IN THE INCOME TAX APPELLATE TRIBUNAL
(DELHI BENCH 'A' : NEW DELHI)

(THROUGH VIDEO CONFERENE)

SHRI N.K. BILLAIYA, ACCOUNTANT MEMBER
and
BEFORE SHRI KULDIP SINGH, JUDICIAL MEMBER

ITA No.375/Del./2016
(ASSESSMENT YEAR : 2006-07)

M/s. Honda Cars India Ltd., A – 1, Sector 40/41, Surajpur-Kasna Raod, Greater Noida (Uttar Pradesh).	vs.	DCIT, LTU, New Delhi.

(PAN : AAACH1765Q)

(APPELLANT) (RESPONDENT)

ASSESSEE BY : Shri Deepak Chopra, Advocate
Shri Amit Srivastava, Advocate
Shri Ankul Goyal, Advocate
REVENUE BY : Shri Sanjay Goel, CIT DR

Date of Hearing : 09.07.2020
Date of Order : 17.07.2020

O R D E R

PER KULDIP SINGH, JUDICIAL MEMBER :

Appellant, M/s. Honda Cars India Limited (hereinafter referred to as 'the assessee') by filing the present appeal sought to set aside the impugned order dated 06.11.2015 passed by the Commissioner of Income-tax (Appeals)-22, New Delhi in an appeal challenging the orders passed by the ld. TPO/AO qua the assessment year 2006-07 on the grounds inter alia that :-

"1. That the order passed by the Commissioner of Income Tax (appeals) [CIT(A)] to the extent prejudicial to the appellant, is bad in law and against the settled principles of law.

2 That the CIT(A) erred in upholding the validity of the re-assessment proceedings under Section 147 of the Act when initiation of proceedings did not satisfy necessary requisites contained in Section 147 of the Act and there being no reason to believe that any income chargeable to tax had escaped assessment.

2.1 That the reassessment proceeding was initiated beyond four years and in the absence of any allegation of the appellant not disclosing truly and fully material facts, reassessment were barred by limitation.

2.2 That the CIT(A) erred in sustaining the validity of reassessment proceedings in the absence of any reason to believe that any income of the appellant chargeable to tax has escaped assessment.

2.3 That the CIT(A) erred in sustaining the reassessment proceedings when the same were barred by limitation under the proviso to section 147 of the Act.

2.4 That the CIT(A) erred in sustaining the reassessment proceedings while not appreciating that the sole basis for initiating such proceedings was on account of reliance placed on the statements of expatriate employees of the appellant which were not admissible and could not form the basis of initiating such proceedings.

WITHOUT PREJUDICE

3. That the AO/CIT(A) erred in making/sustaining an addition of Rs.13,09,82,982 under section 40(a)(i) of the Act while holding that Appellant was required to deduct tax at source of payments made for purchase of raw materials, components etc. from non-residents.

4. That the AO/CIT(A) erred in making/sustaining the addition under section 40(a)(i) of the Act while holding that the provisions of chapter XVIIB of the Act were applicable on such payments.

5 That the AO/CIT(A) erred in law in concluding that there existed a Permanent Establishment (PE)/business connection of Honda Motors, Japan [HMJ] and Honda Trading Asia Co. Ltd. [HTAS], being non-resident companies from whom the Appellant had purchased raw materials, components etc.

5.1 That the CIT(A) erred in following the order of the Hon'ble Dispute Resolution Panel ('DRP') in coming to the conclusion that expatriate employees working in the Appellant company were

working on behalf of the HMJ and as such controlled the day-to-day functioning of the Appellant in terms of technology, economic and other control.

5.2 That the CIT(A) grossly erred in law and facts in accepting the DRP direction that the HTAS has a business connection and PE in India, basis the alleged facts and relationship of the Appellant and HMJ.

5.3 That the CIT(A) erred in following the order of the Hon'ble Dispute Resolution Panel ('DRP') in concluding that the expatriate employees of HMJ constituted a PE of HTAS in India given complete absence of any expatriate employee of the HTAS in the Appellant company.

5.4 That the CIT(A) erred in following the order of the Hon'ble Dispute Resolution Panel CDRP') in coming to the conclusion that the Appellant is dependent upon HTAS for employees, technology and economically when no employee has been seconded by the HTAS to Appellant, no technology has been provided by the HTAS to Appellant and Appellant has no economic dependence on HTAS.

6 That the AO/CIT(A) grossly erred in law in relying on statements of expatriate employees recorded during the course of survey proceedings on the Appellant, such statements having been selectively reproduced and relied upon by the lower authorities.

7 That the AO/CIT(A) erred in not correctly appreciating that in view of the non-discrimination clause Article24(3) of the Indo-Japan Double Tax Treaty] no disallowance could be made in the hands of the Appellant owing to non-deduction of tax on purchase of raw materials, components etc.

8 That the AO/CIT(A) grossly erred in not appreciating that all transactions between the Appellant and the non-resident associated enterprises (AE's) had been determined at arm's length basis and in view of the Article 9 of the Double Tax Treaties, no further income could be attributed to the AE.

9 Without prejudice to the above grounds, that on the facts and circumstances of the case and in law, the CIT(A) has erred in following the order of the Hon'ble Dispute Resolution Panel ('DRP') in attributing 25% of the total income to the activities of the AE's in India alleging that selling of raw material, consumable spare parts, etc. has been carried in India when none of the selling operation is carried in India.

