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Analysis of *Vodafone* Case on Applicability of Transfer Pricing Provisions to Issuance of Equity Shares

In addition to the recent ruling by the Bombay High Court in the *Vodafone India Services* case, the authors consider related case law on the applicability of transfer pricing provisions to the issuance of equity shares to a related party.

1. Introduction

On 10 October 2014, the Bombay High Court ruled in the *Vodafone India Services Pvt. Ltd.* case, [1] (*Vodafone IV*), thereby settling one of the biggest transfer pricing controversies in India. In *Vodafone IV*, the shares of an Indian subsidiary were issued to its non-resident holding company at a price which was less than the arm's length value of such shares, according to the tax authorities. Thus, the assessing officer, based on the order of the transfer pricing officer, made an adjustment due to the shortfall between the arm's length value and the actual price received for the shares issued, deeming it to be income of the taxpayer chargeable to tax. Furthermore, that shortfall was treated as a deemed loan and notional interest thereon was attributed and charged as income.

The questions before the Bombay High Court were (i) whether the alleged shortfall between the so-called arm's length value of equity shares issued to its holding company and the issue price of such equity shares can be considered as income as defined under the Income Tax Act, 1961 (the ITA) and tax levied thereon and (ii) whether the subsequent secondary adjustment, namely attributing the notional interest on such shortfall (which was deemed to be a loan), is sustainable in law.

2. Facts of the Case

The taxpayer is a wholly owned subsidiary of a non-resident company, Vodafone Tele-Services (India) Holdings Limited. The taxpayer required funds for its telecommunication services project in India. Thus, it issued 289,224 equity shares with a face value of INR 10 each, at a premium of INR 8,509 per share to its holding company – which was determined in accordance with the methodology prescribed by the government under the Capital Issues (Control) Act, 1947.

The taxpayer, out of abundant caution, disclosed this transaction (i.e. the issuance of shares to the taxpayer's holding company) as an "international transaction" in Form 3CEB, complying with section 92E read with explanation (i), clause (c) to section 92B of the ITA. Under the ITA, the return of income of a taxpayer must be accompanied with Form 3CEB, which discloses the transactions entered into between the taxpayer and its associated enterprises, the method of benchmarking such transactions, etc.

However, the assessing officer and transfer pricing officer valued each equity share at INR 53,775 and, on that basis, made an adjustment of INR 45,256 per share (amounting to INR 1,308.91 crores, approximately USD 210 million), by treating the shortfall in premium as income.

	Computation of arm's length price	Number/ Amount (INR)
(a)	Arm's length value of each equity shares on 31 Mar. 2008	53,775
(b)	Value of equity shares as per the taxpayer	8,519
(c)	Shortfall per share (c) = (a) – (b)	45,256
(d)	Equity shares issued	289,224
(e)	Price charged by the taxpayer	2,463,899,256
(f)	Arm's length price (f) = (a) x (d)	15,553,020,600
(g)	Total shortfall from arm's length price (g) = (f) – (e)	13,089,121,344

As a consequence of the above, the assessing officer and transfer pricing officer treated the said shortfall as a deemed loan given by the taxpayer to its holding company, and also asserted that periodical interest at the rate of 13.5% per annum was to be charged to tax as interest income. As a result, an additional adjustment to the extent of INR 88.35 crores (approximately USD 14 million) was made, which was determined as follows:

Amount of deemed loan (INR)	13,089,121,344
Period	6 months
Arm's length interest rate (per annum)	13.50%
Arm's length consideration @ 13.97% per annum (INR)	883,515,691

The taxpayer filed a writ petition (*Vodafone III*) before the Bombay High Court (the High Court) challenging:

– the jurisdiction of the assessing officer to refer the matter to the transfer pricing officer for determining the arm's length price under section 92CA of the ITA; and
– the jurisdiction of the assessing officer and transfer pricing officer to tax the above issuance of shares

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1. IN: HC Bombay, 10 Oct. 2014, *Vodafone India Services Pvt. Ltd. v. ACIT*, Writ Petition 871 of 2014.

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considering that this transaction did not result in any income accruing or arising which was chargeable to tax under the ITA.

The High Court in *Vodafone III* accepted the plea of the taxpayer and directed the Dispute Resolution Panel (i.e. the first authority to adjudicate disputes arising due to transfer pricing and other issues as stated in the ITA) to first decide only the preliminary jurisdictional issues raised by the taxpayer. Consequent to these directions, the Panel considered the issue of jurisdiction and rejected the taxpayer's preliminary objection thereto.

