* IN THE HIGH COURT OF DELHI AT NEW DELHI

\+ **ITA No.1341 of 2010**
ITA No.703 of 2011
ITA No.705 of 2011

Reserved on: 16th August, 2011
% Pronounced on: 30th September, 2011

DIRECTOR OF INCOME TAX . . . APPELLANT

Through: Mr. Abhishek Maratha, Sr. Standing Counsel.

VERSUS

BBC WORLDWISE LTD. . . .RESPONDENT

Through: Mr. Saubhagya Aggarwal, Advocate.

CORAM :-
HON'BLE MR. JUSTICE A.K. SIKRI
HON'BLE MR. JUSTICE M.L. MEHTA

1. Whether Reporters of Local newspapers may be allowed to see the Judgment?
2. To be referred to the Reporter or not?
3. Whether the Judgment should be reported in the Digest?

A.K. SIKRI, J.

1. In these three appeals common issue is raised in respect of the same assessee, pertaining to three assessment years. The proposed question of law is as under:

> "Whether the ITAT was justified in the eyes of law in holding that no further income is required to be attributable to the assessee herein as the transaction was at arm's length price, when the mandatory FAR

> analysis in the case of the assessee herein has never been conducted for any assessment year to determine the arm's length price, as provided by Article 7 of the Indo-UK DTA; ratio of judgment in the case of Morgan Stanley; Rule 10B sub-rule – 2 of the Income Tax Rules, 1962 and Section 92C of the Income Tax Act, 1961?"

2. Before we advert to the aforesaid issue, we deem it apposite to take note of some relevant facts. The assessee is a non-resident. It is a company incorporated under the laws of England and Wales and is a part of BBC Group. This BBC group has a company incorporated in India as well, known as M/s. BBC Worldwide India Pvt. Ltd. (hereafter referred to as 'the BWIPL').

3. During the year under consideration, BWIPL was operating as international consumer media company in the areas of television, publishing and programme (for short 'the channel'), which is a standard international channel aired in the English language, operated by the assessee through a separate division, i.e., BBC World Division. The assessee appointed BWIPL as its authorized agent in India under an airtime sales agreement dated 19.9.2000, effective from 13.11.1998, for dollar denominated deals, to solicit orders for the sale of advertising airtime on the channel at the rates and on the terms and conditions provide by the assessee

and to pass on such orders to the assessee for acceptance and confirmation. The payments form the Indian advertisers for airtime sales and sponsorship was to be received directly by the assessee under this agreement, through EEFC account or specific RBI permission. In consideration for the services provided by BWIPL, it was to receive a 15% marketing commission of the advertisement revenues received by the assessee from Indian advertisers. A second airtime sales agreement dated 01.2.1999 was entered into between the assessee and BWIPL for rupee denominated deals for soliciting orders for channel airtime sales, as under the first agreement. The second agreement was executed so as to enable BWIPL to collect payments from Indian advertisers on sales of airtime on behalf of the assessee and remit the same to the assessee, after deducting its commission @ 15%.

4. While filing its return of income for the year under consideration, it declared NIL income. The assessee claimed that it would not be taxable in India on its airtime sales income, being business profits, in the absence of a permanent establishment in India. Later, the return of income was revised so as to disclose an income of

₹81,86,735/-, i.e., royalty income which had inadvertently not been shown in the original return. Other than the said royalty income, the assessee stated, it did not have any income chargeable to tax in India.

5. The Assessing Officer (AO), however, was not enthused with the aforesaid plea taken by the assessee that no income was chargeable to tax in India. He arrived at the conclusion that the primary activity of the assessee in India was that of sale of airtime for the channel. Thus, it was clear that the assessee company was carrying out the activity of airtime sale in India and the assessee had a clear and definite business connection in India inasmuch as there was a real and intimate relation between the business activities carried on outside India and the activity of soliciting, sourcing and collecting advertisement revenues from India that the advertisement revenue received in India in respect of BBC World Channel was a business receipt in the hands of the assessee that BWIPL was acting as an agent of the assessee that BWIPL was acting as an agent of the assessee company and was rendering all services on behalf of the assessee company. BWIPL, i.e., the Indian company prepared the rate-cards, collected the advertisements and advertisement