10 Without prejudice to the above grounds, that the CIT(A) has grossly erred in law and facts in applying the adjusted global profit ratio of the AE's as considered by the Hon'ble DRP after making disallowance of research and development (R&O).

10.1 That on the facts and circumstances of the case and in law, the CIT(A) has erred in accepting increase in the global operating profit ratio by 5.34% (on the basis of global accounts) stating that R&D expense does not relate to HMJ's PE in India.

10.2 That on the facts and circumstances of the case and in law, the CIT(A) has erred in accepting increase in the global operating profit ratio by 5.34% (on the basis of global accounts) when there is no R&D expense incurred by the HTAS.

11 Without prejudice to the above grounds, that the CIT(A) grossly erred in law and facts in rejecting the attribution study filed by the AE's before the Hon'ble DRP.

12 That the CIT(A) grossly erred in law in confirming the applicability of the provisions of section 40(a)(i) of the Act on reimbursements of Rs. 95,75,221 which did not have any element of income embedded in the same.

13 That without prejudice the provisions of section 40(a)(i) of the Act could have been applied on to the amounts which remained payable at the end of the year and could not be applied to all the transactions conducted during the period under consideration.

14 That the CIT(A) grossly erred in remanding the issue relating to allowability of TDS credit in the absence of any power of remand whereas the CIT(A) should have verified and allowed the claim himself.

15 That the AO has grossly erred in law and facts in charging interest under sections 2348, 234C and 234D of the Act.

16 That the AO has erred in law in initiating penalty proceedings under section 271(1)(c) of the Act against the appellant."

2. Briefly stated the facts necessary for adjudication of the issue at hand are : M/s. Honda Cars India Limited (formerly known as Honda Siel Cars India Limited) (hereinafter referred to as 'the assessee') is a subsidiary of M/s. Honda Motor Company Limited, Japan is into the business of manufacture and sale of premium segment passenger cars in India and outside India. During the year under assessment, initially assessment was completed under

section 143(3) of the Income-tax Act, 1961 (for short 'the Act') on 23.12.2009 at an income of Rs.377,06,86,160/- by way of making various additions on account of model fees, royalty, provision of warranty, export commission and air-fare under the technical guidance fee. Thereafter, ld. CIT (A) decided the appeal filed by the assessee and computed the income at Rs.228,76,75,607/- and the appeal filed by the Department stood dismissed and cross objections filed by the assessee were allowed vide order dated 22.07.2011.

3. However, subsequently a survey was conducted by Income-tax Officer, International Taxation, Noida on 24.06.2010 and 19.12.2012 and during the survey proceedings, statements of the employees and expatriates recorded and intimation obtained during the survey proceedings that the non-resident parent company and other affiliate companies had a business connection and a Permanent Establishment (PE) in India as per the provisions of section 9(1)(i) of the Act and relevant tax treaties. It was also noticed from Form No.3CEB report that assessee had made various payments totaling Rs.1057,30,04,248/- to the Associate Enterprise (AE) during the Financial Year (FY) 2005-06 relevant to Assessment Year (AY) 2006-07. Detail of such payment is extracted as under :-

S. No.	Payment made to	Nature of payment as per 3CEB	Amount
1	Honda Motor, Japan	Purchase of raw materials	3,83,29,63,108
2	Honda Trading, Japan	Purchase of raw materials	4,81,26,038
3	Asian Honda, Thailand	Purchase of raw materials	2,95,98,64,281
4	Honda Cars, Philippines	Purchase of raw materials	2,18,87,798
5	Honda Automobiles, Thailand	Purchase of raw materials	2,01,65,969
6	American Honda, America	Purchase of raw materials	2,92,62,299
7	PT Honda, Indonesia	Purchase of raw materials	3,34,83,053
8	Honda Auto Parts, Malaysia	Purchase of raw materials	2,07,17,351
9	Honda Trading, Thailand	Purchase of raw materials	1,10,77,314
10	Honda Access, Thailand	Purchase of raw materials	59,44,576
11	Honda SDN, Malaysia	Purchase of raw materials	94,26,344
12	Honda Parts Manufacturing Corpn., Philippines	Purchase of raw materials	4,66,236
13	Honda Trading, America	Purchase of raw materials	18,53,115
14	Honda Access, Thailand	Purchase of spare parts	54,153
15	Honda Trading, Japan	Purchase of spare parts	10,34,930
16	Honda Motor, Japan	Purchase of spare parts	17,18,38,883
17	Asian Honda, Thailand	Purchase of spare parts	10,99,46,498
18	Honda Motor, Japan	Purchase of cars	98,28,95,774
19	Honda Automobiles, Thailand	Purchase of capital goods	45,07,836
20	Honda Trading, Thailand	Purchase of capital goods	2,01,057,857
21	Honda Trading, Japan	Purchase of capital goods	48,22,78,936
22	Honda Motor, Japan	Purchase of capital goods	3,48,49,947
23	Honda Motor, Japan	Payment of technical know-how	61,20,05,000
24	Honda Motor, Japan	Payment of Royalty	81,71,60,464
25	Honda Motor, Japan	Payment of technical services	13,71,60,464
26	Honda Trading, Japan	Payment of technical services	83,74,855
27	Honda Trading, Thailand	Payment of technical services	1,61,785
28	Honda Motor, Japan	Payment of export commission	3,72,207
29	Honda Motor, Japan	Reimbursement of misc. expenses	45,19,714
30	Asian Honda, Thailand	Reimbursement of misc. expenses	32,34,687
31	Honda Auto Parts, Malaysia	Reimbursement of misc. expenses	1,71,750
32	Honda Automobiles, Thailand	Reimbursement of misc. expenses	53,45,204
33	Honda Trading, Japan	Reimbursement of misc. expenses	8,21,076
		Total	1057,30,04,248

