.D. Mistry & Nishant Thakkar, for Appellant. Ajeet Kumar Jain & O.P. Singh, for Respondent in ITA No.: 7408/Mum/2010. Ajeet Kumar Jain & O.P. Singh, for Appellant. J.D. Mistry & Nishant Thakkar, for Respondent in ITA No.: 7641/Mum/2010.

JUDGMENT

Per Vivek Varma:– (Judicial Member)

The Cross Appeals have been filed by the department and the assessee against the order of CIT(A) 15, Mumbai, dated 25.08.2010. For the sake of brevity and convenience, we passing a common and consolidated order.

ITA No. 7641/Mum/2010: (Appeal filed by the department):

2. The department has raised the following grounds of appeal:

"1. Whether on the facts and in the circumstances of the case and in Law, was the Ld. CIT(A) justified in concluding that M/s. Cadbury India Limited has received several benefits on account of payment of Technical Knowhow Royalty and whether the Ld. CIT(A) was justified in concluding that Royalty for Trademark at 1% and Technical Knowhow at 1.25% for ht entire FY 2001-02 is at Arm's Length.

2. Whether on the facts and in the circumstances of the case and in Law, was the Ld. CIT(A) justified in treating 50% the expenses incurred on Architect & Interior Design amounting to Rs. 21.94 Lacs and expenses incurred on Supply & Installation of Electrical Items amounting to Rs. 14.44 Lacs as Revenue"?

3. The facts in brief are that the assessee is in the business of manufacture, distribution and marketing of malted food drinks, cocoa powder, chocolates, toffees, drinking chocolates and sugar confectionaries. The assessee, having its head office at Mumbai, is having its factories at Thane, Induri and Malanpur and marketing offices located at Delhi, Chennai, Kolkata and Mumbai.

4. The assessee is a subsidiary of M/s Cadbury Schewepps PLC, U.K. Cadbury group has presence in more then 200 countries and it enjoys the distinction of being world's third largest soft drinks company in sales volume and is among the fourth largest confectionary company in the world.

5. Cadbury India Ltd., the assessee entered into certain international transactions with its Associated Enterprises (AEs), which are as follows:

S No.	Name of the Associated Enterprise (AEs)	Country of tax residence of AEs	Nature of relationship	Description of transaction with AEs	Amount Received/receivable paid/payable as per books of accounts (Rs)
(1)	(2)	(3)	(4)	(5)	(6)
1	M/s Cadbury International Limited	U.K.	92A(2)(b)	(i) Purchase of CDM Flavor oils (ii) Cocoa buying service charges	277,238 3,460,441
2	M/s Cadbury Schweppes Pty Limited, Australia	Australia	92A(2)(b)	Purchase of Cocoa beans	1,243,244
3	M/s Cadbury confectionery, Malaysis Sdn. Bhd, Malaysia	Malaysia	92A(2)(b)	Purchase of chocolates	10,110,412
4	M/s Cadbury (Pty) Limited, South Africa	South Africa	92A(2)(b)	Purchase of Chocolates	1,047,364
5	M/s Cadbury Middle East FZE, Dubai, United Arab Emirates	United Arab Emirates	92A(2)(b)	Sale of Chocolates and malted food drinks	4,343,153
6	M/s Cadbury Schweppes Overseas Limited, UK	U.K.	92A(2)(a)	(i) Royalty for the use of Trade Mark (ii) Royalty for technical know-how	63,668,247 56,624,003

7	M/s Cadbury Schweppes Plc., UK	U.K.	92A(1)(a)	Payment of ERP license and maintenance fees	3,601,240

The issue of ALP was referred to the TPO u/s 92CA with regard to transactions relating to Royalty for the use of trademarks at Rs. 6,36,68,247/- and Royalty for technical knowhow at Rs. 5,66,24,003/-

6. With regard to Royalty on technical knowhow, it was found that the assessee had entered into an agreement with its parent AE on 09.03.1993, with the approval(s) of SIA, Government of India, which were granted at various points of time.

7. According to the agreement, the assessee shall pay Royalty at 1.25% of internal sales and exports (Net sales), against which the parent AE shall supply and disclose and make available to CIL (Indian Co.) all knowhow, advice and assistance at all such time that may be mutually agreed between the parties.

8. The TPO, gathering information from other Cadbury units across the globe required the assessee to submit a reply, as to why 1% of gross sales be not taken to be at arm's length instead of 1.25% taken by the assessee in the case of technical knowhow.

9. Looking into the facts of the case, the TPO found out that the assessee has used TNMM for computing ALP of the International transactions by comparing the net margin of the company at entity level, with that of companies engaged in food products, beverages and tobacco business. According to the TPO transactions pertaining to payment of Royalty is not separately and independently benchmarked. He further noted that companies identified by the assessee company i.e. DFM Foods Ltd., Bakeman Industries Ltd., Modern Food Industries (India) Ltd., Parrys Confectionary Ltd and Ravalgaon Sugar Farm Ltd., did not pay any technical fee/royalty. According to him, these companies could not be used in the analysis for benchmarking the royalty payments. Since the total sales of the company is at Rs. 645 crores and international transactions pertaining to this segment is only 14.50 crores, being only 2.24% would not effect the profitability, if the ALP is to be determined at TNMM at entity level. According to the TPO, the most appropriate method, therefore, would be CUP because all other comparables, as supplied by the assessee, either developed their own technology, or they had acquired the technology long back and are no more paying for the transfer of technology. This, in the case of the assessee is not the case, because, the assessee company, i.e. Cadbury India Ltd., is required to pay royalty to its parent AE, CSDL, for the continuous upgradation of technology.

10. The TPO, therefore, concluded that in the case of royalty on technical knowhow the ALP should be computed at 1% of sales, which

comes to Rs. 4,52,99,207/- against 1.25% taken by the assessee at Rs. 5,66,24,003/-.

11. Similarly, the TPO computed royalty paid on trademarks, at Rs. 5,03,31,678/- in place of Rs. 6,36,68,247/- taken by the assessee.

12. Before the TPO, it was submitted this was the first year for the payment of royalty on trademark use, because, earlier, the payment was banned under FERA Rules.

