Legal Decisions

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Transfer Pricing

LD/65/58

Vishnu Eatables (India) Limited
vs.
DCIT, Karnal
3rd October, 2016

AO is required to provide opportunity of being heard to the assessee regarding whether a transaction is an international transaction or not, and serve a reasoned order upon the assessee; HC rejected assessee's contention that TPO-reference is void ab initio on account of AO's failure to furnish the satisfaction note to assessee before making a reference to TPO; Failure to supply satisfaction is 'at the highest a mere irregularity and does not prejudice the assessee in any manner whatsoever'.

The Assessee sought a writ of *certiorari* to quash the reference made by AO to TPO and to quash the satisfaction recorded by AO for making such reference, on the ground that Chapter X [Transfer pricing provisions] provisions were not applicable to the transactions undertaken by the assessee since they were not with its 'associated enterprises'. The assessee argued that the entire proceedings, including the reference to the TPO, for AY 11-12 were without jurisdiction and void.

By notice dated 19.03.2016, the AO called upon the assessee to show cause why its cases for AYs 2011-12 to 2014-15 not be transferred to the TPO, and granted the assessee a hearing. During the course of survey on assessee's premises, various incriminating documents were found. The show cause notice stated that assessee had made sales to its group companies M/s Haryana Trading Company, Dubai managed by one Kushal Mittal and M/s Indian Treat Pvt. Ltd. Singapore managed by one Sunny Mittal; that the sales to the sister concern were under-invoiced with a view to evading tax and that profits from India were diverted to tax havens which were remitted back to India for investing in properties by said Kushal Mittal and his family members. Further, the Accountant's report u/s. 92E in Form No. 3CEB was also not furnished by the assessee.

The assessee, by submission dated 21.30.2016 filed its objections stating that there were no international transaction or specified domestic transaction undertaken by it during the AYs 2008-09 to 2014-15 with an associate enterprise and accordingly it was not required to submit Form No.3CEB. The assessee also requested for a copy of the reference by AO to TPO and a personal hearing.

The AO stated that the provisions of Section 92A were applicable to the case and the case required a reference to the TPO for ALP determination. Even the Pr. CIT approved the reference made by AO to TPO. Aggrieved, assessee filed the present writ petition before Punjab & Haryana HC.

Before HC, the assessee made two submissions

I) In terms of the instructions given by the CBDT circular dated 10.03.2016, the requirement of passing a reasoned order on the objections regarding whether a transaction is an international transaction or not and the service of the order upon the assessee is a condition precedent to the Assessing Officer making a reference to the Transfer Pricing Officer.

II) Non-compliance with either or both the above mandatory conditions render the reference to the Transfer Pricing Officer void.

HC remarked that the first submission was well founded but the second was not.

W.r.t. passing of a 'reasoned order' by AO before making reference to TPO

HC observed that it is necessary for the Assessing Officer to decide the objections, if any, to the applicability of Chapter-X before referring the transactions to the TPO as also before determining the arm's length price himself. HC referred to Bombay HC decision in Vodafone India Service wherein it was held that where a reference is made under section 92CA(1), TPO must determine ALP of the transaction and in doing so he would not be entitled to consider the question as to whether the transaction referred to him is an international transaction or not. Thus where AO himself determines ALP, the assessee would be entitled to question whether the transactions are international transactions or not, and would also be entitled to challenge the same before CIT(A) & then ITAT. However, in a case where AO refers ALP determination to the TPO without affording the assessee an opportunity of being heard and without deciding the objections as to whether the transaction is an international transaction or not, then the assessee would be severely prejudiced since he would then not have had an opportunity of having this objection even considered. This is because once the reference is made u/s. 92A(1), the TPO cannot for reasons stated in the second Vodafone's judgment [2013] 359 ITR 133 (*supra*)] consider the question as to whether the transaction referred to him is an international transaction or not.

This in turn would affect the assessment proceedings itself for the Assessing Officer would also be deprived the opportunity of arriving at a informed decision as to whether the transaction that he *prima-facie* considered to be an international transaction is or is not in fact an international transaction. The first opportunity that the assessee would in such a case have to raise a contention that the transaction is not an international transaction would be before the Disputes Resolution Panel (DRP) or the CIT(A) as the case may be. These are in effect appellate proceedings where the appellate or the higher authority CIT(A)/DRP would have to consider the issue with the benefit of the case of the department as well as of the assessee for the first time. Indeed, even the Revenue would come to know of the assessee's objections and the material in support thereof for the first time. This may in a given case result in the CIT(A) or the ITAT remanding the matter resulting in multiplicity of proceedings.

HC observed that in respect of international transactions, an assessee must maintain certain information as per Section 92D and rule 10D, and report the same as per Section 92E and Rule 10E. Failure to follow these sections results in far reaching consequences upon the assessee. Therefore the assessee is substantially affected by the finding as to whether or not a transaction entered into by it is an international transaction. It is only fair then that an assessee is given an opportunity of being heard on the question as to whether a transaction entered into by it is an international transaction or not.

