IN THE HIGH COURT OF KARNATAKA AT BENGALURU

DATED THIS THE 29TH DAY OF MAY 2018

PRESENT

THE HON'BLE MR. JUSTICE B.S. PATIL

AND

THE HON'BLE MR. JUSTICE S. SUNIL DUTT YADAV

ITA No.65/2018 c/w
ITA Nos.788-790/2017

Between:

M/s. Kaypee Electronics &
Associates Pvt. Ltd.,
302 & 303,
Somapura Industrial
Area 1st Stage, Nidavanda Village,
Somapura Hobli, Nelamangala Taluk,
Bengaluru Rural District - 562 111.
PAN: AACCK 1203 C
(Represented by its Managing Director,
Shri.N.V. Ramana Murthy,
Aged about 52 years,
S/o Sri. Kotilingam Naidu) ... Appellant
(Common)

(By Sri. Shankar.A. & Sri. Chythanya K.K., Advocates)

And:

1. The Deputy Commissioner
of Income Tax, Circle – 4(1)(1),
7th Floor, BMTC Building,
80 Feet Road, Koramangala,
Bengaluru – 560 095.

2. The Assistant Commissioner
of Income Tax, Circle-4(1)(1),
7th Floor, BMTC Building,
80 Feet Road, Koramangala,
Bengaluru-560 095. ...Respondents
(Common)

(By.Sri. Jeevan. J. Neeralgi, Advocate)

* * *

ITA No.65/2018 is filed under Section 260-A of Income Tax Act 1961, arising out of order dated 31.10.2017 passed in Misc. Petition Nos.162, 163 & 164/Bang/2017 (In IT(TP)A Nos.159/Bang/2015, 132/Bang/2016 & 86/Bang/2017), for the Assessment Years 2010-11, 2011-12 & 2012-13, praying to (a) formulate the substantial question of law stated above; (b) allow the appeal and set-aside the impugned order of the Income Tax Appellate Tribunal, Bengaluru 'B' Bench bearing Misc. Petition Nos.162, 163 and 164/Bang/2017 (in IT(TP)A Nos.159/ Bang/2015, 132/Bang/2016 & 86/Bang/2017), dated 31.10.2017 to the extent prejudicial to the interest of the appellant and etc.

ITA Nos.788-790/2017 are filed under Section 260-A of Income Tax Act 1961, arising out of order dated 21.04.2017, passed in IT(TP)A No.159/Bang/2015, for the AY 2010-11, IT(TP)A No.132/Bang/2016 for AY 2011-12 and IT(TP)A No.86/Bang/2017 for the AY 2012-13.

These ITAs having been heard and reserved on 26.04.2018 and coming on for pronouncement of judgment, this day ***S. Sunil Dutt Yadav, J.,*** delivered the following:

<u>J U D G M E N T</u>

ITA Nos.788-790/2017 are preferred by the assessee seeking to set aside the order dated 21.4.2017 passed by the Income Tax Appellate Tribunal (B), Bengaluru in IT (TP) A No.159/Bang/2015, for the Assessment Year 2010-11, IT (TP) A No.132/Bang/2016 for the Assessment Year 2011-12, and IT (TP) A No.86/Bang/2017 for the Assessment Year 2012-13, whereby the Tribunal had dismissed the appeal filed by the assessee challenging the assessment orders for the above mentioned years. On the dismissal of such appeals, present appeals have been filed before this Court.

2. The facts relevant to the dispute are as follows:

The appellant is a company engaged in the business of manufacturing Magnetic based electronic coils, transformers and inductors. It is a subsidiary of M/s. Falco Limited, Hong Kong, and had entered into a technology collaboration agreement dated 29-03-2006 with M/s. Falco Limited which is an associated enterprise (hereinafter referred to as 'AE') for manufacturing electronic components by using technology, enterprise and know how of Falco, marketing, selling the same under the Brand name of Falco, in India and abroad.

3. The assessee was required to pay royalty at 8% to the AE in terms of the agreement and accordingly the assessee had made a payment of royalty of Rs.4,39,93,839/- as per its declaration in Form 3CEB which contains payment of the royalty as above mentioned.

4. The Assessing Officer had referred the matter to the Transfer Pricing Officer (hereinafter referred to as 'TPO' for short) for the purpose of benchmarking the above international transactions who determined the arm's length price in respect of royalty at

Rs.2,75,25,270/-. The TPO opined that payment of Royalty at 8% on sales was not justified as there was no value addition made by the AE.

5. The Assessing Officer passed the draft assessment order under Section 143 sub-clause (3) r/w Section 144C of the Income Tax Act, 1961 (hereinafter referred to as 'Act') vide order dated 28.2.2014 after incorporating the adjustment in terms of Section 92CA of the Act as regards the excess royalty paid by the assesee.

6. Objections were filed by the assessee before Disputes Resolution Panel, who however, confirmed the findings of the TPO, and the assessing officer passed the final assessment order which came to be challenged before the Income Tax Appellate Tribunal, (B) Bench, Bengaluru.

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7. The Tribunal proceeded to dispose of the appeal observing that the only issue that arose for consideration was as to whether the TPO was justified in making the arm's length price adjustment in respect of royalty payment made to M/s.Falco Limited in the given facts of the present case. The Tribunal while rejecting the contention that when TNMM was applied at the entity level there was no necessity for benchmarking in respect of royalty transactions observed that "on mere perusal of order of the LD.TPO its is manifest that the TPO had picked up the transaction royalty alone for the purpose of benchmarking." The Tribunal proceeded to dismiss the appeal while rejecting the ground of the appeal raised by the assessee - company as regards assailing of the addition of arm's length price adjustment on account of royalty payment with respect to the three assessment years in question.