13. After the prohibition was lifted, the assessee in the Board meeting held on 24.04.2001 authorized the company to pay the royalty on use of trademark at 1% of the net sales value, w.e. from April 2001. After getting the approval from the Reserve Bank of India (RBI) an agreement was entered into between Cadbury Limited, Trebor Bassett Limited, Cadbury Scheweppes Overseas Ltd. and Cadbury India Ltd., on 12.02.2002, according to which Cadbury and Trebor granted Cadbury overseas the exclusive rights to distribute its products and use the trademarks and technical information throughout the territory. The said agreement provided "*that Cadbury Overseas hereby grants to company and the Company hereby accepts the exclusive non transferable licence to manufacture, market and sell the products under the Cadbury Trade Marks and Trebor Trade Marks in the territory in accordance with the technical information and specifications*". Herein territory meant India, Nepal, Bangladesh, Bhutan and Sri Lanka.

14. According to the TPO, the agreements seemed to be overlapping, therefore, he asked the assessee to submit the information regarding payments received by CSOL from all group companies. The company vide its letter dated 04.02.2005 submitted the copy of email sent to it from CSOL, which is as under:

S No.	*Overseas Company*	*Territory*	*Royalty rate/ Fee Net Basis*	*Type of Agreement*
(1)	***(2)***	***(3)***	***(4)***	***(5)***
1	*Cadbury Adams Canada Inc.*	*Canada & Export Territory*	*2.50%*	*Trade mark licence-Exclusive & transferable*
2	*Cadbury Food Co. Ltd., China*	*Not specified but excludes exports*	*3.5%*	*Trademark licence sole non-transferable rights*
3	*Cadbury Egypt S.A.E.*	*Republic of Egypt Export territories listed*	*2%*	*Trade mark licence exclusive*
4	*Cadbury France*	*France and such other territories*	*2.00%*	*Trade mark licence*
5	*Cadbury Ghana Limited*	*Ghana*	*2.00%*	*Combined technical services & trademark user agreement*
6	*PT Cipta Rasa*	*The Republic of*	*2.50%*	*Trade mark licence –*

	Primatama	*Indonesia*		*Exclusive & nontransferable*
7	*Cadbury Kenya Limited*	*Kenya, Uganda and Tanzania and any other territories*	*2.00%*	*Trade mark licence*
8	*Cadbury Confectionery Malaysia SDN BHD*	*East & West Malaysia & Brunei & such other territories*	*2.00%*	*Royalty technical information and trade mark licence agreement – exclusive & nontransferable*
9	*Cadbury Nigeria plc*	*Nigeria*	*2.00%*	*Trade mark licence*
10	*Cadbury Poland Sp zo.o*	*Poland*	*2.5%*	*Trademark licence-exclusive and non-transferable*
11	*Dlrol Cadbury LLC*	*Russia plus named export territories*	*3% for confectionery ***	*Trade mark licence exclusive and non-transferable*
12	*Cadbury Dulciora SA*	*Spain and such other countries*	*3.00%*	*Trademark licence and non-transferable*
13	*Crystal Candy (PVT) Limited*	*Zimbawe and such other territories*	*2.00%*	*Trade mark licence exclusive & nontransferable*
14	*Cadbury Nigeria plc*	*Nigeria*	*2.00%*	*Technical Service Agreement*

15. From the chart, the TPO inferred that royalty on trademarks usage is 2% but the assessee company is paying the royalty between 1 to 2.5% and the average on the above comes to 2.32%. The issue was put to the assessee who replied,

> *"The company contended that, "Technical Assistance and Royalty Agreement was approved by Govt. of India, Ministry of Industry, vide letter dated 14.09.2000. The rate of royalty payable as per approval letter was authorized at 1.25%. The comparability of international transaction of payment towards technical assistance can also be judged with reference to the laws and government orders In force [Rule 10B(2)(d)]. Accordingly, under the facts of the case, the payment towards technical assistance to SQL can be said to comply with the Arm's Length Princiole."*
>
> *The company submitted the copy of application dated 30.04.2001. addressed to the General Manager, Reserve Bank of India, Exchange Control Department, Regional Office, Mumbai, for automatic approval for payment of royalty towards trademarks to Cadbury Schweppes Overseas Limited, U.K. In the application, it is mentioned that "the trademarks belonging to Cadbury Schweppes Overseas Limited, U.K. In the application, it is mentioned that "the trademarks CADBURY*

and several other trademarks belonging to CSOL are used by us on our chocolate, drinking chocolate, malted foods and sugar confectionery products which are being manufactured and sold by our company in India and certain other countries. It requested to issue the automatic approval effective 01.04.2001". The Reserve Bank of India, Exchange Control Department, vide letter dated 25.06.2001, has given the approval to enter into Technical Collaboration for manufacture/use of trademarks. The Press Note No.9 (2000 series), of the Government of India, Ministry of Commerce & Industry, Department of Industrial Policy & Promotion (SIA) allowed payment of royalty upto 2% for exports and 1% for domestic sales under automatic route on use of trademarks and brand name of the foreign collaborator without technology transfer.

From the above, it is seen that the approval was sought by the company and granted by the Reserve Bank of India, under the Exchange Control Policy of the Government of India. The branding fee payment, as a general rule is allowed by a Press Note No.9 issued by Ministry of Commerce and Industry. This approval indicates that such payments are not prevented or blocked by the Government, considering the present Exchange Control Policy. There is no intervention from the Government for such payments considering the Exchange Control Policy, but such transaction satisfies the principles of Arm's Length or not is not the concern or within the jurisdiction of the Reserve Bank of India. This requires to be decided as per the provisions of Income Tax Act, 1961. The payment should satisfy the provisions of the Act, separately and independently, irrespective of the allowability of payment as per Exchange Control Policy. Similar is the view of Tax Administration of most of the countries. The Guidelines of Tax Administration of France, on the issue, refers to "please note, finally, that, although the authorization given by the Ministry of Industries or by any other technical department, with respect to the rate of a royalty or of the amount which may be transferred abroad, is not binding on the tax administration, the Inspector, nevertheless have regard to it (source IBFD Publications)'

The company also cited CBDT Circular No.6-P, dated 06.07.1968 and the decision of Pune ITAT, in the case of Kinetic Honda Motor Limited vs. Jt. CIT [77 ITD 396), in support of Its contentions. The Board's Circular and the decision are gone through. The circular as well as the decision of ITAT, Pune, deals with payments covered u/s.40A(2)(b) of the I.T. Rules, 1962 Hon'ble Tribunal referred to the Circular No.6-P, dated 06.07.1968 and observed that, when payments are approved by

one wing of the Government, there is no question of such payments being treated s excessive or unreasonable having regard to legitimate business needs. The Tribunal's decision deals with the remuneration of director of a company approved by Company Law Board. In the present case, as discussed above, the approval by the Reserve Bank of India cannot be considered as an approval for making payments at Arm's Length. The approvals from the Foreign Investment Promotion Board/SIA/RBI, are for the purpose of satisfying the requirements of Foreign Exchange Regulations. In all the applications, the companies were required to justify the payments in Foreign Exchange, by indicating, how the country will be benefiting by the Net Foreign Exchange earning in the arrangements. These approvals are for checking the effect of agreements on the Foreign Exchange Reserve of the country.