4. AO further proceeded to conclude that recipient companies had a business connection and a PE in India and the assessee

company is liable to deduct tax on these payments u/s 195 of the Act which the assessee company had failed to deduct and consequently, provisions contained u/s 40(a)(i) of the Act are attracted and the amount of Rs.1057,30,04,248/- was liable to be disallowed u/s 40(a)(i) of the Act. AO finding these reasons sufficient to believe that due to the failure on the part of the assessee to disclose all material facts truly and fully, income of Rs.1057,30,04,248/- had escaped assessment and consequently initiated the proceedings u/s 147 of the Act.

5. AO noticed that the assessee has made payments to various non-resident companies without deduction of tax u/s 195 of the Act, detailed as under :-

S. No.	*Payment made to*	*Nature of payment as per 3CEB*	*Amount (in Rs.)*
1	*Honda Motor Co. Ltd., Japan*	*Purchase of raw materials*	*5,86,07,09,109*
		Purchase of spare parts	*23,32,089*
2	*Asian Honda Motor Co. Ltd.*	*Purchase of raw materials*	*628,97,48,438*
		Purchase of spare parts	*4,87,681*
3	*Honda Trading (Thailand) Co. Ltd.*	*Purchase of raw materials*	*7,04,84,068*
		Purchase of consumables	*39,25,351*
4	*Honda Trading Corporation*	*Purchase of consumables*	*36,37,335*
		Purchase of raw materials	*2,02,25,846*
		Purchase of spare parts	*79,88,490*
5	*Honda Automobile (Thailand) Co. Ltd.*	*Purchase of raw materials*	*63,14,799*
6	*Honda Access Asia & Oceania Co. Ltd.*	*Purchase of raw materials*	*4,55,03,300*
		Purchase of spare parts	*1,07,383*
7	*Honda Cars Philippines Inc.*	*Purchase of spare parts*	*17,295*
8	*Honda Parts Manufacturing Corp.*	*Purchase of raw materials*	*1,93,771*
		Purchase of spare parts	*22,901*
9	*American Honda Motor Co., Inc.*	*Purchase of raw materials*	*77,60,284*
10	*Honda Trading Asia Co. Ltd*	*Purchase of raw materials*	*35,71,68,651*
		Purchase of spare parts	*90,47,457*
11	*Honda Malaysia Sdn Bhd, Malaysia*	*Purchase of raw materials*	*53,223*
12	*Honda Trading (South*	*Purchase of raw materials*	*21,68,55,944*

	China) Co. Ltd.		
13	*Honda Autoparts Manufacturing (M) Sdn. Bhd*	*Purchase of raw materials*	*31,162*
	Total		*1290,26,14,576*
14	*Honda Motor Co. Ltd., Japan*	*Purchase of Cars (CRV)*	*44,33,42,920*
	Total		*44,33,42,920*
15	*Honda Motor Co. Ltd., Japan*	*Purchase of fixed assets*	*21,82,996*
16	*Honda Trading Corp.*	*Purchase of fixed assets*	*2,79,19,292*
17	*Honda Trading (Thailand) Co. Ltd.*	*Purchase of fixed assets*	*1,37,56,478*
18	*Honda Trading Asia Co. Ltd*	*Purchase of fixed assets*	*22,16,405*
	Total		*4,60,75,172*
19	*Honda Motor Co. Ltd., Japan*	*Royalty Payment*	*159,74,53,887*
	Total		*159,74,53,887*
20	*Honda Motor Cor. Ltd., Japan*	*Technical Guidance Fees*	*7,87,76,635*
21	*Honda Trading Co.*	*Technical Guidance Fees*	*6,47,341*
22	*Honda Trading Asia Co. Ltd.*	*Technical Guidance Fees*	*3,97,27,101*
	Total		*11,91,51,077*
23	*Honda Motor Co. Ltd.*	*Expenses Reimbursed (Paid)/Payable)*	*7,93,41,475*
24	*Honda Automobile (Thailand) Co. Ltd.*	*Expenses Reimbursed (Paid)/Payable)*	*1,45,84,939*
25	*Asian Hodna Motors Co. Ltd.*	*Expenses Reimbursed (Paid)/Payable)*	*2,31,56,315*
26	*Honda R & D Co. Ltd.*	*Expenses Reimbursed (Paid)/Payable)*	*12,28,414*
27	*Honda R&D Asia Pacific Co. Ltd.*	*Expenses Reimbursed (Paid)/Payable)*	*2,81,042*
28	*Asian Honda Motor Co. Ltd.*	*Interest on delayed payment*	*3,10,96,574*
	Total		*14,96,88,760*
	Grand Total		*1525,83,26,392*

6. Consequently, AO assessed the total income u/s 143 (3)/147 of the Act at Rs.12,86,00,74,220/- on account of disallowance u/s 40(a)(i) of the Act.