Next, the taxpayer filed a subsequent writ petition before the High Court, challenging the order of the Dispute Resolution Panel as patently illegal which held that the assessing officer and transfer pricing officer had jurisdiction to tax such shortfall in premium under Chapter X of the ITA (Indian transfer pricing regulations) (*see* Appendix 1), as income that arose in the above international transaction.

3. Main Contentions of the Taxpayer

The taxpayer made the following arguments.

Chapter X of the ITA (Chapter X) is a special provision relating to avoidance of tax. Section 92(1) of the ITA states that "any income arising from an international transaction shall be computed having regard to the arm's length price". Thus, the essential condition for application of section 92(1) of the ITA is that income should arise from an international transaction. In this case, the taxpayer argued that no income arose from the issuance of equity shares by the taxpayer to its holding company.

The word "income" would have to be understood as defined by other provisions of the ITA, such as section 2(24). A fiscal statute must be strictly interpreted upon its own terms, and the meaning of ordinary words may not be expanded to afford a purposeful interpretation.

Chapter X is not designed to bring to tax all amounts involved in a transaction which are otherwise not taxable. Therefore, before any transaction may be brought to tax, taxable income must arise. The interpretation by the tax authorities to tax any amount involved in an international transaction is tantamount to imposing a penalty for entering into a transaction (which in no way gave rise to taxable income) at a value which the tax authorities determine based on application of the arm's length price.

The issuance of shares by the taxpayer to its holding company and receipt of consideration in exchange therefor is a capital receipt under the ITA. Capital receipts may not be brought to tax unless specifically and expressly brought to tax by the ITA.

The assessing officer and transfer pricing officer assumed that the amount of share premium foregone was received, and had the taxpayer invested the same, would have given rise to income. The taxpayer asserted that no tax may be charged on an assumption, estimate or conjecture in the absence of any such income arising.

4. Assertions by the Tax Authorities in Response to the Taxpayer

The taxpayer did not challenge the constitutional validity of Chapter X or the fact that the taxpayer and its holding company were associated enterprises within the meaning of Chapter X. Thus, the provisions of Chapter X are applicable to the facts of the present case.

The legislative history states that even in absence of actual income, notional income may be brought to tax. In this regard, the tax authorities relied on the decision of the Supreme Court in the *Mazgaon Dock* case.[2]

The concept of real income has no application for the purpose of Chapter X and therefore, the difference between the arm's length price and the contracted price must be added to the total income. The word "income", for the purpose of Chapter X, is to be given the broadest meaning so as to include deemed income arising for the purpose of total income under sections 4 and 5 of the ITA.

Chapter X is a complete code in itself and not merely a machinery to compute the arm's length price.

Even if no separate head of income under section 14 covers the transaction, the passing on of the benefit by the taxpayer to the holding company would fall under the head "Income from other sources" under section 56(1) of the Act.

5. Key Observations and Decision of the High Court

The Bombay High Court observed that income arising from an international transaction is a condition precedent for the application of Chapter X. This is from the perspective of examining whether jurisdiction existed with the AO/TPO to apply Chapter X. However, the Court examined the issue afresh and found as follows.

The term "income" as defined in section 2(24) of the ITA, although an inclusive definition, cannot include capital receipts unless it is so specified, as in section 2(24)(vi) of the ITA. Further, capital gains chargeable to tax under section 45 of the ITA are defined to be income. Amounts received upon the issuance of share capital (including the premium) were undoubtedly on capital account. Therefore, due to the lack of express legislation, no amount received, accrued or arising from a capital account transaction may be subject to tax as income. The Court relied on the decision of the Bombay High Court in the *Cadell Weaving Mill* case,[3] which was upheld by the Supreme Court in the *D.P. Sandu Bros. Chembur* case.[4]

The High Court followed the principle of *ex abundanti cautela* (out of abundant caution), rejecting the assertion by the tax authorities that, as the taxpayer had itself reported the transaction in Form 3CEB, it could not raise the issue of jurisdiction to apply Chapter X.

2. IN: SC, 12 May 1958, *Mazgaon Dock Ltd. v. CIT,* 1958 AIR 861.
3. IN: HC Bombay, 6 Feb. 2001, *Cadell Weaving Mill Co. v. CIT*, 249 ITR 265.
4. IN: SC, 31 Jan. 2005, *CIT v. D.P. Sandu Bros. Chembur Pvt. Ltd.*, 273 ITR 1.

Further, the High Court rejected the contention by the tax authorities that Chapter X is a complete code by itself and not merely a machinery provision to compute the arm's length price. The Court also did not agree that it is a hidden benefit of the transaction which is being charged to tax and that the charging section is inherent in Chapter X. The Court stated that it is a well settled position in law that a charge to tax must be specifically mentioned in the ITA, i.e. in the absence of a charging section in Chapter X, it is not possible to read a charging provision into Chapter X.