Due to this, the contention of the company that, the agreement is approved by the Reserve Bank of India, on its own, does not support the Arm's Length nature of the payment, accordingly, rejected.

(ii) It further contended that, "The Transfer Pricing Regulations introduced in India requires complying with Arm's Length Principle by testing the controlled transactions with that of comparable uncontrolled transactions. In other words, it is respectfully submitted that transactions entered into inter-se between associated enterprises-controlled transactions cannot be applied to test the compliance with Arm's Length principle".

16. The TPO rejected the reply of the assessee, observing that controlled transactions cannot be used for computing ALP, as per OECD guidelines in para 1.70, which classified,

"... that evidence from enterprises engaged in controlled transactions with associated enterprise may be useful in understanding the transactions with associated enterprise may be useful in understanding the transaction under review or as a pointer to further investigation. The dealings between associated enterprises, for comparison, can also be used in the cases of last resort where:

(i) There is sufficient data available to demonstrate their reliability.

(ii) Related party comparable data provides the most reliable available data upon which to determine or estimate an Arm's Length outcome.

(iii) In the FMCG Sector, most of the big companies in India, are part of Multi-National Enterprises, and their transactions would certainly be the controlled

> *transactions. There would be very few companies, in the FMCG Sector other than MNCs, wherein, any royalty is paid by them to unrelated parties. The details regarding any such company could not be found on the website of SIA/RBI "www.siadipp.nic.in/publicat/newsltr" meaning thereby in FMCG sector, such royalty payments are not approved".*

Considering the above and as the information regarding payment of royalty by the Cadbury Group entities to CSOL is available, the same is used as a bench mark to decide the Arm's Length rate of royalty and the contention of the company is rejected".

"The company, itself, vide letter dated 20.01.2005 submitted the meaning of the term "Trademark" in the commercial parlance, the same is reproduced below "a market place device by which consumers identify good and services and their source. In the context of trademark nomenclature, it is that the consumers will make future purchase of the same goods and services."

"Trademark recognition develops from years of customer service, consistent packaging, and quality control. Depending on the strength of a trademark, the maintenance of the desired consumer awareness level generally requires significant, continuing advertising investment."

In the case of company, Cadbury India is investing huge amounts in Advertising Campaigns; therefore, It is Cadbury India, who is building the brand value, without commensurate compensation from CSOL. Due to these reasons, it would be more appropriate, to club the payments made for two agreements and compare the same with the payments made by other affiliated companies.

(iv) Cadbury India argued that, "the company in conformity with the regulations and the guidelines, benchmarked the payment of brand fees by application of TNMM. The TNMM method was applied by comparing the margin earned by comparables independent enterprises. As per the said analysis, the net profit margin of the company is within the range of the margins earned by comparable companies. Accordingly, under the facts of the case, the payment towards technical assistance can be said to comply with the Arm's Length Principles/' The assessee has used Transactional Net Margin Method for computing the Arm's Length Price of the International Transactions by comparing the Net Profit Margin of the company :at entity level with that of other companies engaged in Food Products1 Beverages and Tobacco Business. The transaction pertaining to payment of

Royalty is not separately and independently benchmarked. The company has identified DFM Foods Ltd., Bakemans Industries Ltd., Modern Food Inds. (India) Ltd., Parrys Confectionery Ltd. and Ravalgaon Sugar Farm Ltd. From the Prowess/Capitaline Database, it is seen that none of these companies are paying any technical fees/royalty. Therefore, these companies cannot be used in the analysis for benchmarking the royalty payments. The total sales of Cadbury India Ltd. is nearly Rs.645 crores and all international transactions, are of value of 14.50 crores, which is only 2.24% of the turnover. The use of Transactional Net Margin Method, at entity level, for benchmarking such a small transaction, will not be the most appropriate method, because, such a transaction does not in a big way affect the profitability of the company. In the present case, the data regarding comparable, though controlled transactions are available, and therefore, Comparable Uncontrolled Price method is the most appropriate method".

"The total royalty worked out by the company is Rs.63,668,246/-. The company was asked to submit the working of royalty as per Press Note No.1 (2002 Series), issued by Secretariat for Industrial Assistance, Government of India. As per this Press Note, the formula for calculation of royalty for the use of trademark and brand name is:

"Royalty on brand name/trade mark shall be paid as a percentage of net sales, viz., gross sales less agents/dealers' commission, transport cost, including ocean freight, insurance, duties, taxes and other charges, and cost of raw materials, parts, components imports from the foreign I/censor or its subsidiary/affiliated company."

The company submitted the working for the same in Annexure 4 of the letter dated 11.02.2005. The revised royalty payment works out to Rs.61,840,438/- Tax Deduction:

The chronological events leading to payments of this royalty are

(i) Date : 26.04.2001 - Cadbury Board passes the resolution for payment of royalty w.e.f. 01.04.200 1.

(ii) Date : 30.04.2001 - Application made to RBI for approval of royalty payment.

(iii) Date : 25.06.2001 - Date of approval of Exchange Control Department of Reserve Bank of India, providing approval to enter into technical collaboration, for use of trademarks. As per the approval, the duration of agreement will be 10 years from the date of agreement or 7 years from the date of commencement of commercial production whichever is earlier.

(iv) Date : 12.02.2002 - Trademark License Agreement made, though commencement date Is mentioned at 01.04.2001.

The royalty could not have been paid without the approval of RBI, therefore, the company was asked to submit objection to the intention of this office to compute the royalty for Tax Deduction purpose, for the period of 25.06.2001 to 31.03.2002 only. The company submitted that, the Reserve Bank of India, after considering the application of the company, approved payment of trademark royalty from 01.04.2001. The application of the company made to RB! is gone through, wherein, the company requested to issue automatic approval effective 01.04.2001 so that the payment can commence from that date. The approval of RBI, does not refer to effective date of payment, therefore, the royalty for the period of July, 2001 to March, 2002 only, is allowable as Tax Deduction for the year. For these months, the Brand Royalty is computed at Rs. 51,819,324/- and the same worked out as per the computation provided in Press Note No.1 amounts to Rs. 5O,331,678/-".