7. Assessee carried the matter by way of an appeal before the ld. CIT (A) who has sustained the addition of Rs.13,09,82,982/- made u/s 40(a)(i) of the Act by partly allowing the appeal. Feeling

aggrieved, the assessee has come up before the Tribunal by way of filing the present appeal.

8. We have heard the ld. Authorized Representatives of the parties to the appeal, gone through the documents relied upon and orders passed by the revenue authorities below in the light of the facts and circumstances of the case.

GROUNDS NO.1 & 2

9. Grounds No.1 & 2 are dismissed having become infructuous as the reassessment proceedings have been quashed by the ***Hon'ble Supreme Court in the case of Assistant Director of Income-tax, Noida vs. Honda Motors Co. Ltd., Japan in case cited as (2019) 108 taxmann.com 300 (SC)***, copy available at page 17 of the synopsis.

GROUNDS NO.4 to 7 & 9 to 15

10. Grounds No.4 to 7 & 9 to 15 have been dismissed having not been pressed during the course of arguments by the ld. Counsel for the assessee.

GROUNDS NO.3 & 8

11. Undisputedly, when arm's length principle has been followed, there cannot be further profit attributable to a person even if it has PE in India as has been held by Hon'ble Supreme Court in case cited as ***Assistant Director of Income-tax, Noida vs.***

Honda Motors Co. Ltd., Japan in case cited as (2019) 108 taxmann.com 300 (SC), operative part thereof is as under :-

> ***"Section 92, read with section 147, of the Income-tax Act, 1971 – Transfer Pricing – General (Scope of Provision) – Whether once arm's length principle has been followed, there can be no further profit attributable to a person even if it has permanent establishment in India – Held, yes."***

11.1 In the instant case, vide ***order dated 30.09.2009 passed by the Transfer Pricing Officer, Kanpur in case of assessee for AY 2006-07,*** it has been held that transaction of sale and purchase transaction of spare parts, raw material, capital goods and export commission of the assessee with its AE (including Honda Motor, Japan) are at arm's length. This factual position has not been controverted by the ld. CIT DR for the Revenue.

12. Ld. AR for the assessee further contended that the issue in controversy is covered by the order passed by the coordinate Bench of the Tribunal in ***assessee's own case for AYs 2009-10 &2010-11 reported in (2016) 72 taxmann.com 253 (Delhi-Trib) & order dated 18.08.2017 in ITA No.s.4491/Del/2014 7 5483/Del/2014, copy available at pages 76 to 96 & 97 to 140 of the paper book respectively***.

13. We have perused the orders passed by the coordinate Bench of the Tribunal in ***assessee's own case in AY 2010-11 decided vide***

order dated 18.08.2017 (supra) wherein the identical issue has been determined in favour of the assessee by following the order passed in assessee's own case for AY 2009-10 (supra) by returning following findings :-

> ***"12. We have heard the rival submission and perused the relevant material on record. We find that the Assessing Officer made disallowance in terms of section 40(a)(i) of the Act amounting to Rs.1525,83,26,392/-for non-deduction of tax on payments made to HMJ and other AEs under section 195 of the Act holding that such amounts were chargeable to tax in the hands of HMJ /AEs as these entities had permanent establishment and business connection in India. The CIT(A) allowed part relief & the assessee is in appeal on disallowance u/s 40(a)(i) for payments made to two entities only i.e. HMCJ and AH, Thailand.***
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> ***13. It is pertinent to mention here that the issue in dispute has been adjudicated by the coordinate bench of this Tribunal in assessee's own case for assessment year 2009-10 in ITA No. 2056 and 3229/Del/2014. The disallowance under section 40(a)(i) in assessment year 2009-10 has been deleted by the Tribunal in paras13 to 20 of the order. The Tribunal held that in case of Asia Honda Thailand, the dispute resolution panel (DRP) held that the non-resident company had no PE in India and accordingly, the Tribunal reversed the finding of the Ld. CIT-(A)that Asia Honda Thailand had a PE in India, and held that section 195 and consequently 40(a)(i) were not applicable related to the payment to Asia Honda Thailand. Regarding the payment to Honda Motor Co. Ltd Japan, the Tribunal observed that this issue of PE was not adjudicated by the Assessing Officer of that company and therefore disallowance u/s 40(a)(i) of the Act was adjudicated by the ITAT invoking nondiscrimination clause of the DTAA. The Tribunal deleted the disallowance related to payment to Honda Motor Japan applying the proposition of law laid down by the Hon'ble Delhi High Court in the case of CIT Vs. Herbalife International India Private Limited (supra) regarding interpretation of the nondiscretionary article in the Double Taxation Avoidance Agreement(DTAA)between India and Japan. The relevant finding of the Tribunal is reproduced as under:***
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> > ***"13. We have heard the rival contentions. On a careful consideration of the facts and circumstances of the case and perusal of the papers on record and the orders of the authorities below, as well as the case law cited, we hold as***

follows. The sole issue for our consideration is whether the disallowance made u/s 40(a)(i) of the Act read with section 195of the Act, of payments made to non-resident companies is correct in law.