revenue for onward remittance to the U.K. after deducting its commission and all these functions were undertaken by BWIPL in India on behalf of the assessee company and the advertisement revenues collected from India were remitted to the assessee company. The AO, therefore, held that the income of the assessee company from the advertisement revenues accrued or arose in India under Section 9(1) of the Income Tax Act (hereinafter referred to as 'the Act'). It was held that BWIPL constituted a business connection of the assessee as well as a permanent establishment under Article 5(4)(a) and Article 5(4)(c) of the Double Taxation Avoidance Agreement ('DTAA' for brevity) between India and U.K. The profits of the assessee were estimated at an *ad hoc* rate of 20% of the total advertisement revenue attributed to India.

6. The CIT (A) agreed with the findings of the AO and affirmed the same while dismissing the appeal of the assessee.

7. In further appeal before the Income Tax Appellate Tribunal ('the Tribunal' for brevity), the assessee though still maintained that it had no business connection or permanent establishment in India, without prejudice to this contention, the assessee came out with an alternative plea that in any case, the assessee's Indian agent, i.e., BWIPL was

remunerated on an Arm's Length business and, therefore, nothing remains to be taxed in India. For this argument, the assessee took the plea that the Department had itself, after examining the airtime sales agreement, which were effective till November, 2002 accepted that the commission of 15% to BWIPL was a fair transfer price for the airtime sales activity which the taxing authorities have alleged to constitute a permanent establishment of the assessee in India. The assessee referred to the Transfer Pricing order passed by the Transfer Pricing Officer (TPO) in respect of BWIPL for the Assessment Year 2002-03 and pointed out in the case of BWIPL, the same very commission paid by the BWIPL was accepted at Arm's Length Price (ALP) and that it constituted it were transferred price. The assessee also referred to the judgment of Bombay High Court in the case of ***SET Satellite (Singapore) Pvt. Ltd. Vs. DDIT***, 307 ITR 205 (Bom.) holding that the payment of service fee @ 15% of the gross advertisement revenue to its agent represented the price computed on the ALP principle. The judgment of this Court in the case of ***DIT Vs. Galileo International Incorporation***, 114 TTJ 289 (Del) was also referred. It was submitted that in ***Galileo International Incorporation***

(supra), this Court had referred to the CBDT's Circular No.742 dated 02.5.1996 wherein it was recognised that the advertising agent of the foreign telecasting companies in India usually retains service charges @ 15% or so of the gross amount and this Circular had been taken note of in ***DIT Vs. Morgan Stanley and Company Inc.***, 292 ITR 416 (SC).

8. These submissions of the assessee convinced the Tribunal. The Tribunal did not go into the issue of business connection or permanent establishment, which was not addressed before it and confined itself to the issue as to whether the BWIPL had been adequately remunerated on the basis of Transfer Pricing. There is no dispute that if answer to this is in affirmative, then no further income of the assessee is taxable in India. The Tribunal held that once the T.P.O. had himself accepted that commission of 15% paid to BWIPL is a fair transfer price and on the basis of this opinion of the TPO, income declared by the BWIPL for its Assessment Year 2002-03 was accepted by the Department, the Department could not contend otherwise. Referring to the order of the TPO, the Tribunal has noted the following features therein:

"In that order, the TPO accepted that the transaction was at arms length price. It was held that the CUP method selected by BWIPL for determining the arms length price of the commission income earned by it, was acceptable; that this was due to the fact that BWIPL with that charged by an uncontrolled party for similar services; that even otherwise, it was found that the rate of commission in the assessee's trade was fairly uniform and almost everyone was charging the same rate fairly uniform and almost everyone was charging the same rate of commission in the sale of airtime on TV Channels and FM Channels; and that it was therefore, that the arm's length price determined by BWIPL was not being disturbed."