He, therefore, computed the royalty payment on trademark usage at Rs. 5,03,31,678/-.

17. The TPO, therefore, suggested a net adjustment of Rs. 2,46,61,370/- on payment of both kinds of royalties, i.e. royalty on technical knowhow and royalty on trademarks as:

S. No.	Transaction	As per books	ALP as per TPO	Difference
1.	Royalty on tech. knowhow	5,66,24,003	4,52,99,202	1,13,24,801
2	Royalty on trade marks	6,36,68,247	50,33,678	1,33,36,569
	Total	**12,02,92,250**	**9,56,30,880**	**2,46,61,370**

18. The AO, in accordance with the above, made addition to the tune of Rs. 2,46,61,370/- to the income of the assessee.

19. The assessee approached the CIT(A), before whom the assessee reiterated its submissions made before the TPO/AO. The CIT(A) on examining the submissions, made proposal for enhancement for disallowing the entire payment of royalty on trademark usage technical knowhow at 1.25%, as the same were not wholly and exclusively incurred for the purpose of the appellant's business.

20. On receipt of the show cause notice for enhancement, the assessee gave a detailed reply with regard to the genuineness and correctness of royalty payments on both counts. The CIT(A), on receipt of the detailed submission from the assessee held,

"Based on the submissions filed on record, explanations provided from time to time, documents evidencing provision of

technical know-how, I am satisfied that the Appellant has received several benefits on account of payment of technical know-how royalty and the same have been evidenced by supporting documents"

21. On observations with regard to brand ownership, the CIT(A) held,

"5.7 The Appellant, has submitted that the Overseas AEs have merely granted the Appellant, the rights to use the trademarks and all the rights with regard to decision making on licensing / exploitation / sa1e of trademarks, maintaining the trademarks, protecting the trademarks etc continues to lie with the Overseas AEs.

Extracts from The Report on the Attribution of Profits to Permanent Establishments dated 17 July 2008 issued by the OECD were brought to my attention that defines, economic ownership' in the context of Article 7, as under:

"The economic ownership over an intangible asset relates to the ongoing contribution and investment in the property to maintain the development and value of the intangible. This is generally evidenced by marketing expenditure but is not limited to this. It also relates to the exertion of practical control over the intellectual property and hence decision making with respect to the use and exploitation of the asset. In respect of trademarks for example, while expenditure for promotions and advertising may be contributing to the value of the asset through promotion of the brand this may not be sufficient of itself to demonstrate economic ownership of the asset."

In this regard, the Appellant submitted that the economic ownership over an intangible asset could relate to the ongoing significant contribution and investment in the intellectual property to maintain and .develop the value of .the intangible. Thus, the economic owner must have the rights to use and exploit the asset in the first instance. Thereafter the extent to which the exploitation and economic control over the intellectual property is possible subject to the legal contractual relationship between the two parties which governs the terms and conditions.

The Appellant explained that Overseas AE is the intellectual property owner of the trademarks and without access to this trademarks, the Appellant would be unable to exploit the intellectual property in the Indian market. With respect to the exploitation of the intellectual property, it was submitted that the Appellant has merely been granted the right to use the trademarks on the licensed products manufactured in accordance with the prescribed specifications. The Appellant

thereafter undertakes marketing and selling of the products using the brand "Cadbury".

It was further explained that economic and commercial value of, a 'brand' is typically driven by the income-stream it generates. However, the Appellant has merely contributed approximately 1% of the total sales of CSOL over the years from 2001-2008. This clearly indicates the Appellant has hardly contributed to the total group turnover and hence it cannot be termed as the economic owner of the 'Cadbury' brand. In fact, it is because of the global brand that it represents that the Appellant has been able to capture approximately 75% of the market share. It was also stated that while Cadbury has been in India from 1948, the brand per-se has been in existence since 1824 and it was a well developed brand even before it was introduced in India.

5.8 Advertisement expenses incurred by the Appellant

With respect to the advertisement expenditure incurred by the Appellant, it was submitted that marketing expenditure in itself is insufficient for a claim to economic ownership over an asset.

The Appellant has contended that it is in the business of manufacturing and distribution of chocolates, sugar confectionery and malted food drinks in India based on the technology licensed by Overseas AEs, and in this regard, it incurs various business related expenses inter-alia for undertaking advertisements for the creation of "product" awareness of new products and recall value of existing product portfolio in the minds of its customers.

It was further stated the advertising expenditure is typically incurred by the Appellant for the purposes of;

a) Increasing sales of existing products by continuously reminding the customers of its products especially in case of a end in sales or when competitors launches new products / advertisement campaigns such as Kit Kat, Munch, Eclairs etc

b) Counte ring competition / acting as entry barriers for new players eg. Lindt, Mars etc

c) Informing consumers of its new product launches such as Bournville, Cadbury Silk, etc

d) Creating awareness of discounts offered on various products at a particular point of time

e) Creating a recall value of chocolates (as an alternative to Indian sweets) on festive occasions such as Diwali, New Year, Holi etc

f) Reaching out to rural markets for its low cost products

g) Marketing its health drinks/nutraceutical products (Bournvita)

The Appellant has also placed on record sample copies of the advertisement mandates provided to the advertising agencies which evidence the objective and desired outcome of the advertising to be achieved.

It has been contended that advertisements are largely undertaken to create "product recall", "popularize products in the market" "counter competition" etc. It was reemphasized based on the advertising mandated filed by the Appellant, that creating "brand" awareness was not the objective of the advertisements since "Cadbury" brand is already well known respected in India.

It has been submitted that the Overseas AEs provide strict brand guidelines so as to ensure that the overall strategy and vision associated with the brand is adhered to by the Appellant in India. The appellant has also submitted the copy of branding guidelines before me to corroborate the above.

It has also been highlighted by the Appellant that while the increased sales may have benefited the. Overseas AEs by way of increased royalty at 1% on the incremental sales, the same is insignificant as compared to the incremental quantum of profits earned by the Appellant on the increased sales and the taxes paid thereon to the Indian Government Treasury.