13.1. There is no dispute of the fact that out of 18 non-resident associate companies to whom payments have been made, it was held that 16 associated enterprises do not have a P.E. in India. The D.R.P. in the case of Asia Honda Thailand for the A.Y. 2009-10 has held that the Non-resident company had no P.E. in India. Revenue has not filed an appeal on this finding of the D.R.P. Hence we have to reverse the finding of the Ld.CIT(A) that Asia Honda Thailand has a P.E. in India in this A.Y. Thus we have to hold that, except in the case of Honda Motors Japan, payments made to all other 17 non-resident associate companies do not attract the provisions of S.195 and consequently 40(a)(i) of the Act, as no portion of the income of these companies arising from the supply of parts etc. was liable for tax in India.

14. This leaves us with the issue of applicability of the provisions of S.195 r.w.s. 40(a)(i) to Honda Motor Company Ltd.

15. The issue whether Honda Motor Company Ltd. has a PE in India or not should be preferably adjudicated by the AO in the assessment of that company. It is not advisable to determine this issue in collateral proceedings, as is in the case of the assessee. Thus, we adjudicate the issue by considering the arguments of the assessee without prejudice, invoking the non-discrimination clause in terms of Article 24(3)of the DTAA, between India and Japan. The AO in this case has denied the benefit of the non-discrimination clause to the assessee by holding that the provisions of the Income-tax Act are different from the provisions of the DTAA and hence no benefit could be given to the assessee. When the matter came up before the ld.CIT(A), he held that the term used in Article 24(3)related only to royalties, fee for technical services, interest and the term 'other disbursements' necessarily related to payments in the same generic and thus the payments for purchases are not covered by Article 24(3)and hence the benefit of DTAA cannot be given.

16. We find that this issue is no more res integra. The jurisdictional High Court in the case of CIT vs. Herbalife International India Pvt. Ltd., judgment dated 13th May, 2016, has, after considering the argument of the intervener, Mitsubishi Corporation, and the provisions of the Indo-Japanese DTAA has on the issue of 'other disbursements' in para 38 to 42, held as follows:-

> *''38. The question that next arises is whether the payment by the Assessee to HIAI qualifies as 'other disbursements' for the purpose of Article 26 (3)DTAA?*

39. To recapitulate, the case of the Revenue is that the expression 'other disbursements' should take colour from the context and would apply only to income which is of passive character just like interest and royalties. The Revenue invokes the doctrines of 'noscitur-a-sociis' and 'ejusdem generis'. It is submitted that FTS does not qualify as 'other disbursements' since it is not a passive character like royalties and interest.

40. The Court is unable to agree with the above submissions of the Revenue. In the context of which the expression 'other disbursement' occurs in Article 26 (3), it connotes something other than 'interest and royalties'. If the intention was that 'other disbursements' should also be in the nature of interest and royalties then the word 'other' should have been followed by 'such' or 'such like'. There is no warrant, therefore, to proceed on the basis that the expression 'other disbursements' should take the colour of 'interest and royalties'.

41. The expression 'other disbursements' occurring in Article 26 (3)of the DTAA is wide enough to encompass the administrative fee paid by the Assessee to HIAI which the Revenue has chosen to characterize as FTS within the meaning of Explanation 2 to Section 9(1) (vii) of the Act.

42. At one stage of the proceedings, the Assessee sought to contend that the payment was FIS covered under Article 12 (4)of the DTAA. The ITAT did not address this issue. It addressed the question whether, even assuming it was FIS, Section 40(a) (i) of the Act cannot be applied and consequently, no disallowance can be made. Before this Court no question has been framed at the instance of the Assessee that the payment is covered byArticle12 (4)of the DTAA. Consequently, this question is not examined by the Court.

17. Thus, the findings of the ld.CIT(A) on this issue have to be necessarily reversed. Coming to the findings of the AO, we find that the Hon'ble High Court vide paras 46 to 62 of the order in the case of Herbalife International India (supra) has dealt with the issue as under, and when the proposition laid down in this judgement is applied to

the facts of this case, the finding of the A.O. has to be reversed.

> ***"46.Section 40is in the nature of a non-obstante provision and therefore, it overrides the other provisions as contained in Sections 30to38of the Act. This means that the expenditure which is allowable under Sections 30to38of the Act in computing business income would be subject to deductibility condition in Section 40of the Act. The payment of FTS to HIAI would be allowable in terms of Section 37(1) of the Act but before such payment can be allowed the condition imposed in Section 40(a) (i) of the Act regarding deduction of TDS has to be complied with. In other words if no TDS is deducted from the payment of FTS made to HIAI by the Assessee, then in terms of Section 40(a) (i) of the Act, it will not be allowed as a deduction under Section 37(1) of the Act for computing the Assessee's income chargeable under the head 'profits and gains of business'.***
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> ***47. Article 26(3)of the DTAA calls for an enquiry into whether the above condition imposed as far as the payment made to HIAI, i.e., payment made to anon-resident, is any different as far as allowability of such payment as a deduction when it is made to a resident.***
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> ***48. Section 40(a) (i) of the Act, as it was during the AY in question i.e. 2001-02, did not provide for deduction in the TDS where the payment was made in India. The requirement of deduction of TDS on payments made in India to residents was inserted, for the first time by way of Section 40(a) (ia) of the Act with effect from 1st April 2005. Then again as pointed out by Mr. M.S. Syali, learned Senior Advocate for the Intervener, Section 40(a) (ia) refers only to payments of —interest, commission or brokerage, fees for professional services or fees for technical services payable to a resident, or amounts payable to a ITA No. 7/2007 Page 27 of 35 contractor or sub-contractor‖ etc. It does not include an amount paid towards purchases. Correspondingly, there is no requirement of TDS having to be deducted while making such payment.***
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> ***49. However, the element of discrimination arises not only because of the above requirement of having to deduct TDS. The OECD Expert Group***