The High Court rejected the argument of the tax authorities regarding the applicability of section 92(2), and concluded that section 92(2) would have no application in the present case, as there was no occasion to allocate, apportion or contribute any cost and/or expense between the taxpayer and the holding company. Section 92(2) deals with a mutual agreement or arrangement for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility between two associated enterprises. The tax authorities had asserted that the cost incurred (namely the shortfall in the premium received) resulted in the passing on of a benefit to the associated enterprise (the holding company) which is brought to tax. The High Court held that section 92(2) would have no application in cases like the present one, where there was no occasion to allocate, apportion or contribute any cost and/or expense between the taxpayer and the holding company.

The High Court also rejected the contention by the tax authorities that, in view of Chapter X, the notional income is to be brought to tax, and that the concept of real income was irrelevant.

The High Court observed that the Parliament consciously had not brought to tax amounts received from a non-resident for the issuance of shares, as doing so would discourage capital inflow from abroad.

The High Court further noted that income tax is not a tax on capital receipts. The issuance of shares at a premium is a capital account transaction and not income. The classical distinction between income and capital is that which exists between fruit and a tree. Income is a flow, while capital is a fund. The High Court relied on the decision in the *Shaw Wallace* case, which stated that "income has been likened pictorially to the fruit of a tree or the crop of a field".[5]

Chapter X is a mechanism used to arrive at the arm's length price of a transaction between associated enterprises. The substantive charging provisions are found in sections 4, 5 (Scope of income), 15 (Salaries), 22 (Income from house property), 28 (Profits and gains of business), 45 (Capital gain) and 56 (Income from other sources) of the ITA. Thus, the High Court noted that even income arising from an international transaction between associated enterprises must satisfy the test of income under the ITA and must find its home under one of the above heads (i.e. charging provisions), as Chapter X is merely a machinery provision that is used to compute chargeable income at the arm's length price.

Further, the High Court added that the machinery section may not be read de-hors, i.e. apart from, the charging section, relying on the observations of the Supreme Court in the *B.C. Srinivasa Setty* case.[6]

Based on the above reasons and findings, the High Court concluded that the issuance of shares at a premium by the taxpayer to its non-resident holding company does not give rise to any income from an admitted international transaction. Thus, there was no occasion to apply Chapter X in such a case. Regarding the subsequent secondary adjustment of notional interest income, the High Court held that such an adjustment may not be sustained, as it is based on mere estimates and assumptions that the taxpayer "would have invested the same", which is not acceptable. The High Court quashed all the orders of the tax authorities (i.e. those of the assessing officer, transfer pricing officer and Dispute Resolution Panel) and set them aside as being without jurisdiction, null and void.

6. Connected Decisions

6.1. *Shell* case

After the decision in *Vodafone IV*, the Bombay High Court issued its decision in *Shell India Markets Pvt. Ltd.*[7] (*Shell*), which dealt with a similar issue. The facts in the *Shell* case were similar, except that Shell did not disclose the issuance of equity shares to its non-resident associated enterprise as an international transaction in Form 3CEB.

The assessing officer referred the transaction of the issuance of equity shares to the transfer pricing officer for computing the arm's length consideration thereof. Shell argued that, in the absence of income arising from the transaction of issuance of equity shares at a premium, the transaction was not an international transaction which could be brought within the purview of Chapter X, as the issuance of shares was on capital account and did not give rise to any income. However, the transfer pricing officer concluded that, in view of Chapter X, once a transaction between the parties is an international transaction, a transfer pricing adjustment may be made even on capital account. The issue was raised before the Dispute Resolution Panel, which ruled in favour of the tax authorities and thus held that the assessing officer and transfer pricing officer had jurisdiction to bring to tax the shortfall of receipt of premium on the issuance of shares.

A writ was filed by Shell before the Bombay Court against the directions of the Dispute Resolution Panel. The High Court, following its decision in *Vodafone IV*, held that the jurisdiction to apply Chapter X would exist only when income arises out of an international transaction and such income is chargeable to tax under the ITA. Further, it also held that if the taxpayer did not include a particular transaction in Form 3CEB when so required to be included, the

5. IN: PC, , *CIT v. Shaw Wallace & Co. Ltd.*, 6 ITC 178 (PC).

6. IN: SC, 19 Feb. 1981, *CIT v. B.C. Srinivasa Setty*, 128 ITR 294.

7. IN: HC Bombay, 18 Nov. 2014, *Shell India Markets Pvt. Ltd. v. ACIT et al.*, Writ Petition 1205 of 2013.

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consequences thereof, as provided under the ITA, would follow. The High Court held that the mere failure to file the Form 3CEB by the taxpayer would not grant jurisdiction to the tax authorities to tax an amount which the tax authorities do not have jurisdiction to tax.