9. Apart from taking support from the judgment of ***SET Satellite (Singapore) Pvt. Ltd. (supra)*** and the judgment of this Court in ***Galileo International Incorporation (supra)***, the Tribunal also discussed two CBDT's Circulars, on the subject, and interpreted the same in the following manner:

"17. CBDT Circular No.23 of 1969 (supra) is eloquently clear, providing that if the value of the profit attributable to the services rendered by the agent is fully represented by the commission paid, it should be, prima facie extinguish the assessment. "DIT v. Morgan Stanley and Company Inc. (supra", a stated, has taken into consideration CBDT Circular No.23 of 1969 (supra). In that case, since certain employees have been deputed by the foreign company to the Indian affiliate company, the foreign company was held to have a permanent establishment in India. The AAR held that once the Transfer Pricing Analysis was undertaken, there was no further requirement to attribute profits to a permanent establishment. Adjudicating on the issue as to whether the action of the AAR in holding so was correct or no, the Hon'ble Supreme Court held, inter alia, that where the transaction was held to be at arms length, the ruling of the AAR was correct in principle, provided that an associated enterprise, which also constituted a permanent establishment, was remunerated on arm's

length basis, taking into account all the risks-taking functions of multinational enterprises and that in such a case, nothing further would be left to attribute to the permanent establishment.

18. As contended, for the year under consideration, Transfer Pricing guidelines were not applicable. That being so, reliance on behalf of the assessee on "SET Satellite" (supra) cannot at all be said to be misplaced. Therein also, the assessment year being 1999-2000, the Transfer Pricing guidelines were not applicable, as they became applicable from the next year. Pertinently, the Hon'ble Bombay High Court, in the case of "SET Satellite" (supra) as well as CBDT Circular No.23 (supra) was taken into consideration. The facts in the present case are found to be parity with those present in "SET Satellite" (supra), to the extent noticed above. Both the cases concern years before the onset of the Transfer Pricing regime. As such, we hold that "SET Satellite" (supra) has rightly been relied on behalf of the assessee and that it is directly applicable to the assessee's case.

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21. So far as regards the Department's assettiont hat CBDT Circular No.742 (supra) has wrongly been relied on, it is seen that CBDT Circular No.765 dated 15.04.1998 extended Circular No.742 (supra). As per CBDT circular No.742, it was needed to be established, for the applicability of the Circular, that the assessee or a non-resident foreign telecasting company and that it did not have a branch office or a permanent establishment or did not maintain country wise accounts of its operations. The Circular would not apply in the event of any of the said conditions being not satisfied. All the conditions are not to be cumulatively satisfied so as to apply the Circular. In the assessee's case, the assessee had filed before the AO its country accounts for India, wherein the total revenues and expenses of the assessee were allocated to its India activity. A copy thereof has been placed before us. Before the CIT (A), the assessee also filed its audited accounts containing allocation of revenues and expenses to it India activity. A copy thereof has also been furnished before us. The learned CIT (A)

remanded these to the AO. Therefore, evidently, CBDT Circular No.742 (supra) does not apply."

10. Impugning the aforesaid order of the Tribunal in the instant appeal, arguments raised by the Department, predicated on the proposed issue is that the Tribunal was not justified in relying upon the order of the TPO in the case of BWIPL when no such exercise was done in the case of the assessee. It was argued that as per the provisions of Section 92C of the Act, it was mandatory to undertake FAR analysis in the case of assessee, which is provided in Article 7 of the Indo-UK, DTAA as well and for want of such an exercise, reliance upon the TPO order made in the case of BWIPL was totally extraneous.

11. Dialing this argument, submission of Mr. Abhishek Maratha, learned counsel appearing for the Revenue, was that Section 92C(1) of the Act relates to adoption of the most appropriate method having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe. The CBDT has prescribed the relevant conditions in Rule 10B of the Act. The various methods are prescribed in Sub-rule (1) of Rule 10B. He

further submitted that it is pertinent to mention that Rule 10B, Sub-rule (2) of the Income Tax Rules, 1962 deals with the manner of computation of ALP and the aspects connected therewith. It reads as under:

> "2) For the purposes of sub-rule (1), the comparability of an international transaction with an uncontrolled transaction shall be judged with reference to the following, namely:—
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> (*a*) the specific characteristics of the property transferred or services provided in either transaction;
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> (*b*) the functions performed, taking into account assets employed or to be employed and the risks assumed, by the respective parties to the transactions;
>
> (*c*) 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;
>
> (*d*) conditions prevailing in the markets in which the respective parties to the transactions operate, including the geographical location and size of the markets, the laws and Government orders in force, costs of labour and capital in the markets, overall economic development and level of competition and whether the markets are wholesale or retail."