which brought out a document titled Application and Interpretation of Article 24(Non-Discrimination), Public discussion Draft, May 2007 did envisage deduction of tax while making payments to non-residents. It is viewed only as additional compliance of verification requirement which would not attract the non-discrimination rule. The OECD Expert Group noted that —the non-discrimination obligation under tax conventions is restricted in scope when compared with equal treatment or nondiscrimination clauses in an investment agreement." Specifically, in relation to withholding taxes, the Expert Group in the note by its chairman titled —Non-Discrimination in Bilateral Tax Conventions‖ noted as follows: —ITA Nos.2056 & 3229/Del/2014 A.Y. 2009-10 Honda Cars India Ltd.

6. The more limited non-discrimination obligations in tax conventions reflect the practical problems of cross-border taxation. For example, countries frequently collect taxes from non-residents through a system of withholding at source. Withholding is most frequently imposed on passive income, such as dividends, interest, rents, and royalties. Because the recipient may have no connection with the country of source other than the investment generating the income, withholding at the time of payment is likely to be the only realistic opportunity for the source country to collect its tax. Withholding is often not required on payments to residents. However, the application of withholding tax systems is appropriate. Residents have substantial economic connections with their country of residence; so that country is likely to have ample opportunity to collect its tax later, when a tax return is filed. Non-residents may be beyond the collection jurisdiction of the taxing country."(emphasis supplied)

50. While the above explanation provides the rationale for insisting on deduction of TDS from payments made to non-resident, the point here is not so much about the requirement of deduction of TDS per se but the consequence of the failure to make such deduction. As far as payment to a non-resident is concerned, Section 40(a) (i) of the Act as it stood at the relevant time mandated that if no TDS is deducted at the time of making such

payment, it will not be allowed as deduction while computing the taxable profits of the payer. No such consequence was envisaged in terms of Section 40(a) (i) of the Act as it stood as far as payment to a resident was concerned. This, therefore, attracts the non-discrimination rule under Article 26 (3)of the DTAA.

51. The arguments of counsel on both sides focussed on the expression same conditions' in Article 26(3)of the DTAA. To recapitulate, a comparison was drawn by learned counsel for the Revenue with Article 26(1) which speaks of preventing discrimination on the basis of nationality and which provision employs the phrase same circumstances'. Article 26 (2)which talks of prevention of discrimination vis-a-vis computing tax liability of PEs and employs the expression same activities'. The expression used in Article 26 (3)is same conditions'. Learned counsel for the Revenue sought to justify the difference in the treatment of payments made to non-residents by referring to Article 14of the Constitution of India and contended that the line of enquiry envisaged examining whether (a) the classification was based on an intelligible differentia and (b) whether the classification had a rational nexus with the object of the statute.

52.Section 40(a) (i), in providing for disallowance of a payment made to a non-resident if TDS is not deducted, is no doubt meant to be a deterrent ITA No. 7/2007 Page 29 of 35 in order to compel the resident payer to deduct TDS while making the payment. However, that does not answer the requirement of Article 26 (3)of the DTAA that the payment to both residents and non-residents should be under the same conditions' not only as regards deduction of TDS but even as regards the allowability of such payment as deduction. It has to be seen that in those same conditions' whether the consequences are different for the failure to deduct TDS.

53. It is argued by the Revenue that since in the present case no condition of deduction of TDS was attracted, in terms of Section 40(a) (i) of the Act as it then stood, to payments made to a resident, but only to payments made to non-residents, the two payments could not be said to be under the same

condition'. The further submission is that if they are not made under the same condition', the non-discrimination rule under Article 26 (3)of the DTAA is not attracted.

54. In the first place it requires to be noticed that DTAA is as a result of the negotiations between the countries as to the extent to which special concessional tax provisions can be made notwithstanding that there might be a loss of revenue. In Union of India v. Azadi Bachao Andolan(supra) the Supreme Court noted that treaty negotiations are largely —a bargaining process with each side seeking concessions from the other, the final agreement will often represent a number of compromises, and it may be uncertain as to whether a full and sufficient quid pro quo is obtained by both sides.‖ The Court acknowledged that developing countries allow 'treaty shopping' to encourage capital and technology inflows which developed countries are keen to provide to them. It was further noted that the corresponding loss of tax revenues could be insignificant compared to the other non-tax benefits to the economies of developing countries which need foreign investment. The Court felt that this was a matter best left to the discretion of the executive as it is —dependent upon several economic and political considerations.

55. Consequently, while deploying the nexus' test to examine the justification of a classification under a treaty like the DTAA, the line of enquiry cannot possibly be whether the classification has nexus to the object of the statute' for the purposes ofArticle14of the Constitution of India, but whether the classification brought about by Section 40(a) (i) of the Act defeats the object of the DTAA.

