THE INCOME TAX APPELLATE TRIBUNAL
"K" Bench, Mumbai
Before Shri Shamim Yahya (AM) & Shri Pawan Singh (JM)

I.T.A. No. 1228/Mum/2015 (Assessment Year 2010-11)

M/s. Diageo India Pvt. Ltd. **Nicholas Piramal Tower** **Peninsula Corporate Park** **Ganpatrao Kadam marg** **Lower Parel** **Mumbai-400 013.**	**Vs.**	**ACIT-6(2)(2)** **Room No. 504** **Aayakar Bhavan** **M.K. Road** **Mumbai-400 020.**
(Appellant)		**(Respondent)**

I.T.A. No. 1813/Mum/2015 (Assessment Year 2010-11)

ACIT-6(2)(2) **Room No. 504** **Aayakar Bhavan** **M.K. Road** **Mumbai-400 020.**	**Vs.**	**M/s. Diageo India Pvt. Ltd.** **Nicholas Piramal Tower** **Peninsula Corporate Park** **Ganpatrao Kadam marg** **Lower Parel** **Mumbai-400 013.**
(Appellant)		**(Respondent)**

PAN : AAACI3378L

Assessee by	**S/Shri Percy J. Pardiwala, Hiten Chande & Nimesh Vora**
Department by	**Shri Anand Mohan**
Date of Hearing	**07.10.2019**
Date of Pronouncement	**19.12.2019**

O R D E R

Per Shamim Yahya (AM) :-

These are cross appeals by the assessee and the Revenue arising out of the order of the Assessing Officer dated 30.1.2015 u/s. 143(3) r.w.s. 144C(13) of the Act pursuant to the direction of the learned DRP dated 19.12.2014.

2. Grounds of appeal in Revenue's appeal read as under :-

1. "Whether On the facts and circumstances of case and in law, the Hon'ble DRP has erred in allowing set off of reimbursement of AMP expenditure reimbursed by the AE to assessee even after coming to a finding in Para 12.6 of its order that the compensation received by the assessee does not have any sound and scientific basis."

2. "Whether On the facts and circumstances of case and in law the Hon'ble DRP has erred in set off reimbursement of AMP expenditure by the AE to assessee ignoring the fact that the assessee has failed to show proper basis on which the compensation amount has been received on account of reimbursement of AMP."

3. "Whether on the facts and circumstances of the case and in law the Hon'ble DRP has erred in rejecting the comparables used by the TPO for determining the Bright Line test merely by following its earlier order and without going in to merits of the comparables companies."

4. The appellant prays that the direction of the Hon'ble DRP-I on the above grounds be set aside to the file of the AO or confirm the order of the AO.

3. Issues raised in assessee's appeal are as under :-

i) Transfer pricing adjustment on account of advertisement and sales promotion expenses Rs. 14,42,00,000/-.

ii) Disallowance of royalty.

iii) Disallowance of expenses incurred for liaison officer in Sri Lanka Rs.6,69,242/-.

4. Brief facts of the case are that M/s. Diageo India Private Limited (hereinafter referred as DIPL) is engaged in the business of manufacturing and distribution of alcoholic beverages of domestic consumption. Assessee-company is a wholly owned subsidiary of Selvic Netherlands BV, which is a part of Diageo group. During the assessment year the assessee had incurred advertisement expenses of Rs. 15.79 crores and selling expenses of Rs. 25.96 crores. The total AMP expenses were Rs. 41.75 crores. In his order the TPO held that the assessee has incurred excessive AMP expenses which resulted in brand promotion for the AEs without any commensurate compensation from the AEs in this regard. The TPO rejected the segmental data of the assessee and proceeded to allocate the excessive expenses to manufacturing and

distribution segment of the assessee in ratio of sales. Further the TPO also held the following expenses as advertisement expenses contributing to brand promotion of AEs and allocated the same in the sales ratio of manufacturing and distribution segment :-

i) Display, glow signs etc. expenses shown as selling expenses of Rs. 1,87,37,000/- and

ii) AMP expenses of Rs. 1,05,41,690/- shown as AMP expenses on Indian brands owned by DIPL (to the extent of non-submission of vouchers) but evidence not given before TPO.

5. Accordingly, TPO arrived at the revised ratio of advertisement expenses to sales as under :-

Particulars	Manufacturing	Distribution	Indian brands	Total
Sales	203,94,34,000	4,36,03,000	10,75,22,000	219,05,59,000
Advertising expenses as per Assessee	14,45,51,000	4,93,000	1,28,11,690	15,79,71,000
Advertising expenses allocated by TPO in sales ratio	14,70,72,700	31,44,410	77,53,890	15,79,71,000
Allocation of selling expenses treated as advertising expenses by TPO	1,77,84,170	3,80,220		1,91,02,600
Allocation of advertising expenses on brands owned by DIPL to the extent of non-submission of vouchers	1,03,21,030	2,20,660		1,05,41,690
Revised advertising expenses as per TPO	17,51,77,900	37,45,290		17,89,23,190
Ratio of advertising expenses to sales	8.59%	8.59%		-

6. For Manufacturing Segment, TPO proceeded to consider comparable selected by the Assessee to benchmark AMP transactions in manufacturing segment and after rejecting few companies on the ground that they owned intangibles and came to the following set of comparable:

Sr. No.	Company name	Sales	AMP expenses	% of AMP expenses
1	Arthos Breweries Ltd.	22.99	0.00	0.00%
2	Associated Alcohols & Breweries Ltd.	80.88	0.00	0.00%

3	Blossom Industries Ltd.	151.40	1.52	1.00%
4	Empee Distilleries Ltd.	569.50	18.21	3,20%
5	GM Breweries Ltd.	318.48	0.28	0.09%
6	Globus Spirits Limited	265.00	3.54	1.34%
7	Mohan Rocky Springwater Breweries Ltd.	33.30	0.77	2.31%
8	Shiva Distilleries Ltd.	340.87	1.08	0.32%
9	Winsome Breweries Ltd.	48.31	0.57	1.18%
10	Vidhyachal Distilleries Ltd.	37.30	0.62	1.66%
11	John Distilleries Ltd.	444.32	21.60	4.86%
	Arithmetic Mean			1.45%