The Appellant has contended that the correct way of looking at royalty payment is to see the turnover achieved by the Appellant as a result of the license. It has been contended that the payment of Rs 635.68 lakhs to achieve a turnover of Rs 63,606.53 lakhs and to realize the net profit of Rs 8,892.88 lakhs is certainly reasonable and at arm's length.

Further the Appellant has also highlighted that that the advertisement and marketing efforts undertaken by the Appellant, for promoting the sales of its products in India, does not benefit the Overseas AEs directly, as they are not involved in the business of manufacture/trading of such products in India either on its own or through any of its other subsidiaries. Hence, the entire advertisement and marketing expenses incurred are purely for its own, benefit and no direct benefit accrues to Overseas AEs as such.

5.9. With respect to points raised by me during the appellate proceedings on the ruling of the AAR in case of Fosters Australia Ltd, the Appellant submitted that even the AAR and the Revenue department, in the case of Fosters Australia Limited had accepted that the owner of the trademark and the technology was Fosters Australia, overseas company and that the Indian

company was only licensed the trademark and technology for its usage. Accordingly, it is submitted that considering the decision of the AAR in the case of Fosters Australia, the Appellant cannot be considered as the economic owner of the trademark Cadbury".

22. The CIT(A) also took into consideration the AA Ruling in the case of Fosters Australia Ltd., where Fosters Australia was the owner of the trademark and technology and the Indian company was the licensed user. In the decision, it was held that the applicant cannot be considered as the economic user of the trademark. Before the CIT(A) the assessee also relied on certain third party agreements and other group companies, wherein terms and conditions, assigned in the agreements were similar. The assessee placed the copy of agreement with Harshey Food Corp. US, who had been given right to produce, market, advertise, promote, sell and distribute Cadbury licensed products under the trademark of Cadbury UK. It was also argued that the group companies and third parties to whom license has been granted are legally obliged to incur marketing/advertising expenditure while paying Royalty to the licensor and none of these partners' had faced any TP adjustment on the issue of royalty payment to the overseas AE, while undergoing TP audits.

23. The CIT(A), while examining the detailed arguments held,

6.5. The appellant had benchmarked its Royalty for trade mark and technical know how under the TNMM. Its operating margin on operating revenue came to 13.28% whereas those of its comparables in confectionary industry came to 2.17% only. TNMM is a profit based method. A royalty rate for the related party is determined indirectly by selecting a royalty rate that would give the licensee post royalty operating profits that are similar to what an unrelated party would earn by using the intangibles.

The theoretical basis of the TNMM takes the stance that, if intangible property is contributing to an entity nature, the entity will earn profits in excess of what could be observed in the absence of such intangible property. Applied to the facts of this case, the appellants 13.28% margin vis a vis average margin of comparables at 2.17% clearly establishes that the intangible property (Trademark and Technical Know How) has contributed to its excess profits. The TPO has no objection to the selection of comparable companies for benchmarking but has taken the stand that since they (comparables) are not paying trademark royalty and technical know how fees, hence cannot be used for benchmarking this transaction lacks force. In fact what distinguishes the appellant (Cadbury) from its competitors in the chocolate & confectionary market is its valuable brand name backed by the high quality products and it is this crucial factor that gives it a tremendous competitive advantage translating

into an operating margin of 13.28% despite huge turnover. In the absence of such intangible property the comparables average is languishing at 2.17% only. This huge gap justifies the 2.25% payment by the appellant to its AE. There is a direct co-relation between Cadbury's "intangible capital" and its performance.

6.6. As regard the issue of period of royalty payment based on the submissions filed before me and the explanations provided, and reviewing the chain of events, I am of considered view that the Appellant always intended to pay brandname royalty from 1 April 2001 and the same was accordingly stated in its application to the RBI. The payment of brandname royalty was approved by the RBI and RBI has not raised any question on the effective date of royalty payments. It is merely that the Appellant received the RBI approval at a subsequent date. This would however not change the effective date of payment, approved by the RBI and hence the same is allowed.

6.7. To sum up the appellant has demonstrated that the royalty payment for trade mark and know how meets the Arms Length test under TNMM. It has backed it with CUP method including third party comparables like HERSHEY, unrelated third parties in Asia to whom license has been granted. It also demonstrated that its advertisement, marketing and promotion expenses are at par with other in the same line of business. Hence, for reasons recorded as aforesaid and after taking into account all facts and circumstances the royalty for trademark at 1% and technical knowhow 1.25% for the entire F.Y. 2001-02 is considered to be at Arms Length. The consequent addition of Rs. 11,13,24,801/- for technical know how and Rs. 1,33,36,564/- for Trade marks so made is deleted".

24. The CIT(A), not only dropped the enhancement proceedings, he deleted the addition made on account of TP adjustment.

25. Against this decision, the department has filed the appeal before the ITAT.

26. Before us, the DR submitted that the revenue authorities picked up two of the other international transactions, which really pertained to Royalty payment for technical knowhow and use of trademarks. It has been submitted that royalty on technical knowhow was being paid by the assessee company to its parent AE since the signing of the agreement dated 19.03.1993 which was valid upto 08.03.2000, which was extended by SIA vide approval upto 08.03.2000, which was extended by SIA vide approval upto 14.09.2000. He further submitted that since agreement dated 20.12.2000 upto present date, the assessee company has been paying royalty on technical knowhow at the rate of 1.25%. This is being in accordance with the agreements signed on various dates.

27. He further submitted that the assessee started to pay royalty on use of trademark after taking approval of the Board of Directors on 26.04.2001 and consequential approval by the RBI. It was submitted that the assessee had been paying royalty from 12.02.2002 to its parent AE.

28. The DR, advancing the objection made by the TPO submitted that the agreements entered into by group companies in other parts of the world had been paying composite royalty, which came to 2%, whereas, the assessee had been paying royalty ranging between 1% to 1.25% and that the agreements entered into by the assessee company and its parent AE have overlapping clauses, pertaining to the payment of royalty on technical knowhow and trademark usage.

29. Besides this objection, the DR submitted that in the course of proceedings before TPO, the TPO raised the issue of payment of AMP, which had been left without any comments, in respect of computation of ALP.

30. The DR also submitted that CUP method would be most suitable method, as there are no segment wise data available. The DR further submitted that the assessee brought on record fresh agreements, which have not been seen by the AO/TPO along with AMP issue and for this reason, the issue deserves to be restored to the AO who shall reexamine the issue afresh.

