

**IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD 'A' BENCH, HYDERABAD.**

**BEFORE SHRI RAMA KANTA PANDA, VICE PRESIDENT
AND
SHRI LALIET KUMAR, JUDICIAL MEMBER**

ITA-TP.No.495/Hyd/2022		
Assessment Year: 2018-19		
HM Clause India Private Limited, Medchal District, Telangana. PAN : AACCC0087A	Vs.	DCIT, Circle-2(1), Hyderabad.
(Appellant)		(Respondent)
Assessee by:		Shri P. Chidambaram.
Revenue by:		Mrs. K. Haritha, CIT-DR
Date of hearing:		02.08.2023
Date of pronouncement:		29.08.2023

ORDER

Per Shri Laliet Kumar, J.M.

This appeal is filed by the assessee, feeling aggrieved by the order passed by the Deputy Commissioner of Income Tax, Hyderabad dated 29.07.2022 involving proceedings u/s 143(3) r.w.s. 144C(13) of the Act for the A.Y 2018-19, on the following grounds :

“1.That on the facts and circumstances of the case, the assessment order dated 29 July 2022 passed by the Office of the Deputy Commissioner of Income Tax, Circle 2(1), Hyderabad (herein after referred to as "Learned Assessing Officer" or "Ld. AO") under section 143(3) read with section 144C(3) read with section 144B of the Act is bad in law.

2. That on the facts and circumstances of the case, the Ld.AO/Transfer Pricing Officer ("Ld. TPO") erred in making transfer pricing adjustment with respect to Interest on Delayed Receivables of 38,74,591 to the income of the Appellant without appreciating the facts of the case.

3. That on the facts and circumstances of the case and in law, the Ld. AO/Ld. TPO erred in treating the outstanding receivables as international transaction u/s 92B of the Act.

4. That on the facts and circumstances of the case and in law, the Ld. AO/ Ld. TPO erred in ignoring the fact that the balance of outstanding payable with Associated Enterprises (AE) is more as compared to the outstanding balance of the receivables with AE.

5. That on the facts and circumstances of the case and in law, the Ld. AO/ Ld. TPO erred in not appreciating the fact that the receivables are a result of the business transactions of the Appellant and cannot be segregated from integral part of the operations of the Appellant;

6. That on the facts and circumstances of the case and in law, the Ld. AO/ Ld. TPO having accepted the primary transactions to be at arms length under Transactional Net Margin Method ought not to have separately benchmarked outstanding receivables as it is subsumed in the main transaction.

7. That on the facts and circumstances of the case and in law, the Ld. AO/ Ld. TPO erred in considering the fact that neither the AE charges to Appellant in case of delay in outstanding payables nor the Appellant charges to AE in case of delay of the amount receivable.

8. That on the facts and circumstances of the case and in law, the Ld. AO/ Ld. TPO erred in not considering the fact that the Appellant has not charged interest in respect of belated trade receipts from Non-AE and as such the Appellant adopted a consistent practice of not charging interest for belated trade receivables from AE transaction also.

9. Without prejudice that TNMM is the most appropriate method, the AO ought to have appreciated that internal CUP method is the second most appropriate method.

10. That on the facts and circumstances of the case, the Ld. AO/ Ld. TPO erred in not granting the benefit of working capital adjustment to the Appellant as prescribed under Rule 1013(1)(e) of the Income-tax Rules, 1962 ["the Rules"].

11. That on the facts and circumstances of the case and in law, the Ld. AO/ Ld. TPO erred in not appreciating the fact that charging of notional interest on receivables is equivalent to hypothetical income and not real income;

12. That on the facts and circumstances of the case and in law, the Ld. AO/Ld. TPO erred in considering CUP as the Most Appropriate Method for benchmarking Interest on delayed receivables.

13. Without prejudice to the above, the TPO has incorrectly applied CUP method.

14. That on the facts and circumstances of the case and in law, the Ld. AO/ Ld. TPO erred in making the adjustment on account of interest on receivables computed on ad-hoc basis by applying short term deposit rates of State Bank of India.

15. Without prejudice, that on the facts and circumstances of the case and in law, the LD. AO/ Ld. TPO erred in not adopting the LIBOR based rate, while determining the arm's length price of the interest on delayed receivables.

16. That on the facts and circumstances of the case and in law, the Ld. AO/ Ld. TPO erred in considering a very low credit period of just 30 days instead of considering industry average credit period.”