The HC therefore stated that the opportunity of raising objections and being heard on this issue ought to be granted by the Pr.CIT since it is the Pr. CIT who ultimately grants or refuses the approval to refer the transaction to TPO for ALP determination. However, if an assessee is given such an opportunity before the Assessing Officer, that would be sufficient, since AO would undoubtedly have to forward the same alongwith the objections, if any, to the Pr.CIT while seeking his approval.

HC observed that the assessee's case fell within paragraph 3.3 (c) and the first subparagraph after the opening part of paragraph 3.4 CBDT circular dated 10.03.2016 containing guidelines for implementation of TP provisions, which relate to search and seizure operation at the assessee's premises and non-filing of accountant's report u/s 92E respectively. HC rejected Revenue's contention that in cases relating to search and seizure operations, it was not necessary for AO to pass a speaking/reasoned order.

HC stated that Para 3.3(c) cannot be read in isolation and must read with Para 4. HC observed that it was clear that satisfaction is to be in writing and AO must furnish reasons for the same, which requirements had been complied with by AO. In the instant case, the satisfaction recorded by AO contained sufficient reasons, as he had indicated the relationship between the assessee and the other parties and made a comparative chart and alleged that the sales were under-invoiced, which was sufficient to refer the matter to TPO. HC remarked that "Whether the allegations are true or not must be tested before the authorities under the Act and not in a Writ Petition under Article 226. The challenge on this ground is, therefore, unsustainable."

W.r.t. serving of order recording satisfaction upon the assessee?

HC observed that the order recording satisfaction upon which the Pr.CIT grants his permission must be served upon the assessee. The purpose of this exercise of granting the assessee an opportunity of raising objections and being heard and the requirement of the Assessing Officer to furnish reasons for the satisfaction for the reference of the transaction to the TPO for determination of the arm's length price is *inter-alia* to enable the assessee firstly to meet the case and represent against it to the TPO before the Assessing Officer on the ground that there is no international transaction and secondly in the event of his objections being overruled, an opportunity of challenging the same before the Disputes Resolution Panel or the CIT(A) as the case may be, and thereafter before the ITAT.

Assessee contended that the satisfaction that was recorded by AO was not served upon the assessee, and therefore the reference was void and consequently all the proceedings before TPO were void. HC rejected this submission. HC observed that if assessee's objections are overruled, it is open for him to challenge the same before CIT(A) / DRP, and the assessee is not entitled as a matter of right to invoke the writ jurisdiction at the stage of reference by the AO to TPO.

The Assessee's grievances can be raised in a challenge to the draft assessment order before the Disputes Resolution Panel or the final assessment order before to the Commissioner of Income Tax (Appeals). The requirements of the rules of natural justice and of the said circular dated 10.03.2016 would have been met, even if the satisfaction note is furnished subsequently. In any event, the assessee cannot raise the question as to whether or not the referred transaction is an international transaction before the Transfer Pricing Officer. It is, therefore, sufficient if he is served with the order subsequently even alongwith the draft assessment order or the assessment order as the case may be. However, if satisfaction note is not furnished at all, then the assessee can always apply for the same either before the authorities and failing which by filing a writ petition.

HC observed that *"The failure to supply the satisfaction note before the reference to the TPO is at the highest a mere irregularity and does not prejudice the assessee in any manner whatsoever."* HC stated that if this contention was accepted, it would lead to the startling result of the entire assessment proceedings being annulled on account thereof, and there was nothing in the Act or in the circular that warrants such an interpretation.

Accordingly, HC dismissed the writ petition, and stated that as reference to the TPO had already been made after obtaining the approval of the Pr. CIT, the assessee's objection may be taken before the DRP/ CIT(A). HC added that *"it is only fair that if the petitioner chooses the DRP route or the CIT(A) route, the DRP or the CIT(A) as the case may be ought to first adjudicate the question as to whether the said transactions are international transactions or not. If they come to the conclusion that they are not international transactions, certain consequences may follow which we keep open for the petitioner to take before the DRP or the CIT(A) as the case may be".* HC clarified that in the event of CIT(A)/ DRP coming to the conclusion that they are international transactions, it would not be necessary for them to stall the proceedings and they may proceed to decide them finally.

Observing that penalty proceedings u/s 271(G) were initiated for violation of provisions of Chapter-X, HC stated that since the assessee did not have an opportunity of representing its case to the effect that these transactions were not international transactions, it was only fair then that while the penalty proceedings may continue the order imposing penalty, if any, shall not be implemented till the decision of the DRP or the CIT(A) as the case may be, on the preliminary issue as to whether it is an international transaction or not. ■