7. For the distribution segment, the TPO considered the following comparable and arrived at average of AMP expenses to sales as under:

Sr. No.	Company name	Sales	AMP expenses	% of AMP expenses
1	Alna Trading & Exports Ltd.	1.22		0.00%
2	Nuway Organic Naturals India Ltd.	11.87	0.05	0.4.2%
3	Chhotabhai Jethabhai Patel Tobacco Products Co Ltd.	166.25	0.36	0.22&
4	DPIL Ltd.	26.46	0.42	1.59&
5	Red Peppers Ltd.	6.64	-	0.00%
	Arithmetic Mean			0.45%

8. TPO thus held that while on average, the comparables in manufacturing and distribution segment spent 1.45% and 0.45% respectively of their sales on advertisement, whereas the assessee has spent 8.59% of its. sales on advertising, and thus based on the bright line for each of the two segment, proceeded to determine that for the manufacturing segment the assesses had incurred excessive advertising expense of Rs 14.56 crores, whereas for the distribution segment, the assessee had incurred excess advertising expenses of Rs 0.36 lakhs and made a total adjustment of Rs 14.91 crores

9. While making adjustment on account of AMP expenses, TPO did not allow the deduction for the brand contribution of Rs 65.05 lakhs received by the assessee from its AEs in respect of AMP expenses incurred by the assessee on their behalf.

Markup on AMP expenses

10. Further, TPO has treated the excessive AMP expenses incurred by the Assessee as market support/sales support services provided by the Assessee to its AEs. He proposed 11 comparables with average 19.26%. Considering submissions of the assessee, TPO finally arrived at 7 comparables with average of 13.96% and worked out an adjustment of Rs 2.08 crores being markup on AMP expenses.

Corporate tax grounds**:**

11. During the year under consideration, DIPL paid royalty to its AE viz. Diageo North America ('DNA') of Rs 6.28 crores. The AO disallowed the said payment on ground that the Assessee was unable to prove that the same was incurred wholly and exclusively for the purpose of business and disallowed the expenditure under section 37(1) of the Act.

12. Assessee has incurred expenses of Rs 6.7 lakhs for its Liaison Office ('LO') in Sri Lanka. The AO disallowed the same on the grounds that Assessee was not able to provide information to prove existence of LO in Sri Lanka and therefore disallowed the same under section 37(1) of the Act.

Apropos Advertisement and sales promotion expenses :-

13. On this issue learned DRP observed that majority of assessee's objection on this are covered by the previous learned DRP order. Hence, it held that there can be no dispute that excessive India AMP expenses is incurred to benefit the AE brands on global basis.

14. Learned DRP further held that the TPO has rejected the segmental data on the ground that the assessee has not been able to submit supporting documents and vouchers and hence, allocation is without any basis. It also observed that as noted by the TPO that segmental results have been audited three years after the close of relevant financial year and that the auditors have

merely done arithmetical verifications to confirm the allocations. Hence, it did not find any infirmity in the action of the TPO. Learned DRP further directed the TPO to verify the actual working provided by the assessee and delete the double disallowance if any.

15. On the issue of exclusion of AMP expenses incurred on the brands owned by the assessee it noted the contention of the assessee that it owned two brands which viz. 'Sharkooth' and 'Nilaya'. It noted the assessee's submission that the assessee maintained brand-wise ledger accounts of AMP expenses and hence even in the absence of all vouchers, such audited accounts may be accepted. It also noted the assessee's submission that the issue is covered in favour of the assessee by several orders in earlier years. Further learned DRP referred to the order of earlier Panel for A.Y. 2009-10 and observed that only that part of AMP expenses claimed for own brands has not been considered for TP analysis for which vouchers have been produced by the assessee. That there is no dispute that the assessee has not produced vouchers of Rs. 1.05 crores and used for own brands. Therefore it held that these expenses cannot be considered to be incurred for own brands. Accordingly, following the learned DRP direction for A.Y. 2009-10 assessee's objection was rejected.

16. As regards objection of exclusion of sales promotion expenses, learned DRP noted that DIPL had incurred total selling expenses of Rs. 25.96 crores. Further, TPO considered only Rs. 24.08 crores as selling expenses and held the balance Rs. 1.87 crores as advertising expenses. The assessee submitted that the said expenses of Rs. 1.87 crores should be considered as selling expenses. However, learned DRP rejected this contention.

17. As regards amount recovered from AEs, learned DRP accepted the contention and directed the TPO to reduce the brand contribution received from AMP expenses while computing the AMP adjustment for distribution segment.

18. Against this order assessee is in appeal before us.

19. Learned counsel of the assessee submitted that the Transfer Pricing officer has stated that assessee has incurred excess AMP expenditure as compared to comparables and therefore AMP is held to be international transaction. That the TPO applied the bright line test to determine the existence of international transaction. That dispute resolution said that the reimbursement of expenses by the AE to the extent the benefit is derived by the AE is itself indicator that expenses incurred for the AE. However it is assessee's submission that the DIPL has incurred AMP expenses on its own business for increasing sales. He submitted that the same is not an international transaction. He further submitted that even if some benefit occurs to others, no adverse inference against the assessee can be taken . He further submitted that amendment to the agreement dated 29/11/2010 was made between assessee and Diego Brand PV whereby the assessee receives a contribution which is in the nature of payment from the brand owners, not as a consideration for rendering the service but the consideration is made to ensure that assessee earns arm's-length return for its activities. The learned counsel of the assessee contended that the contribution by the AE was aimed at ensuring that the assessee achieves arm's-length margin of 5% in the manufacturing segment and 3% margin in the distribution segment. In this regard the learned counsel of the assessee placed reliance upon ITAT decision in assessee's own case for assessment year 2008 – 09 and assessment year 2009–10. Furthermore, learned counsel of the assessee referred to the decision of Hon'ble Delhi High Court in the case of Maruti Suzuki India Ltd supra. Learned counsel further submitted that bright line test is not a prescribed method under the income tax act. For this proposition he also placed reliance upon several case laws. Accordingly it is the submission of the assessee that there is no agreement arrangement or and understanding between the assessee and its AE. Further bright line test is not a prescribed method and it cannot be used to infer the existence of an international transaction. Further

the impugned AMP adjustment doesn't fall under any of the prescribed methods under the act read with rule. Hence, adjustment made on account of AMP expenses deserves to be deleted.

