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AMP exp. incurred on brand promotion of foreign AE would attract TP provisions

Summary – The Delhi ITAT in a recent case of Yum Restaurants (India) (P.) Ltd., (the Assessee) held that where incurring of AMP expenses by assessee towards promotion of brand legally owned by foreign AE constituted a transaction, transfer pricing adjustment in relation to such AMP expenses was sustainable in principle

Where there was functional dissimilarity between assessee and one company, same was to be excluded from list of comparables during transfer pricing study of assessee

Facts - I

- The assessee operated company-owned KFC outlets in India. Certain international transactions were reported which were referred by the Assessing Officer to the Transfer Pricing Officer (TPO).
- The TPO held that the AMP expenses incurred by the assessee were a mere brand building exercise done for the benefit of the AE, which ought to have been reimbursed with necessary mark-up. He therefore, reduced reimbursement and by adding mark-up of 9.98 per cent, he proposed TP adjustment on that account.
- On appeal, the DRP held that no interference was warranted in respect of the TP adjustment.
- On second appeal:

Held - I

- It is noticed that the Special Bench of the Tribunal in *L.G. Electronics India (P.) Ltd.* v. *Asstt. CIT* [2013] 140 ITD 41/29 taxmann.com 300 (Delhi), by majority decision, has *inter alia* held that incurring of AMP expenses towards promotion of brand, legally owned by the foreign AE, constitutes a 'transaction'. The contention that no disallowance could be made out of AMP expenses by benchmarking them separately when the overall net profit rate declared by the assessee was higher than other comparable cases, also came to be specifically rejected by the Special Bench. Resultantly, the transfer pricing adjustment in relation to such AMP expenses was held to be sustainable in principle. It can be seen that the TPO did not have the benefit of the Special Bench order in the case of *L.G. Electronics India (P.) Ltd.* (*supra*) and the DRP failed to apply it correctly to the facts of the case, by making sweeping observations generally without considering the effect of relevant factors laid down by the Special Bench. In such circumstances, the ends of justice would meet adequately if the impugned order on this issue is set aside and the matter is restored to the file of the Assessing Officer/TPO for a fresh determination of disallowance, if any, on account of Transfer pricing adjustment for AMP expenses in the light of the decision of the Special Bench in the case of *L.G. Electronics India (P.) Ltd.* (*supra*).

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Facts - II

- The assessee benchmarked segment of 'support services' provided outside India by applying Transactional Net Margin Method (TNMM) with Profit level indicator (PLI) of OP/TC.
- The TPO, *inter alia,* held that one company MFMC was not to be considered as a comparable company, and with remaining companies, the TPO determined their average OP/TC and that led to TP adjustment.
- The DRP upheld action of the TPO.
- On second appeal:

Held – II

- The only issue raised by the assessee was against the exclusion of company MFMC.
- It is found from the details filed by the assessee before the authorities below that said company is a HR services company. As against this, the assessee under this segment is engaged in providing liaison services, market development and ongoing support to the licencees outside India, as is evident from service agreement. Obviously, the nautre of services provided by the assessee to its AEs is no match with those provided by MFMC. When this fact was confronted to the assessee, he also candidly admitted the functional dissimilarity, however, maintaining that it should nevertheless be directed to be included. The rationale of this contention cannot be appreciated for the apparent reason that unless a company passes the test of functional comparability in the first instance, it cannot be taken up for further comparison. Under these circumstances, it is held that the authorities below were justified in not including this company in the list of comparables, though on a different reason.

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