31. The Senior Counsel appearing on behalf of the assessee responded that in so far as the royalty on technical knowhow is concerned, 2% has been accepted in the case of the assessee over the years. He further pointed out that as per the data placed before the TPO and then before the CIT(A) the average royalty received by the parent AE from global entities is coming to 2.32% (as recorded by the revenue authorities in their orders). According to the Senior Counsel, even the guidelines issued by OECD is at a higher percentage at 2.25%, therefore, the royalty paid to the parent AE is well within the prescribed limits and therefore, no AL adjustment is called for. Similarly, the royalty payment on trademark usage, at 1% is well within the arms length and has been continued from the preceding year.

32. On the issue of AMP issue, the Senior Counsel submitted that since the issue was never before the TPO, the enhancement proceedings as initiated by the CIT(A) were dropped, after being fully satisfied.

33. The Senior Counsel placed reliance on the decision of Lumax Industries Ltd. vs ACIT, in ITA No. 4456/Del/2012, wherein the coordinate Bench at Delhi has accepted TNMM on royalty payments. He submitted that the case law relied upon by the DR, wherein the ITAT rejected TNMM and restored the issue to the file of the AO, does not have any relevance, when a definite finding from the coordinate Bench is there.

34. He further relied on the decision in the case of ITO vs Industrial Roadways, reported in 112 ITD 293, wherein the coordinate Bench at Mumbai held, "*that if additional evidence furnished by the assessee before the first appellate authority is in nature of a clinching evidence, leaving no further room for doubt or controversy, in such a case no useful purpose would be served by following evidence/material to AO to obtain report and in such exceptional circumstances, said requirement may be dispensed with*". He therefore, submitted that there is no occasion for restoring the TP issue to the file of the AO to look into the issue of AMP, which is not impugned before us.

35. The Senior Counsel, therefore, submitted that the CIT(A) was correct in holding that the payments made under both the types of royalties were at arms length and no adjustment addition needs to be made.

36. The DR in the rejoinder submitted that the in the interests of justice the issue needs to be restored to the file of the TPO.

37. We have heard the detailed arguments from both the sides. The basic issue is the correctness of ALP on the royalty payments made by the assessee company to its parent AE on account of technical knowhow and trademark usage.

38. From the arguments of the DR, made on behalf of the TPO, the agreement for paying royalty on technical know how at 1.25% and trademark usage at 1.25%, were overlapping and thus, TNMM method used by the assessee was incorrect. According to the TPO, the best method to ascertain ALP in the interest case was CUP, as the transactions were controlled. This was reasonable, as no data was available from independent source to benchmark the transactions.

39. On going through the records and the orders of the revenue authorities, we find that in so far as the payment of royalty on technical knowhow concerned, the assessee has been paying to its parent AE right from 1993, as, other group companies are paying across the globe. It has been accepted by the TPO that the payment does not effect the profitability of the assessee, if we are to examine the issue from that angle as well. In any case the payment of royalty on technical knowhow is at par with the similar payments from the group companies in other countries & region. Besides this, the payment is made as per the approval given by the RBI and SIA, Government of India. Hence there cannot be any scope of doubt that the royalty payment on technical knowhow is not at arms length.

40. Coming to the issue of royalty payment on trademark usage, we find that the assessee, in fact is paying a lesser amount, if the payments are compared with the payments towards trademark usage, by the other group companies using the Brand Cadbury in other parts of the world. On the other hand, if we examine the argument taken by the TPO with

regard to OECD guidelines. On this point the assessee's payment is coming to a lesser figure, as discussed in detail by the CIT(A).

41. We are not going into the arguments advanced by the DR/TPO on geographical differences, and payments made to Harshey, as these arguments gets merged in the interpretation and details available in the table supplied by the assessee and taken note of by the TPO and the CIT(A).

42. We are also not referring to the case of Maruti Suzuki Ltd. as we find that in so far as the instant case is concerned, there is really no relevance.

43. On the basis of the above observations, we are of the opinion that the royalty payment on trademark usage is within the arms' length and does not call for any adjustment.

44. We, therefore, sustain the order of the CIT(A) and reject the grounds as claimed by the department.

45. Ground no. 1 as raised by the department is rejected.

46. Ground no. 2 pertains to domestic issue, wherein the CIT(A) allowed the 50% of expenses incurred on renovation of office complex and other expenses pertaining to electric installation, treating the same to be revenue.

47. The facts are that the assessee undertook refurbishing of the Cadbury House and claimed an aggregate expense of Rs. 2,39,38,000/-, which is as under:

Party Name	***Description***	***Amount (Rs.)***
Dalal Consultants	*Upgradation of Cadbury House*	*21,73,793*
Dalal Consultants	*Upgradation of Cadbury House*	*5,73,924*
Nitin Parulekar Architects	*Architects, interior design work*	*88,860*
Hitesh Shah & Associates	*Plumbing/removing window frams/ debris, etc.*	*30,160*
Hitesh Shah & Associates	*Plumbing/removing window frams/debris, etc.*	*30,160*
Hitesh Shah & Associates	*Fixing Ms Steel support/bamboo scaffolding*	*29,040*
Roshan Electrical Contractor	*Supply & Installation of electrical items*	*14,44,694*
Interscape	*Civil, Exterior and Plumbing works*	*1,60,63,652*
S.R. Network	*UTP CAT 5 cable/connectors/cords/ cabling work*	*10,45,103*

Geeta Network	*Repairing with upholstery work Board rooms chairs*	*34,240*
Geeta Network	*Repairing with upholstery work /Dir Chairs/Meeting room chairs/staff chairs*	*99,720*
Neutron Electronics	*Reinstallation charges NEC-M-100*	*50,000*
	TOTAL	***2,39,38,000***

48. The assessee in its submissions before the AO claimed that in fact the repairs, renovation, refurbishing, plumbing expenses and architects fee was much higher and much more. The assessee had suo moto capitalized all the expenses, which were in the nature of capital.

49. The AO disallowed the entire expenditure, claimed as revenue by the assessee. The AO observed in the assessment order that "*the whole exercise has resulted into the additional utilizable space and long term increase in the value and strength of the building. The items claimed as revenue expenditure are part and parcel of the total expenses incurred on renovation and therefore, only a part cannot be said as capital expenses and remaining as revenue expenditure, therefore, the entire expenditure is disallowed as capital expenditure and 10% depreciation is allowed*". He, therefore, added back Rs. 2,15,44,200/- (Rs. 2,39,38,000 0 Rs. 23,93,800/-).