12. Concluded his arguments, the learned counsel summed up his submission that:

A. FAR Analysis is mandatory to be conducted in every assessment year to determine the income of a non-resident;

B. The issue concerning the determination of the ALP has been raised by the assessee before the Tribunal for the first time;

C. The Tribunal cannot do the FAR Analysis or substitute FAR Analysis of the Permanent Establishment for it, when it has not been done by the AO or TPO;

D. Article 7 of the Indo-UK DTAAA also provides that the FAR Analysis is to be conducted for determining the assessable income of the non-resident;

E. No FAR Analysis has been done by the AO at any point in time for any assessment year in the case of the assessee herein;

F. CBDT Circular No.742 dated 02-05-1996 is applicable to the facts of the instant case, as the assessee is not maintaining any country wise accounts;

G. Ratio of the decision in the case of ***Morgan Stanley (supra)*** has been done in the case of the assessee herein;

H. When no FAR Analysis has been done in the case of the assessee, then to reach the conclusion that nothing more is attributable to the assessee is absolutely baseless and illegal;

I. The FAR Analysis in the case of BWIPL has resulted in the additional income of ₹3.60 Crores; and

J. If the FAR Analysis is done in the case of the assessee, then it would reveal its real character as to its ALP.

13. Learned counsel for the respondent/assessee refuted the aforesaid submissions. He submitted that reliance upon the FAR Analysis done by the TPO in the case of BWIPL was most relevant, as it is this very commission which was paid by the assessee to BWIPL and once it is treated as ALP in the case of BWIPL, that would be the most material and direct evidence in the case of assessee as well. It was argued that the transfer pricing provisions were introduced in the Act vide Finance Act, 2002 from Assessment Year 2002-03, providing that any income arising from an

international transaction shall be computed having regard to the ALP. For computing the ALP, a contemporaneous documents including the FAR and economic analysis would be required to be maintained in certain cases as prescribed. Therefore, for the first two years in appeal, i.e., assessment year 2000-01 and 2001-02, neither the assessee nor its Indian agent (BWIPL) was required to undertake a FAR Analysis under the prevailing provisions of law (pre-transfer pricing regime). For the Assessment Year 2002-03 (the first year under new transfer pricing provisions), the FAR Analysis was prepared and submitted by the BWIPL, *inter alia*, in respect of its functions performed in India for the assessee. BWIPL was paid a commission of 15% on the gross sales, for soliciting advertisement and marketing advertisements and sponsorships. BWIPL's case for the Assessment Year 2002-03 was also assessed by the TPO under Section 92CA(3) of the Act and the FAR Analysis for this transaction was recorded and the remuneration was held to be at an ALP. He further submitted that a transfer pricing reference was also made under Section 92CA of the Act in the assessee's own case for the Assessment Year 2002-03 and it was held

by the TPO that no adverse inference/addition could be drawn.

14. He also submitted that in ITA No.705/2011 for the Assessment Year 2003-04, the assessee had duly submitted the accountant's report under Form 3CEB in relation to its international transactions, in compliance with the transfer pricing regulations. It is also relevant to note that a transfer pricing reference was made under Section 92CA of the Act in the assessee's case for the Assessment Year 2003-04 and no addition was made by the TPO.

15. After considering the respect arguments, we are of the opinion that no substantial question of law arises in the instant cases as we do not find any justification in interfering with the impugned order of the Tribunal. Following pertinent aspects which emboldened stand out and stare at the face of the Department and shut its case completely:

    (i) The provisions of transfer pricing was introduced for Finance Act, 2002 from the Assessment Year 2002-03 and therefore, in respect of two appeal for the Assessment Years 2000-01 and 2001-02, no such FAR Analysis was even required.