20. Furthermore, it is the submission of the assessee that no separate AMP adjustment is warranted under the TNMM approach. Hence, it is said that even if AMP is considered to be an international transaction, bundled transaction approach should be adopted and the TNMM analysis as performed by the assessee in its TP study should be accepted. Furthermore, it is the submission of the assessee that AMP expenditure on brands owned by the assessee is to be excluded from the total AMP expenditure. Furthermore, it is the submission of the assessee that sales related expenses are to be excluded from the total AMP expenditure. It is the submission of the assessee that assessee has incurred selling expenditure however the TPO has considered certain heads of selling expenses akin to advertisement expenditure while computing the AMP adjustment.

21. It is a submission of the assessee that TPO has failed to appreciate that the above heads of expenditure were also selling in nature as they do not contribute to brand promotion of the AE, but are incurred by the assessee to increase its sales. Furthermore, assessee has submitted that certain expenses which have been treated as advertising expenses in the profit and loss account are actually in the nature of selling expenses.

22. In this regard assessee has placed reliance upon ITAT order for assessment year 2007 in assessee's own case wherein relief of selling expenses has been granted while computing AMP adjustment. Assessee has further placed reliance upon several case laws in support of the above proposition

23. Per contra learned departmental representative referred to the definition of international transaction in the provisions of the act. Referring to the above

he submitted that to construe the AMP expenditure as an international transaction at least there should be one enterprise who is a non-resident and there should be a mutual agreement between the parties for allocation apportionment or to contribute any cost or expenses incurred in connection with benefit or services or facility.

24. Learned departmental representative submitted that the mutual agreement as required in the provision of the act does exist in the present case he referred to the amendment dated 29.11 .2010 with effect from 1 April 2009 to the agreement dated 19.9 .2016 between DIPL and overseas associated enterprises under:-

> *"9A. The licensee will incurred various AMP expenses on its own account in relation to its sales of the licensed products within the territory, and the licensor may bear by way of contribution a portion of the AMP expenditure. Such contribution shall be made in such form and quantum as may be agreed by the parties each year. Each of the licensee and licensor will contribute to AMP expenditure in the manner aforementioned for the anticipated benefits that such expenditure will bring to each of their businesses."*

25. Referring to the above learned departmental representative submitted that all the parameters which are necessary as per the provision of section 92B to consider whether AMP is an international transaction or not are existing in the present case. He further submitted that the dispute resolution panel has also rightly held that the reimbursement of AMP expenses by the AE to the extent the benefits is derived by the AE, is itself an indicator that AMP expenses are incurred by the AE. He further submitted that the argument of the assessee that the reimbursement of AMP expenses from the AE to ensure the arm's-length return for its manufacturing and distribution activities is without any basis. In this regard he again referred to the amended clause and submitted that the argument of the assessee is not at all in consonance with the language of the above said clause. His admitted that this is purely an assumption. Further suomoto fixing a 5% margin without any TP analysis for

all the years itself shows that assessee's intention of not following the TP provisions. He submitted that the assessee first fixes its own margin at 5% and then tries to find out most appropriate method and comparable which suits its design and this is not in accordance with law.

26. The learned counsel thereafter submitted that once it is proved that the AMP expenditure is an international transaction then arm's length price has to be determined by the assessee as well as TPO. The learned departmental representative submitted that the TPO has adopted bright line test as a tool to find out the ALP of the AMP. However the learned departmental representative conceded that BLT was negated by Hon'ble Delhi High Court in the case of M/s. Sony Ericsson Mobile Communications India Ltd. However he submitted that the decision came much after the present issue was decided by TPO and DRP. Learned AR submitted that even though BLT was negated in the said case the issue was set aside to find out the ALP of AMP based on the directions given by the Hon'ble court. Learned departmental representative reiterated that the assessment proceeding was not annulled by the Hon'ble High Court and the matter was remitted back to the lower authorities. Hence, learned departmental representative submitted that this issue may be set aside to the TPO with a direction to follow the principle enumerated by the High Court.

27. The learned departmental representative further submitted that even though the BLT was negated the ALP of AMP expenses has to be computed as per the principle as enumerated by the Hon'ble Delhi High Court in the case of M/s. Sony Ericsson Mobile Communications India private limited, Luxottica India Eyewear Private Limited and Heinz India private limited as the facts are similar to this case.

28. As regards the assessee's argument that no separate ALP has to be determined for AMP expenses under aggregation of TNMM as profit margin of the assessee is more than the comparables, he referred to ITAT decision in the

case of M/s. BMW India Ltd vide para 15 of the said order. Referring to the above he submitted that the argument of the assessee cannot be accepted.

29. As regards the AMP expenses incurred by the assessee towards its own brand, the learned departmental representative submitted that the same may be allowed subject to the quantum computed by the TPO. As regards the sales related expenses learned DR submitted that the principal as narrated by the Hon'ble Delhi High Court in the case of MS Sony Ericsson Mobile Communications India private limited and others are applicable to the case.

30. Referring to the distribution segment the learned AR made the same argument as above. In this regard he referred to clause 7.1 as under:-

> *"The distributor will incur various AMP expenses on its own account in relation to its sales of products within the territory and the company shall bear by way of contribution at least 50% of the AMP expenditure incurred by the distributor. Such contribution may be made in such for and quantum as may be agreed by the parties. The distributor and each of the company will contribute to the AMP expenditure in the manner aforementioned for the anticipated benefits such expenditure will bring to each of their businesses."*

31. The learned DR submitted that the decision of ITAT in the case of BMW India is squarely applicable to the assessee's case. He submitted that the assessee argued that decision is not applicable to the assessee's case as the assessee's majority income is from the manufacturing segment. Learned departmental representative submitted that this factor is important only if there is no brand contribution/reimbursement of AMP or no understanding between the associated enterprises to incur the AMP expenses. He submitted that in the present case on the basis of facts and legal principle the existence of international transaction in respect of AMP expenses is already elaborated above. Hence he prayed that the matter made the remitted back to the TPO to apply the principle animated by the Hon'ble Delhi High Court in the case of measures Sony Ericsson Mobile complication India private limited .