6.2. *Equinox Business Parks*

Recently, the Bombay High Court ruled in favour of the taxpayer in *Equinox Business Parks*.[8] This case dealt with similar issues, namely:

- whether the issuance of equity shares and compulsory convertible debentures gives rise to income from an international transaction and is chargeable to tax under the ITA;
- whether the arm's length price of the equity shares and compulsory convertible debentures (CCDs) should be revised upwards; and
- whether the shortfall in receipt of the arm's length price on the issuance of shares and CCDs should be treated as a deemed loan on the alleged shortfall on which the deemed interest was to be charged to tax.

6.3. *Leighton India Contractors*

In *Leighton India Contractors*,[9] the Bombay High Court also dealt with a similar issue, namely whether the issuance of equity shares by the taxpayer company to its non-resident associated enterprises, and the conversion of its preference shares held by the non-resident associated enterprises into equity shares, would attract the provisions of Chapter X.

6.4. *Essar Projects (India)*

In *Essar Projects (India)*[10] the Bombay High Court again dealt with a similar issue, namely whether it makes any difference to the taxability of a transaction involving the issuance of shares to a non-resident entity, if the declaration filed in Form 3CEB is not sufficient. In other words, the issue concerned whether an inadequate declaration may have the effect of converting non-taxable income into taxable income.

Relying on *Vodafone IV*, the Court held that:

- the sine qua non to apply Chapter X is the arising of income under the ITA out of an international transaction. This income must be chargeable under the ITA, before Chapter X may be applied;
- the definition of income does not include within its scope capital receipts arising out of a capital account transaction unless so specified in section 2(24) of the ITA as income;
- there is no charge in the ITA to tax amounts received and/or arising on account of the issuance of shares by an Indian entity to a non-resident entity in sections 4, 5, 15, 22, 28, 45 and 56 of the ITA. This is because such amount arises out of a capital accounts transaction and, therefore, is not income;
- Chapter X does not contain any charging provision, but is a machinery provision to arrive at the arm's length price of a transaction between associated enterprises; and
- Chapter X does not change the character of the receipt, but merely permits the requantification of income uninfluenced by the relationship between the associated enterprises.

7. Concept of Real Income

The High Court judgments in *Vodafone*, *Shell* and other cases reiterate the fundamental principle that the taxability of any receipt as income, is to be determined under the charging provisions of the ITA, and that the ITA brings to charge only real income and not notional or hypothetical income, except in the limited circumstances which must be so legislated in clear, precise terms.

In *Shoorji Vallabhdas and Co.*, the Supreme Court held as follows:

> Income tax is a levy on income. No doubt, the Income Tax Act takes into account two points of time at which the liability to tax is attracted, viz., the accrual of the income or its receipt; but the substance of the matter is the income. If income does not result at all, there cannot be a tax, even though in book-keeping, an entry is made about a 'hypothetical income', which does not materialise. Where income has, in fact, been received and is subsequently given up in such circumstances that it remains the income of the recipient, even though given up, the tax may be payable. Where, however, the income can be said not to have resulted at all, there is obviously neither accrual nor receipt of income, even though an entry to that effect might, in certain circumstances, have been made in the books of account. [11]

The Supreme Court reiterated this proposition once again after 50 years in the *Excel Industries Ltd.* case. [12]

The Gujarat High Court in the *Acharya D.V. Pande* case observed that:

> What is the natural connotation of income is, however, nowhere to be found in the IT Act. The IT Act merely describes sources of income and prescribes the methods of computing income, but what constitutes income, it discreetly refrains from saying. The decided cases of course declare that "income" is a term of formidably wide and vague import and it is a word difficult and perhaps impossible to define in any precise general formula. But, howsoever broad may be the connotation of the word "income." one thing is clear that income for tax purposes must be money or money's worth. [13]

It is for the income tax authorities to prove that a particular receipt is taxable. In deciding whether an item of receipt is taxable as income, a court may consider the evidence in the light of the statements made by the taxpayer and the taxpayer's conduct; but in arriving at its conclusion there must be a fair and reasonably full review of the evidence.[14]