(ii) For the Assessment Year 2002-03, FAR Analysis was prepared and submitted by the assessee's agent BWIPL. BWIPL had submitted that it had received commission @ 15% on the gross sale from the assessee for selling marketing advertisement and sponsorship and as per BWIPL, it was a reasonable commission paid on arm's length basis. Matter was referred to TPO under Section 92CA (3) of the Act, who clearly opined that the aforesaid commission paid to BWIPL was ALP. Once it is treated as ALP at the hands of recipient, we fail to understand how a different view can be taken in the case of assessee who had paid the same commission to its agent. Therefore, we fail to appreciate the contention of the Department that the FAR Analysis by the TPO in the case of BWIPL was not relevant.

(iii) Moreover, in the assessee's own case for the Assessment Year 2002-03, transfer pricing reference was made to the TPO under Section 92CA (3) and TPO had opined that no adverse

inference/addition could be drawn. Learned counsel for the assessee produced the order dated 31.12.2004 passed by the TPO, in this behalf, *inter alia*, stated as under:

> "A reference under Section 92CA was received in the case of BWIPL from its assessing officer. All the above mentioned international transactions have been examined at length in the order under section 92CA (3) dated 31st March, 2004, subsequently rectified vide order under section 154 dated 30th November, 2004 in the case of BWIPL for the assessment year 2002-03. In that order, no adverse inference was drawn in respect of the arm's length price of all the international transactions as declared by the assessee except the transaction for availing market services. The arm's length price for the international transaction for availing market support services was determined at Rs.10,90,52,410/- instead of an amount of Rs.7,44,30,694/- as declared by the assessee. However, since this adjustment would have the effect of reducing the income chargeable to tax or increase in the loss, as the case may be, in the case of assessee the provisions of section 92 shall not apply in this case i.e. the effect of the adjustment made in the arm's length price of the transaction availing marketing support services by the assessee shall be ignored while computing the income of the assessee."

(iv) Even if the next Assessment Year, i.e., 2003-04, the assessee had submitted the account's report in relation to its international transactions. For

this year also, reference was made to TPO, which again passed the orders dated 07.3.2006, once again opining that no adverse inference could be drawn in respect of ALP. Following portion of the said order is worthwhile to quote:

> "A reference under Section 92CA was received in the case of BWIPL from its assessing officer. All the above mentioned international transactions have been examined at length in the order under section 92CA(3) dated 09.01.2006. In that order Arm's Length Price of international transaction mentioned above has been revised upward but there is no reciprocal effect in the case of assessee in view of provisions of sub-section 3 of Section 92 of Income Tax Act.
>
> Hence no adverse inference is drawn in respect of arm's length price of the above mentioned transaction in the hands of assessee company."

(v) We do not find any merit in the plea of the Department that country-wise accounts have not been made by the assessee and therefore, the deemed rate of taxation at 10% of advertisement revenue as per Circular No.742 dated 02.5.1996 issued by the CBDT, should be applied to tax the revenue of the Permanent Establishment of the assessee. In this regard, we note that in the

course of assessment proceedings, the assessee had prepared its country accounts for India, allocating total revenues and expenses of the assessee to India activity and filed the same before the AO. This fact has been recorded by the Tribunal in its order in Assessment Year 2000-01. In the light of this observation, Circular No.742 is not applicable in the instant appeal.

16. When the aforesaid factual position is kept in mind, the judgment of the Bombay High Court in ***Set Satellite (Singapore) Pvt. Ltd. (supra)*** is clearly attracted. In that case the High Court has held that if correct ALP is applied and paid, nothing further rwould be left to be taxed in the hands of the foreign enterprise. In the said case, ***Morgan Stanley (supra)*** as well as Circular No.23 issued by the CBDT was taken into consideration. The Court was also pleased to record that the commission paid to the agent was 15% services performed by the assessee's agent in India was in line with the existing industry standards in India at the prevalent time. Reliance was also placed on Para 3 of

Circular No.742 dated 02.5.1996 issued by the CBDT, which referred to the fact that the agent's commission from foreign telecasting companies is 15% or so of the gross sum, to contend that the CBDT itself had considered 15% as the normally accepted commission rate payable to agents of the telecasting companies.

17. We are, thus, of the opinion that no question of law arises. These appeals are accordingly dismissed.

(A.K. SIKRI)
JUDGE

(M.L. MEHTA)
JUDGE

SEPTEMBER 30, 2011
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