32. In rejoinder learned counsel of the assessee submits that the marketing policy is merely a guidance for the marketing activities to be undertaken by DIPL and to adhere to the marketing code of conduct. He submitted that assessee company is into alcohol industry which has certain restrictions on the marketing and advertisement office product. Accordingly DIAGEO group has worldwide formulated a set of guidelines to market alcoholic products in a certain responsible way. He submitted that the said code of conduct doesn't prove nor substantiate that DIPL had rendered any services to its AE under the head AMP expenses or that it is directing DIPL to incur AMP expenses. Further there were no contractual obligation on DIPL to perform/incur AMP expenses on behalf of the AE. Learned counsel submitted that to qualify as an international transaction within the scope of section 92(B) following essential ingredients are required that the transaction should be between 2 or more associated enterprises either or both of home are non-residents.

33. That the transaction should be in the nature of purchase, sale or lease of tangible or intangible property or provision of services or lending or borrowing money or any other transaction having a bearing on the profits, income, loss on of the associated enterprises.

34. He submitted that the AMP expenses therefore enhancing sale of alcoholic beverages products manufactured distributed by DIPL in the domestic market was in the business interest of the DIPL to the same.

35. Learned counsel of the assessee further submitted that decision of BMW India is not applicable to the present case. Referring to the same he submitted that there is neither any binding obligation on DIPL to incur AMP expenses not does it render any service to the AE.

36. The learned counsel of the assessee further more submitted reliance upon the Delhi High Court decision in the case of Whirlpool of India Ltd 381

ITR 154, wherein the Delhi High Court has observed that it is not discernible that there was any obligation to incur an extent of AMP expenses to build the brand of foreign AE.

37. Lastly the learned counsel of the assessee submitted that even if AMP expenditure is held to be an international transaction, since assessee's margin under TNMM has been accepted to be at arm's-length by the TPO no separate adjustment for AMP can be made hence matter need not be remanded back to the TPO for a 2nd innings

38. The learned departmental representative has made a submission that issue of intensity adjustments in AMP expenses has been considered by ITAT in detail in recent judgement of ITAT in the case of Luxottica India eyewear private limited. He submitted that the guidance on the issue is available in the judgement of ITAT.

39. We have carefully considered the submissions, the case laws and perused the records. We find that all the decisions which have been claimed by the learned counsel of the assessee to be in his favour are based on the premise that there was no agreement between the parties to incur the AMP expense. It was also found that there was no arrangement or obligation between the parties to incur those expenditure. However in the present case we find that this plank miserably fails. Even the decision of ITAT in assessee's own case for earlier year doesn't help the assessee as subsequently there was an amendment in the agreement between the parties. These amendment have already been mentioned in the above said submissions. Even at the sake of repetition we may mention the amendment with regard to the manufacturing segment and the distribution segment which reads as under:-

> *"9A. The licensee will incurred various AMP expenses on its own account in relation to its sales of the licensed products within the territory, and the licensor may bear by way of contribution a portion of*

the AMP expenditure. Such contribution shall be made in such form and quantum as may be agreed by the parties each year. Each of the licensee and licensor will contribute to AMP expenditure in the manner aforementioned for the anticipated benefits that such expenditure will bring to each of their businesses."

"The distributor will incur various AMP expenses on its own account in relation to its sales of products within the territory and the company shall bear by way of contribution at least 50% of the AMP expenditure incurred by the distributor. Such contribution may be made in such for and quantum as may be agreed by the parties. The distributor and each of the company will contribute to the AMP expenditure in the manner aforementioned for the anticipated benefits such expenditure will bring to each of their businesses."

40. From the above it is amply clear that in the present case there is a mutual agreement in existence between the assessee and its AE to incur AMP expenses and further that agreement is also existing to allocate or apportion or to contribute the AMP cost or expense. The agreement also clarifies that the level of AMP expense allocation or apportionment contribution is based on the benefit received. Thus when there is an agreement that the overseas associated enterprise will share the AMP expense of the assessee when benefitted, undoubtedly the AMP expense becomes an international transaction and the TPO cannot be debarred from examining the said international transaction with respect to the arms length price. This becomes amply clear from the fact that the overseas associated enterprise has also contributed a sum of Rs.65,05,000 towards its contribution to the AMP expense incurred by the assessee. The contention of the learned counsel of the assessee that the sum has been paid not by way of any expense having been incurred by the assessee towards AMP expense of the overseas associated enterprise but to enable the assessee to meet certain rate of return of income. The submission is not at all acceptable. Firstly this is not emanating out of the agreement. It is only an explanation carved out by the assessee. The claim of the learned counsel of the assessee that the contribution is meant to ensure that the assessee has a margin of 5% income in the manufacturing segment and 3% margin in the distribution segment is at best a self-serving statement.

Moreover as pointed out by the learned department representative this claim itself shows that assessee is having scant regard to the Transfer Pricing mechanism. It shows that assessee has a predetermined margin and thereafter went around finding comparables to justify the same. This is totally in constraint of the Transfer Pricing laws and jurisprudence. On this plank itself this explanation fails. Further it defies logic that overseas AE will pay gratuitous sum to the assessee, without any benefit to itself.