2. The brief facts of the case are that assessee is a company engaged in the business of purchases and sale of vegetable seeds and research and development and settings. Assessee filed its return of income for A.Y. 2018-19 on 29.11.2018 declaring total income of Rs.16,04,14,750/- under normal provisions and at income of Rs.14,78,03,870/- u/s 115JB of the Income Tax Act, 1961. The case was selected for scrutiny and notice u/s. 143(2) of the Act was issued to the assessee on 22.09.2019 which was duly served upon the assessee. During the year under consideration, the assessee company had entered into international transactions within the meaning of section 92CA of the Act. Thereafter, the case was referred to the Transfer Pricing Officer (TPO) in order to get arm's length price of those transactions determined by the TPO. The TPO vide order u/s 92CA(3) of the Act dt.31.07.2021 proposed an amount of Rs.38,74,591/- in respect of interest on delayed receivables as the transfer pricing adjustment. Accordingly, made adjustment u/s 92CA amounting to Rs.38,74,591/- to be added to the income of the assessee.

2.1. Consequently, a draft assessment order was passed on 24.09.2021 with total income to be assessed u/s 143(3) r.w.s. 144C(1) of the Income Tax Act at Rs.16,48,95,494/-. Thereafter, against the proposed draft order, assessee filed objections before

the DRP – 1, Bengaluru, who vide its order dt.10.06.2022 directed the TPO to adopt SBI short term deposit rates for subject year as ALP interest rate and compute the adjustment. Taking into consideration, the order giving effect dt.07.07.2022, assessment was completed determining the taxable income at Rs.16,48,95,494/-.

3. The solitary issue raised is with respect to trade receivables outstanding by the assessee from its Associated Enterprise (hereinafter referred to as "A.E."). During the year under consideration, as per the Transfer Pricing Officer's order, trade receivables by the assessee from its A.E. works out to Rs.6,19,93,459/-.

4. The Assessing Officer, after affording an opportunity of hearing, has determined the interest on trade receivables u/s 92B(1) of the Act by applying the SBI short-term deposit rates. The relevant finding given in Paras 6.3 to 6.5 which is to the following effect :

“6.3 The next issue arises as to whether it is an international transaction which at all needs to be benchmarked separately. In this regard, attention is drawn to the amendment explanation (1) to Sec. 92B which has been inserted by Finance Act, 2012 with effect from 01.04.2012. As per the amendment the term international transaction includes:

“.....Capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business.....”

6.4 As can be seen from the above amendment, any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business advancement is covered under the definition of international transactions, It may be of relevance to mention that the transfer pricing regulations also require that it is not only the form but the overall arrangement/ substance of the transactions that must be kept in mind. Towards this end, the following provisions from the regulations are produced:

Section 92F(v) of the Income-tax Act states:

"Transaction includes an arrangement; understanding or action in concert, whether or not such arrangement, understanding or action is formal or in writing;"

Similarly, Rule 108(2)1 states:

"The contractual terms (whether or not such terms are formal or in writing) of the transactions which lay down explicitly or implicitly how the responsibilities, risks and benefits are to be divided between the respective parties to the transactions."

6.5 Above provisions read with the well-established doctrine of 'substance over form' (applied by the Courts in numerous judicial decisions) indicate that transfer pricing regulations are to be applied keeping in mind the overall scheme of the taxpayer's business arrangement.

*In **Swadeshi Cotton Mills Co Ltd v CIT (6311R 57)** the Supreme Court held that the mere existence of an agreement between two parties on the supply of goods or services did not mean that the Revenue authority had not discretion in deciding whether the payment had been made wholly and exclusively for the purpose of business. Merely because of the existence of an agreement, the Income-tax Officer is not bound to agree that the payment was made exclusively and wholly for the purpose of the business.*

*In **Madhowji Oharamshi Mfg Co Ltd v CIT (78 ITR 62)**, the Supreme Court held that the appointments of the selling agent and the managing agent and the agreements to pay compensation for termination of their contracts formed a chain of sham or colourable transactions designed to withdraw large sums of tax free money.*

*In **JK Cotton Mfrs Ltd v CIT (101 ITR 221)** it was held that the circumstances indicated that the expenses incurred were not dictated by commercial expediency, but were inspired by profit hunting and tax avoidance motive and hence, could not be allowed as deduction,*

*In **McDowell & Co Ltd v CTO (154 ITR 148)** the Apex Court upheld Revenue's right to disregard a transaction and look at its substance, if it was undertaken as an anti-avoidance tool. The tax consequences of interlocking, interdependent and predetermined transactions were to be judged by reference to its substance. A series of transactions into which steps that had no commercial purpose apart from the avoidance of tax liability had been inserted, had to be ignored."*