50. The assessee approached the CIT(A), before whom the assessee reiterated its submissions. The CIT(A) taking into consideration the submissions placed before him, along with the evidence and details, pertaining to the issues of various renovation jobs, allowed benefit to the extent of 50% on the interior designs work at Rs. 21,94,800/- and supply and installation of electrical items at Rs. 14,44,694/-.

51. Against these allowances, the department is in appeal before the ITAT.

52. Before us, the DR submitted that the view taken by the AO was correct because the nature of renovation work is of enduring benefit and falls squarely within the capital field. On the basis of these arguments, the DR submitted that even the allowance of 50% by the CIT(A) was unjustified.

53. The AR on the other hand pleaded that the expenses incurred by the assessee are purely in the nature of repairs and maintenance and are allowable as revenue.

54. We have heard the arguments of the parties before us and area of dispute for our consideration is very limited, i.e. 50% allowance on the payment made to Nitin Parulekar Architects for interior design works at Rs. 21,984,800/- and payment made to Roshan Electric Contractors at Rs. 14,44,694/-.

55. The CIT(A) has allowed only 50%, though, on adhoc basis, the impugned expense, which according to us are quite reasonable.

56. We, therefore, sustain the order of the CIT(A) and reject the ground of appeal, as filed by the department.

57. Ground no. 2 is therefore, rejected.

58. In the result, appeal filed by the department is dismissed.

ITA No. 7408/Mum/2010: (Assessee appeal):

59. The following grounds have been raised:

"GROUND NO. 1- Expenditure incurred on rural development Rs. 1,07,891/-.

On the facts and in the circumstances of the case and in law, the CIT(A) erred in confirming the action of the Additional Commissioner of Income Tax, Range 5(1), Mumbai ("the AO") of disallowing Rs. 1,07,891/-, being expenditure incurred on rural development in villages near the Appellant's factory, on the alleged ground that the said expenditure has no nexus with the business carried out by the Appellant without considering the fact that such expenditure incurred out of commercial expediency, it enhances the corporate image of the Appellant Company and also promote its business.

GROUND NO. 2: 8OHHC - Miscellaneous Income and Trade Discount Rs. 9944,920/- and Rs. 5,13,72,467/-

On the facts and in the circumstances of the case and in law, the CIT(A) erred in confirming the action of the AO of treating miscellaneous income and trade discount as part of the total turnover for the purpose of computing deduction u/s. 8OHHC of the Act.

GROND NO. 3 : 8OHHC — Interest Rs. 6,47,94,044/-

On the facts and in the circumstances of the case and in law, the CIT(A) erred in confirming the action of the AO of reducing 90% of the gross interest received while computing deduction u/s. 8OHHC of the Act on the alleged ground that there is no nexus between the two without netting off the same against interest paid.

GROUND NO. 4: Payment to Third Party Manufacturer Rs. 22,64,396/-

On the facts and in the circumstances of the case and in law the CIT(A) erred in not considering and directing the AO to allow the deduction of Rs 22,64,396/- being actual payment made to the Third Party Manufacturer on account of contractual obligation

GROUND NO.5: General

The Appellant craves leave to add, to alter and/or amend all or any of the foregoing grounds of appeal.

60. Ground no. 1 pertains to disallowance of Rs. 1,07,891/- on account of rural development.

61. The CIT(A) sustained the disallowance, following the order of his predecessor in the preceding year(s). We also find that the addition has been sustained by the coordinate Bench in the assessee's own case in assessment year 2001-02 in ITA No. 975/Mum/2005.

62. In the impugned order, we find that the assessee has placed reliance on the decision of *CIT vs Madras Refineries Ltd.*, reported in 266 ITR 170 (Mad). This case has not been considered by the CIT(A), rather, the CIT(A) followed his predecessor's order. As a correct judicial propriety, the issue should be held against the assessee, following the order of the coordinate Bench in the preceding year, but the fact that the assessee factory is located in the village belts at Induri, near Mumbai and Malana, in Madhya Pradesh. The upliftment of these areas, though not directly relatable to the business of the assessee but is certainly a matter of good corporate governance through corporate citizen, which is encouraged by the government. This is what has been held in the case of Madras Refineries Ltd. (supra). It may not be out of place to mention, that in the case of Indian Rayon & Industries Ltd. (now known as Aditya Birla Nuvo Ltd.), (where one of us was a party to the decision), in ITA No. 5421/Mum/2005 have allowed a similar expense.

63. In these circumstances, in the interest of justice and the current need for being a better corporate citizen, the issue is restored to the file of the AO, who shall reexamine the nature of expense in the light of Madras Refineries Ltd. (supra) and Aditya Birla Nuvo Ltd. ITA No. 5421/Mum/2005 (supra) and allow the expense, if the assessee has incurred expenditure for upliftment of local village community, as a good corporate citizen.

64. Issues raised in Grounds No. 2 to 4 are dealt with and are covered by the various orders of the coordinate Benches of the ITAT, in the case of the assessee. Since the grounds are covered on identical issues, we for the sake of brevity are not deviating from the inferences drawn by the coordinate Benches.

65. Ground no. 2 pertains to Miscellaneous income and trade discounts amounting to Rs. 99,44,920/- and Rs. 5,13,72,467/-.

66. At the time of hearing, the AR pointed out that the issue is covered by the order of the coordinate Bench in ITA No. 957/Mum/2005 in assessment year 2001-02 in assessee's own case, wherein in para 6.1, it has been held,

> *"6.1 After hearing both parties, we find that this issue is covered by the decision of the Tribunal in assessee's own case in assessment year 1995-96 in ITA No.1641/M/2003 dated 8.10.2010. The Tribunal in the said year noted that the miscellaneous income which included trade discounts, miscellaneous sales, sales tax,*