41. Once it is established that there is an agreement and arrangement of the assessee incurring AMP expenses on behalf of the overseas enterprise and getting reimbursement of the same the next question arises of determination of arm length price. In this regard it is the submission of the learned counsel of the assessee that the TNMM method applied by the assessee takes care of this. However we note that identical argument was submitted in the case of BMW Ltd supra. In our considered opinion the ratio arising out of the decision of BMW is also applicable in the present case. We may grainfully refer to the ITATs adjudication in the said case as under:-

> *"3. We have heard the rival submissions and perused the relevant material on record. The learned Sr. counsel submitted at the outset that there is no international transaction of AMP expenses in the instant case and as such there can be no question of determining its ALP. For bolstering this proposition, he relied on the judgment of Hon'ble Delhi High Court in Maruti Suzuki India Ltd vs. CIT & Another (2016) 381 ITR 117 (Del). The learned Sr. AR submitted that the TPO considered only the higher amount of expenditure incurred by the assessee vis-a-vis other comparable companies for drawing an adverse inference of there being an international transaction of brand promotion by the assessee for its AE. This was countered by the ld. DR, who strongly refuted the assertion of there being no international transaction of AMP expenses and the consequential determination of its ALP.*
>
> *4. We have gone through the relevant material on record and are not convinced with the submission advanced on behalf of the assessee that the treatment of AMP expense as an international transaction by the TPO is based only on excessive expenditure. It is found that the TPO has referred to other materials to support his conclusion of the existence of an international transaction of AMP expenses. He referred to the agreement dated 1.1.2006 between the assessee and BMW Germany and also reproduced relevant clauses of the same on page 13 of his order.*

Clause 2.2 of the Agreement deciphers the responsibility of the assessee in the Contract Territory Contract (India). Relevant parts of the clause are as under:-

> *"2.2. Responsibility in the Contract Territory BMW India represents the interests of BMW AG in the Contract Territory. It is responsible for the sales promotion and the full utilization of the market potential for the Contract Goods in the Contract Territory. .....*
>
> *Furthermore, BMW India undertakes the following functions in the Contract Territory in accordance with the laws of the contracting territory. .....*
>
> *Performance of an adequate advertisement and sales promotion as well as public and media relation.*
>
> *....."*

5. Clause 3 of the Agreement is also material for our purpose, which has been equally taken note of by the TPO as well in his order. Relevant parts of clause 3 read as under :-

"3.1. Responsibilities for Sales and Advertising The BMW India will establish and supervise in the Contract Territory an efficient BMW distribution network for sales, service and parts supply according to the recommendations of BMW. To this end, BMW India will, in its own name, enter into dealer contracts in accordance with law of the Contracting Territory."

6. On going through clause 2.2 of the Agreement, it becomes palpable that the assessee represented the interest of BMW AG in India and is responsible for the sales promotion in India. Later part of the clause stipulates that the assessee undertook certain functions in India, which include "performance of an adequate advertisement and sales promotion as well as public and media relations." Clause 3 of the Agreement refers to the responsibilities of the assessee for advertising. It provides in no unambiguous terms that the assessee will meet its responsibility for the promotion of sales .... and undertook for applying its best efforts and adequate resources towards effective sales promotion and advertising Clause 3.6 of the Agreement stipulates that the assessee "will establish and supervise ..... an efficient BMW distribution network for sales .... according to the recommendations of BMW. A close scrutiny of the above clauses of the Agreement makes it abundantly clear that the assessee was assigned and it accepted the duty to perform advertisement and sales promotion and also assumed responsibility for deploying adequate resources towards effective sales promotion and advertisement of the goods in India. It is not a case where the assessee on its own volition took up such a huge advertisement, marketing and promotion of the brand owned by its AE. In fact, it was the `responsibility' of the assessee and it `undertook' the function of `performance of an adequate advertisement and sales promotion' pursuant to the Agreement dated 1.1.2006 with BMW AG. Thus it is apparent that the assessee was under a binding obligation to advertise and promote the brand of its AE.

7. The assessee's Transfer pricing study report, as referred on page 13 and 14 of the TPO's order, also mentions that "BMW India ensures that it follows the global guidelines provided by BMW Group in terms of the usages of BMW banners, specifications for release of print advertisement in terms of font size, page layout etc.' It is thus clear that not only the Agreement between the assessee and BMW AG but also the assessee's own acknowledgment in the TP study report are flawless

pointers to the fact that it carried out AMP functions as a duty assigned by its AE, to be discharged strictly in accordance with the global guidelines provided by the BMW Group.

8. There is another interesting aspect of the matter. One of the reported international transactions is "Reimbursement of expenses (Amount received)" amounting to Rs. 67,21,54,60/-. On being pointed out to give the nature of such Reimbursement of expenses received, the learned AR took us through page 47 of the paper book, which is a part of the assessee's Transfer Pricing study report, reading as under:-

"Clause IV- Reimbursement of expenses from BMW Group Under Class IV transactions, reimbursement of expenses by BMW Group to BMW India is included. During the year, such reimbursements were primarily on account of BMW Service Inclusive Package / normal warranty claims raised by BMW India on BMW Group and certain marketing and promotion expenses incurred by BMW India on behalf of BMW Group. These expenses were subsequently reimbursed by BMW Group to BMW India...."

9. It is evident from the above extract of the Transfer Pricing Study report that the assessee received reimbursement of certain marketing and promotion expenses incurred by BMW India on behalf of BMW Group. A further detail of such reimbursements has been given in the Tax Audit Report of the assessee, whose relevant part is as under:-

Reimbursement of marketing / business promotion / other expenses

Ultimate Holding Company 16,869,213

Ultimate Holding Company (333, 945)

Fellow Subsidiaries 378, 197

Fellow Subsidiaries (545, 780)

10. The learned AR stated that the assessee received reimbursement of marketing and promotion expenses to the tune of Rs.3,33,945/- from its AE. This shows that the asessee's holding company reimbursed AMP expenses only to the tune of Rs. 3.33 lac as against enormous amount spent by the assessee for promotion of the brand owned by its AE pursuant to the agreement dated 1.1.2006. Factum of the existence of an Agreement obliging the assessee to undertake advertisement and brand promotion in accordance with the global guidelines and the AE reimbursing AMP expenses, albeit, to a very nominal extent, goes a long way to establish the existence of arrangement between the assessee and its AE for promoting BMW brand in India.