56. The argument of the Revenue also overlooks the fact that the condition under which deductibility is disallowed in respect of payments to non-residents, is plainly different from that when made to a resident. Under Section 40(a) (i), as it then stood, the allowability of the deduction of the payment to a non-resident mandatorily required deduction of TDS at the time of payment. On the other hand, payments to residents were neither subject to the condition of deduction of

TDS nor, naturally, to the further consequence of disallowance of the payment as deduction. The expression under the same conditions' in Article 26 (3) of the DTAA clarifies the nature of the receipt and conditions of its deductibility. It is relatable not merely to the compliance requirement of deduction of TDS. The lack of parity in the allowing of the payment as deduction is what brings about the discrimination. The tested party is another resident Indian who transacts with a resident making payment and does not deduct TDS and therefore in whose case there would be no disallowance of the payment as deduction because TDS was not deducted. Therefore, the consequence of non-deduction of TDS when the payment is to a nonresident has an adverse consequence to the payer. Since it is mandatory in ITA No. 7/2007 Page 31 of 35 terms of Section 40(a) (i) for the payer to deduct TDS from the payment to the non-resident, the latter receives the payment net of TDS. The object of Article 26 (3)DTAA was to ensure non-discrimination in the condition of deductibility of the payment in the hands of the payer where the payee is either a resident or a non-resident. That object would get defeated as a result of the discrimination brought about qua non-resident by requiring the TDS to be deducted while making payment of FTS in terms of Section 40(a) (i) of the Act.

57. A plain reading of Section 90(2) of the Act, makes it clear that the provisions of the DTAA would prevail over the Act unless the Act is more beneficial to the Assessee. Therefore, except to the extent a provision of the Act is more beneficial to the Assessee, the DTAA will override the Act. This is irrespective of whether the Act contains a provision that corresponds to the treaty provision. In Union of India v. Azadi Bachao Andolan(supra) the Supreme Court took note of the Circular No. 333 dated 2nd April 1982 issued by the CBDT on the question as to what the assessing officers would have to do when they find that the provision of a DTAA treaty is not in conformity with the Act.: —Thus, where a Double Taxation Avoidance Agreement provided for a particular mode of computation of income, the same should be followed, irrespective of the provision of the Income Tax Act. Where there is

no specific provision in the Agreement, it is the basic law, i.e., Income Tax Act, that will govern the taxation of income."

58. Further in Union of India v. Azadi Bachao Andolan(supra), after taking note of the decisions of various high courts on the purpose of Double Taxation Avoidance Conventions qua Section 90 of the Act, the Supreme court observed as under: "A survey of the aforesaid cases makes it clear that the judicial consensus in India has been that Section 90 is specifically intended to enable and empower the Central Government to issue a notification for implementation of the terms of a double taxation avoidance agreement. When that happens, the provisions of such an agreement, with respect to cases to which where they apply, would operate even if inconsistent with the provisions of the Income Tax Act. We approve of the reasoning in the decisions which we have noticed. If it was not the intention of the Legislature to make a departure from the general principle of chargeability to tax under Section 4 and the general principle of ascertainment of total income under Section 5 of the Act, then there was no purpose in making those sections subject to the provision of the Act. The very object of grafting the said two sections with the said clause is to enable the Central Government to issue a notification under Section 90towards implementation of the terms of the DTAs which would automatically override the provisions of the Income tax Act in the matter of ascertainment of chargeability to income tax and ascertainment of total income, to the extent of inconsistency with the terms of the DTAC.

59. Consequently, the Court negatives the plea of the Revenue that unless there are provisions similar to Section 40(a) (i) of the Act in the DTAA, a comparison cannot be made asto which is more beneficial provision.

60. The reliance by the Revenue on the decision of this Court in Hyosung Corporation v. AAR (2016) 382 ITR 371 (Del) is misplaced. There the Court negatived a challenge to the constitutionality of Section 245R(2)(i) of the Act on the ground that it was violative of Article 14of the Constitution as well as Article 25of the DTAA between India and

South Korea. Section 245R(2) of the Act barred a non-resident applicant from approaching the Authority for Advance Ruling (AAR) where the matter was pending before any income tax authority. The matter, therefore, only pertained to the procedure of filing a petition before the AAR and not as regards any substantive right. The decision of the Pune Bench of the ITAT in Automated Securities Clearance Inc. v. Income Tax Officer (supra)is no assistance to the Revenue since the said decision is said to be overruled by the Special Bench of the ITAT in the case of Rajeev Sureshbhai Gajwani vs ACIT (2011) 8 ITR (Trib) 616 (Ahmedabad).

61. In light of the above discussion, question (b) is answered in the affirmative, i.e., in favour of the Assessee and against the Revenue by holding that Section 40(a) (i) of the Act is discriminatory and therefore, not applicable in terms of Article 26 (3)of the Indo-US DTAA.

62. Accordingly, question (a) is answered in the affirmative, i.e., in favour of the Assessee and against the Revenue by holding that the ITAT was correct in allowing a deduction of Rs. 5.83 crores being the administrative fee paid by the Assessee to HIAI."