5. Feeling aggrieved, the assessee has challenged the draft order dt.24.09.2021 before the Dispute Resolution Panel (DRP) and the DRP had also confirmed the order of TPO and the findings

of DRP was given in Para 2.1.15 to 2.1.16 of the order which is to the following effect :

“2.1.15 The assessee also raised a plea that it has not charged interest from both AEs and non-AEs and hence interest cannot be imputed on the AE transactions. It was also pleaded that the assessee does not pay interest on the advances & trade payables from the AEs. In this regard, it is relevant to note that the assessee failed to submit any information in regard to the non-AE transaction, such as the terms of service and payment, the credit period along with the relevant agreement and documents. Similarly, the assessee has not submitted complete information relating to payables such as date of invoice, credit period, date of payment, period of delay with supporting invoices. Therefore, these pleas are liable to be rejected.

2.1.16 As regards adoption of ALP interest rate, in the facts of the case, we consider that, it is pertinent to look into the opportunity costs i.e., the income that the assessee would have earned, had the assessee received the amounts in time. This has to be determined taking into account the Indian market conditions, the assessee being taken as the tested party. Factoring these aspects, we are of the view, that the 58 short term fixed deposit interest rate may be the appropriate ALP rate to measure the interest compensation in these types of transactions. In this regard, we place reliance on the principle held by the Honourable Bangalore ITAT in the case of Logik Microsystems Erd (ITA No.423/Bang/2019 dated 07.10.2010) (2010-TI I-50-ITAT Bang-TP), under similar factual circumstances, wherein it was observed, "While adopting the Indian rate. it is not proper to rely on PLR of the State Bank of India. This is because if the funds were brought in time and those funds were properly deployed, the assessee company may earn an income at the maximum rate applicable to deposits and not at the rate applicable to loans. We find it appropriate to adopt a reasonable rate that would be available to the assessee on short-term deposits". Accordingly, the TPO is directed to adopt the SBI short term deposit interest rate for the subject year as the ALP interest rate and re-compute the adjustment to be made to the total income. As the SBI short term deposit rate is an index rate adopted under Indian conditions to charge interest it is not an adhoc rate as contended by the assessee. Therefore, we reject the plea of the assessee to adopt LIBOR rate for the purpose of computing interest on outstanding receivables.”

6. Feeling aggrieved with the findings of DRP, the assessee is now in appeal before us.

7. The first contention made by the assessee before us is that the assessee has a trade outstanding payable to its AE to an extent of Rs.21,35,64,228/- which is higher than the trade outstanding receivables from its AE which is to the extent of Rs.6,19,93,459/-. Therefore, no adjustment can be made in the hands of the assessee towards the trade receivables as there is a negative balance.

7.1. The second contention made by the assessee before us is that the lower authorities have applied SBI short term deposit rate for short term fixed deposits' interest to bench mark and compensate the interest to the assessee for the outstanding due. It was submitted that despite the SBI term deposit rate, the Libor + 200 basic points are required to be applied.

8. On the other hand, the ld.DR had submitted that as per the definition of Section 92B of the Act, outstanding trade receivables are considered to be a separate international transaction which is required to be benchmarked. The outstanding payables by the assessee to its A.E. are not the subject matter of the present dispute. It is not relevant for the determination of Arms Length Price (ALP) and therefore, the first contention raised by the assessee has no merit.

9. Further, the ld.DR had submitted that the Tribunal in the case of Satyam Venture Engineering Services Pvt. Ltd. (TS 581 ITAT 2015 (HYD), Apache Footware India Private Limited in ITA 568/Hyd/2022 and M/s. Aurobindo Pharma Limited (ITA No.485/Hyd/2022) has decided the issue by applying the SBI

short term deposit rate, and therefore, the same interest rate on trade receivables is required to be applied.

10. Ld.DR further submitted that recently, the co-ordinate Bench of the Tribunal in the case of Kartar GDC India (P) Ltd., ITA No.484/Hyd/2022 and Imedx Information Services (P) Ltd., ITA 1755/Hyd/2019 has granted Libor 200 + basic points on the trade receivables, therefore, the same principle is required to be applied.