11. Reliance of the learned Sr. AR on the judgment in the case of Maruti Suzuki (Supra) to fortify his point of view of there being no international transaction of AMP expenses, is misconceived. In that case, the existence of international transaction was negatived by the Hon'ble Delhi High Court on the ground that the Revenue could not demonstrate any international transactions of ALP expenses except for showing higher amount of AMP expenses incurred by that assessee vis- à-vis other independent parties. Adverting to the facts of the instant case, we find that apart from such higher AMP expenses, the TPO has elaborately referred to the relevant

clauses of the Agreement between the assessee and its AE along with the TP Study report, showing the responsibility of the assessee to perform "adequate advertisement and sales promotion" in accordance with the global guidelines of the BMW Group for the use of BMW brand and further the AE also acknowledging such service of the assessee but reimbursing a minuscule part of expenses incurred by the assessee on advertisement marketing and promotion. It is further relevant to note that the judgment in the case of Maruti Suzuki (Supra) is based on a manufacturing company performing advertisement and promotion. In contrast, the assessee is engaged not only in the sale of manufactured goods but also the traded goods. Profit and loss accounts of the assessee shows Sale of manufactured goods at Rs. 624.66/- crore and those of traded goods of Rs.611.87 crore. Thus, it is manifest that the volume of assessee's business from trading and manufacturing is almost equal and it is not a case of manufacture alone as was there in the case of Maruti Suzuki (Supra). It is, ergo, vivid that the ratio laid down in Maruti Suzuki (Supra) is not applicable due to differentiation in the facts of the extant case.

12. It is further relevant to note that the Tribunal in assessee's own case for immediately preceding assessment year, namely, 2009-10 has decided such issue against the assessee vide its order dated 21.10.2014 in ITA No. 385/Del/2014. It is also worthwhile to mention the learned AR's contention that the Tribunal for the assessment year 2008-09 decided such issue in assessee's favour by its order dated 16.8.2013. We find from the Tribunal order for the later A.Y. 2009-10, which was also decided at a later point of time, that the Tribunal took a conscious decision of the existence of an international transaction of AMP expenses requiring determination of ALP, after duly considering its order passed for the A.Y. 2008-09. Though the tribunal decided this issue in favour of the assessee for the A.Y. 2008-09, it was candidly admitted by the ld. AR that, on an appeal preferred by the Revenue against the tribunal order for such earlier year, a substantial question of law has been admitted by the Hon'ble High Court. In view of the foregoing discussion, we reject the assessee's contention and hold that the authorities below were justified in treating AMP as an international transaction.

13. Next comes the question of determination of ALP of the international transaction of AMP expenses. It is seen that the TPO applied bright line test to find out the value of international transaction and then determined the ALP of AMP expenses. The Hon'ble Delhi High Court in Sony Ericson Mobile Communications (India)Pvt. Ltd. vs. CIT (2015) 374 ITR 118 (Del) and other judgments has held that bright line test cannot be applied for determining the ALP of AMP expenses. The Hon'ble High Court in Sony Ericson Mobile Communications (supra) has restored the matter of determination of its ALP for a fresh determination in the light of guidelines laid down in such a case. It considered the distribution and the brand promotion activities as inter- connected transactions and harped on their aggregation. Crux of the relevant observations of the Hon'ble High Court, which is crucial for our purpose, can be summarized as under :-

- *Inter-connected international transactions can be aggregated and section 92(3) does not prohibit the set-off [Paras 80 & 81]; Ø AMP is a separate function. An external comparable should perform similar AMP functions. [Paras 165 &166] ;*
- *Bright line test cannot be applied to work out non-routine AMP expenses for benchmarking [Para 194(x)];*

- *ALP of AMP expenses should be determined preferably in a bundled manner with the distribution activity [Paras 91, 121 & others] ;*
- *For determining the ALP of these transactions in a bundled manner, suitable comparables having undertaken similar activities of distribution of the products and also incurring of AMP expenses, should be chosen [Paras 194(i), (ii), (viii) & others]; If no comparables having performed both the functions in a similar manner are available, then, suitable adjustment should be made to bring international transactions and comparable transactions at par [Para 194 (iii)] ;*
- *If adjustment is not possible or comparable is not available, then, the TNMM on entity level should not be applied [Paras 100, 121, 194(iii) & (vi)] ;*
- *In the above eventuality, international transaction of AMP should be viewed in a de-bundled manner or separately [Paras 121& 194(xi)] ;*
- *In separately determining the ALP of AMP expenses, the TPO is free to choose any other suitable method including Cost plus method [Para 194(xiii)];*
- *In so making a TP adjustment on account of AMP expenses, a proper set off/purchase price adjustment should be allowed from the other transaction of distribution of the products [Para 93] ;*
- *Selling expenses cannot be considered as part of AMP expenses [Paras 175 & 176 of the judgment].*

14. With the foregoing understanding of the ratio decidendi of the judgment of the Hon'ble Delhi High Court in the case of Sony Ericsson (supra), which is probably the only judgment that has laid down the mechanism for determining the ALP of AMP expenses in an elaborate manner, let us examine the facts of the case. The assessee applied TNMM as the most appropriate method. Since the profit margin declared by the assessee was favourably comparable with the average margin of the comparables, the assessee claimed that no adjustment should be made on account of AMP expenses because such expenses stood subsumed in the overall operating profit.

15. We are unable to countenance such a point of view of the assessee for deletion of the addition towards AMP expenses on the plain logic of the assessee's profit margin being favourable with that of comparables. This is a fallacious argument. It is pertinent to note that the TPO examined and got satisfied with the assessee's profit margin vis-à-vis the comparables only qua the international transactions of manufacturing/distribution functions. He separately determined the ALP of AMP expenses, albeit, without examining the AMP functions carried out by the assessee and the comparables. Manner of determination of the ALP of the distribution activity and AMP activity has been set out by the Hon'ble High Court to be conducted, firstly, in a bundled manner by considering the distribution and AMP functions performed by the assessee as well as the probable comparables. If probable comparables having performed both the functions are not available, then to determine the ALP of AMP expenses in a segregated manner. As such, it becomes immensely important to separately examine the distribution and AMP functions undertaken by the assessee as well as probable comparables. It is vital to highlight the difference between AMP expenses and AMP functions. Whereas AMP functions are the means by which AMP activity is performed, AMP expenses is the amount spent on the performance of such means (functions). To put it simply, an examination of AMP functions carried out by the assessee and the probable comparables is sine qua non in the process of determination of the ALP of the international transaction of AMP spend, either in a segregate or an aggregate