These findings are binding on us. Thus, we have to uphold the arguments of the ld. counsel for the assessee and reverse the findings of the AO as confirmed by the ld.CIT(A).

18. Coming to the argument of the ld. DR that the conditions stated in Article 24(3)are not satisfied, as provisions of Article 9(1)applies, as the transactions are between AEs and the profits which would, but for those conditions would have accrued to one of the enterprises, but by reason of those conditions have not so accrued, we find that the Transfer Pricing Officer in all these cases has come to the conclusion that the transactions between the Associated Enterprises are at arm's length price. The ld. DR made strenuous and elaborate submissions bringing out certain issues raised by the AO, to persuade us that TPO was wrong in coming to the conclusion that the transactions between the AEs and the assessee are at arm's length. We find that the TPO has passed the order after the surveys were conducted on the assessee. If the AO had certain additional material facts, he could have

brought it to the notice of the TPO and asked for a fresh report. In our view, this argument of the Ld. D.R. is erroneous, as the revenue wants to take a stand that the transactions between the assessee and its AE are not at arm's length for the limited purpose of denying the benefit of the non-discrimination article in the DTAA to the assessee and not for making any additions under the transfer pricing provisions. Year after year, the transfer pricing officer has given a finding that the transactions between the assessee and the AE are at arm's length. The ld. DR, without specifically pointing out as to what is the difference between the arm's length price and the price at which the transactions have taken place between the assessee and the AE and without quantifying the excess/shortage in the price, seeks to invoke Article 9(1).In our view, such an argument is devoid of merit and hence we dismiss the same.

19. The ld. DR relies on the judgment of the jurisdictional Delhi High Courtin the case of Jansampark Advertising & Marketing (P) Ltd. (supra) and pleads that the Tribunal should set aside the matter to the AO/TPO to re-adjudicate the issueITA Nos.2056 & 3229/Del/2014 A.Y. 2009-10 Honda Cars India Ltd. as to whether the transactions between the A.E. and the assessee are at arm's length or not. We do not think that the facts and circumstances of the case warrants such an action by the Tribunal. The Transfer Pricing Officer passed his order on 29th January, 2013, whereas the surveys were carried out on 24.2.2010 and 19th December, 2012. No specific defects are pointed out, either in the TP report or in the order of the Transfer Pricing Officer and only general submissions are made before us in this regard. Hence, this contention is also dismissed as devoid of merits. On the submissions made by the Ld.D.R. on Article 14, 15and16of the Constitution, technical expression in the UN Model Convention, etc., we find that the Jurisdictional High Court has considered all these issues in the case of Herbalife International India (supra). Respectfully following the same, these arguments are rejected.

20. In view of the above discussion, we allow this ground of the assessee and delete the disallowance made u/s 40(a)(i) of the Act, by applying the propositions of law laid down by the Jurisdictional High Court regarding interpretation of the non-discrimination article in the Double Taxation Avoidance Agreement between India and Japan. We do not adjudicate the other issues argued before us for the reasons already discussed."

> ***14. In the year under consideration, the Ld. CIT(DR)repeated the arguments made before the Tribunal in assessment year 2009-10 and also contested that non-discrimination clause of article 24(3) of the DTAA between India and Japan is not applicable over the assessee and there was no discrimination qua the payer. However, we find that as far as the payment to Honda motor Japan is concerned, the issue in dispute is squarely covered by the decision of the Tribunal in assessment year2009-10, wherein the Tribunal has followed the decision of the Hon'ble Delhi High Court in the case of CIT Vs. Herbalife (supra). We note that Hon'ble High Court in the case of Herbalife (supra) has also considered the amendment in provisions of section 40(a)(i) of the Act by way of insertion of sub-clause(ia) w.e.f. 01/04/2005. Accordingly, respectfully following the decision of the Hon'ble Delhi High Court and the order of Tribunal (supra), we delete the disallowance in respect of payment to Honda motor Japan.***
>
> ***15. Regarding payment to Honda Asia Thailand in the year under consideration, the assessee contended that no PE has been held by the DRP in the case of non-resident company in assessment year 2010-11 and this fact was not controverted by the Ld. CIT-(DR), thus, following the decision of the Tribunal in assessment year 2009-10, we hold no disallowance could be made under section 40(a)(i) of the Act for payment made to Honda Asia Thailand without deduction of tax at source."***

14. In view of what has been discussed above and following the order passed by the coordinate Bench of the Tribunal in assessee's own case (supra), we are of the considered view that addition made/sustained by the AO/CIT(A) of Rs.13,09,82,982/- u/s 40(a)(i) of the Act for not deducting the tax at source of payments made for purchase of raw material, components, etc. from non-resident Indian is not sustainable in the eyes of law, hence ordered to be deleted. Consequently, Grounds No.3 & 8 are determined in favour of the assessee.

GROUND NO.16

15. Ground No.16 being premature needs no specific findings.

16. Resultantly, the appeal filed by the assessee is partly allowed.

Order pronounced in open court on this 17th day of July, 2020.

sd/-	**sd/-**
(N.K. BILLAIYA)	**(KULDIP SINGH)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Dated the 17th day of July, 2020
TS

Copy forwarded to:
1.Appellant
2.Respondent
3.CIT
4.CIT(A), New Delhi.
5.CIT(ITAT), New Delhi.

AR, ITAT
NEW DELHI.