

ITAT removes effect of cost reimbursed from AE as comparable wasn't getting any reimbursement for its services

Summary – The Delhi ITAT in a recent case of Seagram Manufacturing (P.) Ltd., (the Assessee) held that where assessee incurred expenses for rendering for marketing support services to its AE and it was reimbursed by its AE but comparables selected by assessee were not reimbursed for certain specific functions carried out by them, in order to bring tested party and comparables at level playing field, it became necessary that reimbursed cost should be considered in cost base as well as part of income so as to neutralize any variation in cost incurred by assessee towards carrying out marketing support services

Facts

- The assessee-company was engaged in the business of blending, bottling and trading of Indian made foreign liquor (IMFL). In order to promote duty free sales of these international brands in India, assessee provided need based marketing support services to its parent company in Hongkong (Seagram). Seagram reimbursed the actual marketing cost incurred by assessee for performing the above services and paid the fixed commission of US \$ 2500 per month to assessee.
- Assessee claimed that its market support services function was within +/- 5 per cent of the average of NCPs of comparable cases.
- The TPO noticed that the reimbursed expenses were routed through assessee's accounts and were mentioned as part of 'international transaction of market support services'. However, while preparing the segmented accounts, these reimbursements were excluded both from the receipts and the expenditure. For NCP Ratio calculation also, reimbursed expenses were not included in the 'cost'. He had observed that when assessee which incurred expenses in the first place and recorded them in its books, there could be no justification in excluding them from 'total cost' for calculating NCP ratio. He concluded that reimbursed expenses should be taken as a part of 'cost' to be used for calculating NCP ratio. He, accordingly, calculated the NCP ratio for the marketing support services and he made addition.
- Commissioner (Appeals) had partly allowed the assessee's appeal.

Held

- The short point for consideration, after elaborate consideration of facts, is whether the cost reimbursed to assessee by its AEs was to be included in the cost base for determining the NCP of assessee or not. The claim of assessee is that assessee was getting advances from its AEs for performing certain functions on behalf of AEs only. These functions included organization of various functions such as Golf Championship, Polo Championship sponsored by AEs. The marketing support services implies that assessee is providing support services for building up the market for its AEs. It

cannot be disputed that had this activity been performed by an independent entity, it would have been compensated not only towards the cost incurred by it but also a mark up on the same would have been realized. As regards the comparables selected by assessee and accepted by TPO, which were performing Marketing support services, there was nothing on record to suggest that all such comparables were also being reimbursed for certain specific functions carried out by them. Under such circumstances, in order to bring the tested party and comparables at level playing field, it become necessary that reimbursed cost should be considered in the cost base as well as part of income so as to neutralize any variation in the cost incurred by assessee towards carrying out marketing support services. Admittedly, at first place assessee has incurred all these expenses and then got reimbursed by its AEs. All risks incidental to these expenses were at assessee's account and not AE. Commissioner (Appeals) has very rightly excluded any allocation towards finance charges because assessee had received advance from its AEs. Both employees co-ordinated with various agencies which were to conduct or organize these events. He has observed that research was also conducted on behalf of Seagram, findings for which were communicated to Seagram. It would suffice to observe that assessee played a vital role in all the activities done to promote sales of Seagram in India and the meager amount of US \$ 2500 per month was not at all justified considering the services rendered by assessee. One could appreciate assessee's contention of not including the reimbursement of expenses as part of the cost base if income of Marketing Support Services did not include these reimbursements but that is not so. TPO has included the same.