manner. What Their Lordships have held is to bundle the distribution activity with the AMP activity, being two separate but connected international transactions, for the purposes of determination of the ALP of both these international transactions in a combined manner. The argument of the assessee that since the profit margin of the comparables is much less than the assessee and hence no separate addition should be made for AMP functions, if taken to a logical conclusion, will make the AMP spend as a non-international transaction, which, in our considered opinion, is not appropriate in the given facts. Once AMP expense has been held to be an international transaction, it is, but, natural that the functions performed by the assessee under such a transaction need to be compared with similar functions performed by a comparable case. If AMP functions performed by the assessee turn out to be different from those performed by a probable comparable company, then, an adjustment is required to be made so as to bring AMP functions performed by the assessee as well as the comparable, at the same pedestal. If we concur with the contention of the assessee that the addition on account transfer pricing adjustment of AMP expenses be deleted without any examination of the AMP functions carried out by the assessee as well as comparables, this will amount to snatching the tag of international transaction from AMP expenses, which admittedly exists in facts and circumstances of the present case. What Their Lordships in Sony Ericsson (supra) have held is that the distribution activity and AMP expenses are two separate but related international transactions. It is only for the purposes of determining their ALP that these two should be aggregated. The process of such an aggregation does not take away the separate character of the AMP expenses as an international transaction. An analysis and examination of the manufacture/distribution and AMP functions carried out by the assessee must be necessarily done in the first instance, which should be then compared with similar functions performed by some comparables. If the manufacture/distribution and AMP functions performed by the assessee turn out to be different from those performed by probable comparables, then, a suitable adjustment should be made to the profits of the comparable so as to counterbalance the effect of such differences. If however differences exist in such functions, but no adjustment can be made, then, such probable comparable should be dropped from the list of comparables. If, in doing this exercise, there remains no company doing comparable manufacture/distribution and AMP functions, then, both the international transactions are required to be segregated and then examined on individual basis by finding out probable comparables doing such separate functions similarly. For the international transaction of AMP spend, this can be done by, firstly, seeing the AMP functions actually performed by the assessee and then comparing it with the AMP functions performed by a probable comparable. If both are found out to be similar, then the matter ends and a comparable is found and one can go ahead with determining the ALP of such a transaction. If the AMP functions performed by the two entities are found to be different, then adjustment is required to be made in the case of a probable comparable, so as to make it uniform with the assessee. The assessee may have possibly done, say, four different AMP functions as against the probable comparable having done, say, only three. In such a scenario, again the adjustment will be warranted. In another situation, the AMP functions performed by the assessee and probable comparable may be similar but with varying standards, which will also call for an adjustment. Crux of the matter is that the AMP functions performed by the assessee must be similar to those done by the comparables, in the same manner as such functions are compared in any other international transaction. However, in computing ALP of AMP spend, the adjustment or set off, if any, available from the distribution function, should be made. Essence of the judgment in the case of Sony Ericson Mobile (supra) is that the two international transactions of Distribution and AMP should be examined on the

touchstone of transfer pricing provisions, but on an aggregate basis. Determining the ALP of two transactions in an aggregate manner postulates making a comparison of both the functions of manufacture/distribution and AMP carried out by the assessee with the comparables, so that surplus from the manufacture/distribution activity could be adjusted against the deficit, if any, in the AMP activity. The Hon'ble High Court has no where laid down that the AMP functions performed by the assessee should not be compared with those performed by the comparable parties. On the contrary, it turned down the contention raised by the ld. AR urging for not treating AMP as a separate function, which is apparent from the extraction from para 165 of the judgment : `On behalf of the assessee, it was initially argued that the TPO cannot account for or treat AMP as a function. This argument on behalf of the assessee is flawed and fallacious for several reasons. There are inherent flaws in the said argument'. It held vide para 165 of the judgment that : `An external comparable should perform similar AMP functions.' Thus it is manifest that comparison of AMP functions is vital which cannot be dispensed with. The alternative prescription of the judgment is that if ALP of both the transactions of Distribution and AMP cannot be determined in a combined manner, then the ALP of AMP functions should be separately done. The stand of the assessee urging the consideration of profit on an entity level without making comparison of AMP functions done by the assessee as well as the comparable, will render this alternative approach incapable of compliance. Canvassing such a view amounts to treating AMP spend as a non-international transaction, which is patently incapable of acceptance.

16. We summarize the legal position from the judgment in Sony Ericsson (supra) that the distribution and AMP functions are two separate international activities, which need to be compared with uncontrolled transactions. Because of their inter-twinning, it is only for the purposes of determining their ALP that both these transactions can be aggregated in first instance, so that the surplus from one could be adjusted against the deficit from the other in an overall approach. It does not mean that because of aggregation, the AMP expense transaction sheds its character of a separate international transaction and hence the AMP functions should not be matched with the AMP functions carried out by probable comparables. If suitable comparables can be found having performed both distribution and AMP functions, then, their ALP should be determined on aggregate basis. If, however, there is some difference in the distribution or AMP functions performed by the assessee vis-à-vis the probable comparables, then an attempt should first be made to iron out such difference by making a suitable adjustment to the profit margin of comparables. If such an adjustment is not possible, then such probable comparable should be eliminated. If, by making a comparative analysis of the distribution and AMP functions jointly, there remains no comparable case performing such distribution and AMP functions, then, the international transaction of AMP should be segregated and their ALP be determined separately by applying a suitable method. However, in so determining the ALP of such an international transaction of AMP expenses on separate basis, a proper set off, if any, available from the distribution activity, should be allowed.

17. Adverting to the facts of the instant case, we find that the assessee did not separately report the international transaction of AMP expenses. Even under the transfer pricing analysis done by it on entity level, there is no identification of AMP functions, what to talk of comparing such functions with the other comparables in a combined or separate approach. The TPO treated the AMP spend as a separate

international transaction. He segregated routine AMP expenses incurred by the assessee for his business from the non-routine AMP expenses by treating such non-routine AMP expenses leading to the creation of marketing intangible for its AE. Then he applied a mark-up of 11.05% to determine the ALP of this transaction. There is no attempt to find out the mark-up of comparables by analyzing the AMP functions carried out by the assessee vis-à-vis the comparables. To put it straight, neither the assessee nor the TPO have followed the prescription of the judgment in the case of Sony Ericsson (supra) for benchmarking.