8. The said order of the Tribunal has been challenged in the present appeals. The appeals had been admitted on 10.1.2018 to consider the substantial questions of law formulated in the memorandum of appeal which are as follows:

> *I. Whether, in the facts and in the circumstances of the case, the Tribunal is right is law in upholding adjustment to royalty although such royalty formed part of operating cost under enterprise level TNM method which was accepted?*
>
> *II. Whether, on the facts and in the circumstances of the case, the Tribunal erred in law in failing to follow the decisions of the co-ordinate bench of the same jurisdiction?*
>
> *III. Whether, in the facts and in the circumstances of the case, the Tribunal is right in law in failing to adjudicate various other grounds raised by the Appellant?*

As the questions of law at (I) and (II) are interlinked, the same are considered together.

9. The counsel for the appellant submits that when the appeals were being heard the appellant had contended that the question regarding the necessity of separate benchmarking in respect of royalty payment when the TPO had accepted the TNMM at the entity level was covered by the decision of ***Sony Ericsson Mobile Communications India Pvt. Ltd*** and the decision of the co-ordinate Bench of this court in the case ***Siemens VDO Automotive Ltd. Vs. DCIT*** **(TP) A No.923/B/2012** dated 25-01-2017 had held that as the royalty paid was already forming part of operating cost, there was no necessity of separately bench marking royalty and the same had been reiterated by the Tribunal in ***(2014) 33 ITR (T) 700, (2016) 75 taxmann.com 145,*** which were not referred to by the Tribunal while passing the impugned order.

10. The appellant contends that the Tribunal has disposed of the appeals by recording a finding only as regards the issue of royalty and its adjustment by the TPO under Section 92CA of the Act in respect of the royalty paid to the AE, that there was no occasion to advance arguments as regards the other issues adverted to in their memorandum of appeal filed before the Tribunal as regards ground Nos. C (1 to 3) and D (1 to 3 and 5 to 9) and that the said questions have remained unconsidered which has prejudicially affected the appellant.

11. It is apparent from the impugned order that there is no discussion as regards the applicability or otherwise of the decision of the co-ordinate bench referred to in paras 9.2 and 9.3 of the memorandum of appeal filed herein, while deciding the question of separately bench marking royalty where royalty paid was already a part of the operating cost. Further, there

is strength in the assertion of the appellant as regards non-hearing on the grounds raised in the memorandum of appeal referred to supra at para 7 which is apparent on a bare perusal of the impugned order.

12. In para 14 of the order of the Tribunal, the Tribunal while considering the reduction of expenditure incurred under telecommunication, freight and travelling in foreign currency from export turnover has held the issue in favour of the assessee-company by relying on the decision of the jurisdictional High Court in the case of ***TATA Elxi Limited*** **(349 ITR 98).** In so far as the said point having been held in favour of the assessee the same not being a subject matter of challenge in the present appeal, findings in para 14 of the impugned order remains undisturbed.

13. In view of the discussion made above, the substantial questions of law on which the appeals had been admitted are answered as follows:

(a) <u>Question nos.(I) and (II) :</u>

Suffice it to say that as per the discussions made above, it is apparent that the contentions of the appellant as regards the issue referred to in substantial question of law raised at question No.(I) was decided without discussing the applicability or otherwise of the decision of the Delhi High Court in the case of ***Sony Ericssion Mobile Communications India Pvt. Ltd.*** *Vs.* ***Commissioner of Income Tax,*** and the decision of the Co-ordinate Bench of the Tribunal in the case ***M/s. Siemens VTO Automative Ltd. Vs. Deputy Commissioner of Income Tax.*** In view of the same, while answering the substantial question No.(II) in favour of the assessee, it is opined that there is no necessity to record a finding on the issues raised in substantial question No.(I).

(b) <u>Question no.(III):</u>

The said question is answered in the affirmative in view of the discussion made above.

14. Hence, it is a fit case to be remanded with a direction to decide afresh, on all contentions urged in the memorandum of appeal. The findings of the tribunal recorded are also set aside for consideration afresh.

15. Accordingly, the order of the Tribunal in IT (TP) A No.159/Bang/2015, IT (TP) A No.132/Bang/2016 and IT (TP) A No.86/Bang/2017 are set aside relegating the parties to the Tribunal with a directed to hear the appeals afresh on all grounds urged in the memorandum of appeals raised before the Tribunal subject to observation made in para 13.

16. It is clarified that the observations made while disposing these appeals is for the limited purpose of disposing the appeals and the Tribunal shall decide the appeals uninfluenced by the observations made herein.

17. I.T.A.No.65/2018 has been filed challenging the order of the Income Tax Appellate Tribunal, Bengaluru in Misc. Petition. No.162, 163 & 164/Bang/2017 (In IT (TP) A. Nos.159/Bang/2015, 132/Bang/2016 and 86/Bang/2017) dated 31-10-2017.

18. In view of allowing the appeal in I.T.A. Nos.788-790/2017 whereby the matters in IT (TP) A. No.159, 132 and 136 & 86 (see prayer in I.T.A. Nos.788-790/2017) have been set aside and remanded for fresh consideration, the appeal in I.T.A.No.65/2018 does not survive for consideration and is disposed of as having become redundant.

Sd/-
JUDGE

Sd/-
JUDGE

RS/*
ct:am

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