11. We have heard the rival submissions and perused the material available on record. In the decision of Apache (supra), we have held as under :

“9. We have heard the rival submissions and perused the material on record. From the perusal of the order passed by the TPO, it is clear that both the lower authorities have given an elaborate reasoning for coming to the conclusion that the delay in receiving the receivables is an international transaction and is required to be bench marked in accordance with law. We are reproducing hereinbelow the chart filed by the assessee which is to the following effect :

APACHE FOOTWEAR INDIA PVT. LTD / AY 2018-19				
Export Receivables Realisation pattern during				
A.Y. 2018-19				
	<i>Particulars</i>	<i>Total Number of Invoices during the A.Y. 2018-19</i>	<i>Amount Export Invoice value in Rs.</i>	<i>% of invoices realized to total invoices raised during the year</i>
A)	<i>Realised within credit period</i>	3,001	6,48,15,77,864	91.22
B)	<i>Realised beyond credit period of 60 days</i>			
	<i><10 days</i>	241	36,27,20,363	5.10
	<i>10-20 days</i>	204	18,88,04,889	2.66
	<i>20-30 days</i>	45	7,11,80,351	1.00
	<i>30-45 days</i>	--	--	--
	<i>45-60 days</i>	--	--	--
	<i>>=60 days</i>	29	11,63,338	0.02
	<i>Sub total (B)</i>	519	62,38,68,941	
	<i>Total (A) + (B)</i>	3520	7,10,54,46,805	

10. From the perusal of the Chart, it is absolutely clear that there were 519 invoices valued at Rs.62,38,68,941/- for which the payments were due beyond the credit period 60 days. In our view, the

lower authorities have computed the Arm's Length Price and have mentioned that the same being international transaction, the same is required to be bench marked by considering the SBI short term deposit interest rate.

11. The above-said issue of delay in receivables is no more *res integra*. The co-ordinate Bench in the cases relied upon by the Revenue examined the issue and thereafter directed the TPO / Assessing Officer to apply rate of interest of 6% on outstanding receivable at the year end. The assessee had relied upon various judgements. All these judgments have been considered by the co-ordinate Bench and thereafter, the above said direction was issued by the Bench.

12. The reliance of the assessee on the decision of Hon'ble Delhi High Court in the case of *PCIT Vs. Boeing India Pvt. Ltd.*, reported in 2022 (10) TMI 498 is of no use to the assessee as in the said judgement, the Hon'ble Delhi High Court in Para 15 had mentioned that the issue receivable is essentially a question of fact. As mentioned hereinabove, in the present case, there is a delay in receiving the outstanding of Rs.62,38,68,941/- in respect of 519 invoices as mentioned hereinabove and there is no explanation given by the assessee for such a delay in receiving the amount. The very purpose of benchmarking the transaction is to ascertain whether assessee, who is similarly situated, would render the same kind of services at the same or similar price to a third party or not. If we examine the issue in the above-said context, it would be clear that the assessee would charge bank interest or any other interest with a view to compensate itself on account of delay in making the payment. Hence, we do not find any error in the same.

13. The reliance of the assessee in the case of *Betchal India Pvt Ltd (supra)* is also not correct as A.Y. in that case was 2010-11. By the Finance Act, 2012, the Explanation was inserted in Sec.92B of the Act and by virtue of which "payment or deferred payment or receivable or any other debt arising during the course of business" has been considered to be an international transaction which is required to be benchmarked. Following the above said Explanation, the co-ordinate Bench for the subsequent assessment years vide order dt.16.05.2017 in the case of *Betchal India Pvt. Ltd ITA No.6530/Del/2016 (supra)* had decided the issue against the assessee. In view of the above, the decision relied upon by the assessee is of no help to assessee.

14. So far as the argument of the assessee that the assessee is a debt free company and therefore, no borrowed fund was used for making supplies to it's A.E. and therefore, is not liable to be compensated for the delay in receiving the receivable is concerned, the same in our view, suffers from inherent flaw as in the T.P. analysis, the TPO is required to examine whether the assessee had supplied the product / services to it's A.E. at Arm's Length Price or not ? If by providing the services / goods at a discounted rate or permitting the assessee to receive the payment after a long period of 60 days or 90 days, then it will amount to permitting the A.E. to use the working capital of the assessee for the purposes of earning the profit. No prudent business man would venture into this kind of activity and permit a third party to use the working capital of the assessee and earn profit thereon. In the present case, though the assessee was required to maintain the T.P. Study and file the same before the TPO to show that the assessee's transactions with it's A.E.

were at Arms Length however, nothing has been brought to our notice that the assessee has brought any comparable instance. In these circumstances, the TPO had applied the banking rate as applicable to short term loans. In our view, the same is required to be corrected and instead thereof, ALP is to be computed by adding notional interest @ 6% on the receivable. Considering the totality of facts and circumstances, in view of the decisions cited supra and in view of foregoing discussion, we dismiss the appeal of the assessee. Accordingly, the appeal of the assessee is dismissed.”