18. Further, we note that no detail of the AMP functions performed by the assessee is available on record. Similarly, there is no reference in the order of the TPO to any AMP functions performed by comparables. In fact, no such analysis or comparison has been undertaken by the TPO. The assessee has also failed to draw our attention towards any material divulging the AMP functions performed by the assessee as well as comparables. As such, it is not possible to determine the ALP of AMP expenses at our end, either in a combined or a separate approach.

19. Since the orders of the authorities below are not in conformity with the ratio laid down in Sony Ericsson (supra) as discussed above and further necessary details for doing this exercise at our end are also not available, we set aside the impugned order and send the matter back to the file of the TPO/AO for determining the ALP of the international transaction of AMP spend afresh in accordance with the manner laid down by the Hon'ble High Court in Sony Ericson Mobile (supra).”

42. In our considered opinion the ratio arising out of the above said case law is fully applicable on the facts of the case. Hence, following the aforesaid case law we remit the issue to file of the assessing officer to follow the direction of the ITAT as above and determine the arm length price in this regard. As regards to the other adjustment in this regard being claimed by the assessee, the same are consequential. The AO shall consider the same afresh and decide as per law. The ld. Counsel of the assessee claimed that the TPO should not be given second innings. We find the same is not tenable in light of facts and case laws referred hereinabove.

Apropos disallowance of royalty.

43. On this issue, the assessee has claimed deduction of Rs.6.28 Crores paid as royalty to Diageo North America and service tax thereof Rs.65.05 lakhs. The AO disallowed the same by holding that expenditure was not wholly and exclusively for the purpose of business. While doing so, the AO noted that earlier this royalty was not paid as the AE has waived off the same because of

economic condition of the assessee. But as the sales started improving it had started paying the royalty to the AE we.f. A.Y.2009-10 onwards. That w.e.f. 1st July 2008, royalty percentage was increased from 1% to 5%. Further, the AO had noted that assessee had stated that royalty was paid to Associated Enterprises the benchmarking of payment of royalty transaction has been submitted to the TPO. The TPO after referring to the submission has made no disallowance in respect of benchmarking adopted by the assessee. It was further claimed that royalty is bonafide expenditure which is incurred for using Smirnoff brand i.e. wholly and exclusively for business purpose of the assessee. While considering the objection of the assessee in this regard, the DRP noted that the assessee has not produced royalty agreement. It observed that this issue was also considered in the DRP order for A.Y.2009-10. Referring to the above, the DRP held that the same has to be disallowed u/s.37(1) of the Act. While giving effect to the above DRP direction, as regards the disallowance of royalty expenditure of Rs.6,28,34,827/- which was proposed to be disallowed u/s.37(1) in the draft assessment, the AO held that since this claim has been rejected by the DRP, the AO was making addition of Rs.6,28,34,827/-. In this regard, upon hearing both the Counsel and perusing the records, we find that it is the claim of the assessee that payment of royalty is an international transaction and assessee has submitted the benchmarking report and the Transfer Pricing Officer has not made any adjustment. In this view of the matter, the Transfer Pricing officer has not made any adjustment. Hence, it was not open to the AO to apply the benefit test and make the disallowance u/s.37(1) of the Act, without proper examination of all aspects of the claim. We find that assessee's submission in this regard have not been properly appreciated by the Assessing Officer, hence, in our considered opinion, the aforesaid issue deserves to be remitted to the AO for fresh consideration. We direct accordingly.

44. As regards the claim of Rs.5,01,03,438/- pertaining to A.Y.2009-10, which is now being claimed to be allowable on payment basis u/s.40(a)(ia) of

the Act, we find that the same was disallowed in the earlier year by applying the Section 37(1) of the Act holding the same that it is not for the purpose of the business. Once it was held that the said payment was not allowable for A.Y.2009-10, the same cannot be claimed to be allowable in A.Y.2010-11 on payment basis u/s.40(a)(ia). Hence, this claim of the assessee is not sustainable, hence, we uphold the orders of the authorities below, disallowing the royalty payment of Rs.5,01,03,438/- paid to Diageo North America pertaining to A.Y.2009-10 which has been claimed on payment basis u/s.40(a)(ia) in the present assessment year.

Disallowance of expenses incurred for liason office at Sri Lanka.

45. During the course of assessment proceedings, it was noted that assessee had incurred certain expenses for its liaison office at Sri Lanka. On enquiry as to why the same should not be disallowed under section 37(1) the assessee responded that assessee was earlier receiving some consideration from an independent Co ID Lanka Ltd. for the services rendered by it. However for assessment year 2009-10 and assessment year 2010-11, no income was earned through the liason office.

46. The AO disallowed the same on the ground that assessee had not carried out any business activity in Sri lanka Or received any income from Sri Lanka. The DRP also rejected the objection by the assessee by following its earlier year order.

47. Against this order assessee is in a before us. We have heard both the Council and perused the records. We find that assessee was incurring expenses in respect of liason office expenses at Sri lanka. It is undisputed that during the current year as well as previous year no income was received on account of activities of the liason office. No detail for the activities conducted by the liason office is also on record. In the earlier year also this claim was

rejected. Accordingly, we do not find any infirmity in the order of the assessing officer in this regard.

48. In the result these appeals are partly allowed.

Order has been pronounced in the Court on 19.12.2019.

Sd/-	Sd/-
(PAWAN SINGH)	(SHAMIM YAHYA)
JUDICIAL MEMBER	ACCOUNTANT MEMBER

Mumbai; Dated : 19/12/2019

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent
3. The CIT(A)
4. CIT
5. DR, ITAT, Mumbai
6. Guard File.

BY ORDER,

//True Copy//

(Assistant Registrar)

Karuna, Sr.PS ITAT, Mumbai