> *excise duty etc. had to be included in the total turnover except the sales tax and excise duty which did not contain an element of turnover in view of the judgment of the Hon'ble Supreme Court in the case of CIT vs. Lakshmi Machine Works (290 ITR 667). The facts this year are identical. Therefore, we confirm the order of CIT(A) except in relation to sales tax and excise duty which will be excluded from the total turnover.*
>
> *7. The sixth dispute is regarding reduction of 90% of interest from profit of business as per Explanation (baa) while computing deduction under section 80 HHC. Assessee had received interest on FDRs, ICDs and others aggregating to Rs.5,21,04,545/-. The AO excluded 90% of the same from the profit of the business while computing deduction under section 80 HHC which in appeal was confirmed by CIT(A). Assessee has disputed the decision of authorities below to exclude 90% of the gross interest and not net interest income.*
>
> *7.1 We have heard both the parties, perused the records and considered the matter carefully. Earlier the Hon'ble High Court of Bombay in case of CIT vs. Asian Star Co. Ltd. (326 ITR 56) had held that 90% of gross interest has to be reduced from the profit of business as per Explanation (baa). However the said decision of the Hon'ble High Court has not been up held by the Hon'ble Supreme Court who in the case of ACG Associated Capsules Ltd. (343 ITR 89), have recently held that 90% of net receipts have to be reduced as per Explanation (baa). We, therefore, set aside the order of CIT(A) and hold that 90% of net interest income is required to be reduced after deducting expenses incurred having nexus with earning of interest income. The issue is thus restored to AO for working out 90% of net interest income after allowing opportunity of hearing to the assessee".*

67. The DR placed reliance on the orders of the revenue authorities.

68. We have gone through the orders of the revenue authorities and have also perused the order in ITA No. 975/Mum/2005 (supra). We find the issue is covered and we do not find any reason to deviate from the order in the assessee's own case. We hold accordingly.

69. Ground no. 2 is therefore allowed.

70. Ground no. 3 pertains to reduction of gross interest from the computation of deduction u/s 80HHC.

71. At the time of hearing, the AR pointed out that the issue is covered by the order in ITA No. 975/Mum/2005 in paras no. 7 and 7.1, which reads as under:

> *7. The sixth dispute is regarding reduction of 90% of interest from profit of business as per Explanation (baa) while computing*

deduction under section 80 HHC. Assessee had received interest on FDRs, ICDs and others aggregating to Rs.5,21,04,545/-. The AO excluded 90% of the same from the profit of the business while computing deduction under section 80 HHC which in appeal was confirmed by CIT(A). Assessee has disputed the decision of authorities below to exclude 90% of the gross interest and not net interest income.

7.1 We have heard both the parties, perused the records and considered the matter carefully. Earlier the Hon'ble High Court of Bombay in case of CIT vs. Asian Star Co. Ltd. (326 ITR 56) had held that 90% of gross interest has to be reduced from the profit of business as per Explanation (baa). However the said decision of the Hon'ble High Court has not been up held by the Hon'ble Supreme Court who in the case of ACG Associated Capsules Ltd. (343 ITR 89), have recently held that 90% of net receipts have to be reduced as per Explanation (baa). We, therefore, set aside the order of CIT(A) and hold that 90% of net interest income is required to be reduced after deducting expenses incurred having nexus with earning of interest income. The issue is thus restored to AO for working out 90% of net interest income after allowing opportunity of hearing to the assessee".

72. On going through the order of the revenue authorities and the order of the Coordinate Bench in assessee's own case in assessment year 2001-02, we are of the opinion that for the sake of continuity and consistency the issue be restored to the file of the AO.

73. Ground no. 3 is allowed for statistical purposes.

74. Ground no. 4 pertains to payments of Rs. 22,64,396/- made to third party manufacturers.

75. The CIT(A) has followed the decision taken by his predecessor. In the order of the ITAT in ITA No. 975/Mum/2005, in the preceding year, the addition has been sustained, wherein it has been held in paras no. 3 and 3.1,

"3. The second dispute is regarding disallowance of provision for contractual liability towards 3rd party manufacturers/ convertors in relation to excise duty payable amounting to Rs.61,44,628/-. The assessee was is engaged in the business of manufacturing and sale of malted foods, cocoa based products including confectionary which were being manufactured at its own factory as well as under agreement with third party manufacturers/converters at their factories. In respect of products manufactured at company's own factory, excise duty is paid on the basis of company's wholesale trade price less permissible deductions in the nature of post manufacturing expenses (PME) incurred by the company on freight, octroi,

additional sales tax etc. The third party manufacturers converters were initially paying excise duty on the products manufactured for Cadbury on the basis of cost of raw material, packing material and conversion charges which included third party manufacturers/converters' margin of profit. However, the excise authorities disputed the said basis of valuation and claimed that excise duty on products manufactured by third party manufacturers/converters is payable on the basis of Cadbury's whole sale trade price less PME. Accordingly, the excise department issued a show cause cum demand notice and directed the manufacturers/converters to pay excise duty on the basis of normal price worked out from the prices charged by the assessee company to their wholesale dealers. The said third party manufacturers/converters disputed the basis adopted by the Excise authorities for levy of excise duty and the said dispute became the subject matter of appeal before the Excise Duty Appellate Authorities. Although the primary liability to pay the excise duty was that of the third party manufacturers/converters, the said excise duty liability was to be paid by the assessee company as per the agreements as and when was payable. Since the said dispute was not settled in the year under consideration, the assessee company retained the liability in respect of the disputed amount to the extent of Rs.61,44,628/- in view of its contractual obligations towards the third party manufacturers/converters by reducing its sales to that extent and crediting the accounts of the third party manufacturers/converters. In the result, the sales were shown less to that extent in the Profit & Loss Account and in effect, deduction was claimed on account of provision for liability towards contractual obligation to the third party manufacturers/ converters in computing the total income which was disallowed by the AO following decision in earlier year. In appeal the CIT(A) has confirmed the disallowance following the appellate order in the earlier year, aggrieved by which the assessee is in appeal before the Tribunal.

3.1 After hearing both the parties, we find that this issue had been adjudicated by the Tribunal in assessment year 1994-95 in ITA No.282/M/00. In the said year, the Tribunal noted that the assessee was following mercantile system of accounting as per which contractual liability accrued on the date of its ascertainment and was allowable in the year of ascertainment. In this case, the liability was pending in dispute and therefore, the same had not been incurred during the year. Facts this year are identical and, therefore, respectfully following the decision of the Tribunal in the year 1994-95 (supra), we confirm the order of CIT(A)disallowing the claim".

76. As the facts are identical and the reasoning given by the ITAT is one the similar basis, we, therefore, following the order of the coordinate Bench in the preceding assessment year, confirm the disallowance.

77. Ground no. 4 is rejected.

In the result, appeal filed by the assessee is partly allowed.

To sum up:

Assessee's appeal in ITA 7408 of 2010 stands partly allowed

Revenue's appeal in ITA 7641 of 2010 stands dismissed.

Order pronounced in the open Court on 13th November, 2013.