12. From the reading of our decision, it is clear that whenever there are outstanding trade receivables, the same are required to be benchmarked by applying the SBI Short term deposit interest rate for the subject year to determine the ALP interest rate. In the present case, undoubtedly, the assessee was to receive the amount from its foreign A.E. for the services provided by it in Indian currency. As such, in our view, the view taken by us, is in accordance with law laid down by the Hon'ble Delhi High Court in the case of Cotton Natural Vs. CIT (supra). Further, assessee was to receive the amount from its A.E for the services rendered to its AE which was withheld by its AE. In the absence of the availability of due amount, the assessee was required to approach to the banks in India for the purposes of raising the funds necessary for carrying out its day-to-day activities in the form of short term bank loan. If the assessee had received the amount within the stipulated time, then the said outstanding amount would have been available for operations of the assessee, however, keeping that issue in mind, assuming the assessee has approached the bank for the purpose of making arrangements for some advances, the assessee would be required to pay interest to the said bank.

13. On the contrary, if the assessee has a surplus amount, then the assessee may deposit the said amount with the bank and would earn interest as applicable to the short-term deposit. In view of the above, we do not find any reason to deviate from our view taken in the case of Apache (supra). With respect to the other decision relied upon by the Id.AR for the assessee, it is interesting to note that in the said decision, the co-ordinate Bench of the Tribunal came to the conclusion that Libor + 200 points are required to be applied on the interest received on advances, and that decision was made in the case of foreign currency. However, the point remains that our decision in the case referred to herein was not brought to the attention of the co-ordinate Bench of the Tribunal while passing the said decision.

14. Further, it is relevant to mention that LIBOR (London Interest Bank Rate) is applicable in the case of lending by one bank to the other. However, in the case of assessee like before us, which is doing a business for earning the profit cannot be equated with the bank loan taken by the bank from another bank. In the case of Enterprise, which is rendering the services or manufacturing or supplying the products, there are lot of factors which are materially different than lending of money. Further, if one person is manufacturing, rendering services, then the same cannot be equated by with the lending money business. Prices, remuneration and risk for money lending and the other manufacturing and trading activities, are entirely different.

15. Further, in the present case, the assessee has supplied the services to its AE and the AE is due to make the payment for the services / goods received by it to the assessee. Assuming, the assessee gives the same kind of services to the third party, then the assessee would charge interest from the third party. Moreover, if the advances were given by a person, then the prices of the product would be less as the assessee would have availability of funds at disposal for the purpose of carrying out its activities. Because of withholding of funds in case of outstanding receivables, there would be deficit of funds and would be required to borrow the funds to carry out day-to-day activities, albeit those funds would be available to the assessee at the prevailing rate of interest in India. Hence, the SBI short term rate would be the appropriate rate for the purpose of determining the ALP on the outstanding amount. Now, in light of the above, we do not find any reason to take a contrary view as we have taken in the case of Apachi Footware India Private Limited (supra).

16. During the course of arguments, it was submitted that the Assessing Officer has not been given any grace period for making the payment. However, we notice that on page 7 of the Assessing Officer's order, it is mentioned that the assessee has failed to provide any service agreement / invoice to the Assessing Officer. Therefore, in the absence of any such contemporaneous evidence showing the grace period, the Assessing Officer has granted 30 days. In our view, the normal trend to be followed is 30 days. However, in the case of Apache Apache Footware India Private Limited (supra), based on the agreement, we have accepted it to

60 days. In the present case, there was no agreement provided by the assessee to show that there was an agreement between the assessee and its AE wherein the time for making the payment was provided as 30 days. In our view, the Assessing Officer is right for granting 30 days as a grace period and beyond that the Assessing Officer / lower authorities have held that the assessee is liable to pay the interest as outstanding amount for the said period. In the light of the above, we do not find any reasons to interfere with the order of TPO. Thus, the appeal of the assessee is dismissed.

16. In the result, the appeal of the assessee is dismissed.

Order pronounced in the Open Court on 29th August, 2023

Sd/- (RAMA KANTA PANDA) ACCOUNTANT MEMBER	Sd/- (LALIET KUMAR) JUDICIAL MEMBER
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Hyderabad, dated 29th August, 2023

TYNM / SPS

Copy to:

S.No	Addresses
1	HM Clause India Private Limited, 6-98/4, Survey No.563/Part, Gowdavelli Village, Medchal Mandal, Medchal District, Telangana.
2	Deputy Commissioner of Income Tax, Circle – 2(1), Hyderabad.
3	Dispute Resolution Panel (DRP), Bengaluru
4	Director of Income Tax (IT & TP), Hyderabad
5	Addl. Commissioner of Income Tax (Transfer Pricing), Hyderabad.
6	DR, ITAT Hyderabad Benches
7	Guard File

By Order