8. IN: HC Bombay, 19 Nov. 2014, *Equinox Business Parks Pvt. Ltd. v. Union of India et al.*, Writ Petition 1273 of 2014.
9. IN: HC Bombay, 18 Nov. 2014, *Leighton India Contractors Pvt. Ltd. v. Union of India et al.*, Writ Petition 732 of 2014.
10. IN: HC Bombay, 19 Nov. 2014, *Essar Projects (India) Ltd. v. Union of India et al.*, Writ Petition 1399 of 2014.
11. IN: SC, 27 Mar. 1962, *CIT v. Shoorji Vallabhdas and Co.*, 46 ITR 144 (SC).
12. IN: SC, 8 Oct. 2013, *CIT v. M/s. Excel Industries Ltd.*, (2013) 358 ITR 295 (SC).
13. IN: HC Gujarat, 17 Sept. 1964, *Acharya D.V. Pande v. CIT*, (1965) 56 ITR 152 (Guj).
14. IN: SC, 14 Apr. 1967, *Udhavdas Kewalram v. CIT*, (1967) 66 ITR 462 (SC).

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Once it is shown that a receipt is taxable, the burden of proof shifts to the taxpayer to show that it falls under an exemption provision. [15]

The scheme of Chapter X is to compute income or determine the allowance of any expense or interest, arising from an international transaction, having regard to the arm's length price. For Chapter X to be applicable to a transaction, it must be determined that the transaction falls within the definition of "international transaction" under section 92B(1) of the ITA. Further, after determining that the transaction falls under the definition of international transaction, it also must be established that such international transaction results in income arising or accruing under section 92(1) of the ITA. Therefore, for the machinery section to apply, as regards the computation of income arising from an international transaction in line with the arm's length price, both the conditions for the deemed existence of an international transaction and consequently the income arising or accruing from such a transaction must be cumulatively satisfied. The failure to fulfil both conditions will result in the inapplicability of the machinery section (i.e. section 92(1)) and thus, Chapter X would not apply to such transaction.

8. Conclusion

These judgments in the *Vodafone* and *Shell* cases, among others, reiterate the first principles of taxation under the ITA. These judgments have highlighted a significant aspect of the jurisdictional issue for the applicability of Chapter X, underscoring that Chapter X is a machinery provision and not a charging provision.

Transfer pricing provisions have not replaced the concept of income or expenditure as normally understood under the ITA. The Bombay High Court once again clearly stated that taxing provisions may not be read on the basis of intent, but must be construed strictly on the basis of the text of the statute. Further, what has not been provided under the ITA cannot be presumed to exist without there being an express provision for the same.

The Bombay High Court quoted a passage by Rowlatt J. in the *Cape Brandy Syndicate*[16] case, approved by the House of Lords in the *Canadian Eagle Oil Co. Ltd.* case,[17] to emphasize the above:

> In a taxing Act, one has to look merely at what is clearly said. There is no room for any intendment. There is no equity about tax. There is no presumption as to tax. Nothing is to be read in, nothing is to be implied. One can only look fairly at the language used.

The above principle was restated by Justice J.C. Shah (as he then was) in the *Modi Sugar Mills* case, as follows:

> In interpreting a taxing statute, equitable considerations are entirely out of place. Nor can taxing statutes be interpreted on any presumptions or assumptions. The court must look squarely at the words of the statute and interpret them. It must interpret a taxing statute in the light of what is clearly expressed. [18]

The High Court has reiterated the basic principles of interpretation of taxing statutes, stating that such provisions must be read as a whole, without rejecting and/or adding words thereto. The rejection of words in a statute to achieve a pre-determined objective is not permissible, as this would amount to an effective redrafting of legislation, which would be beyond the jurisdiction of the courts.

The *Vodafone* judgment demonstrates that there is a conceptual difference between transfer pricing literature and the scope of Indian domestic tax law, to bring within its net all such concepts debated in such literature.

The Central Board of Direct Taxes (CBDT) has stated that it accepts the decision made in *Vodafone IV* and has directed that the *ratio decidendi* of the judgment must be adhered to by the field officers in all cases where this issue is involved:[19] "[T]he Court has held, inter-alia, that the premium on share issue was on account of a capital account transaction and does not give rise to income and, hence, not liable to transfer pricing adjustment". Also, the acceptance of the decision by the CBDT would mean that no further appeal is to be filed against the Bombay High Court decision before the Supreme Court.

15. IN: SC, 21 Apr. 1965, *Parimisetti Seetharamamma v. CIT*, (1965) 57 ITR 532 (SC).
16. IN: KB, 1921, *Cape Brandy Syndicate v. Inland Revenue Commissioners*, (1921) 1 KB 64 (statement by Rowlatt J.).
17. IN: HL, 1946, *Canadian Eagle Oil Co Ltd v. The King*, 27 TC 205.
18. IN: SC, 31 Oct. 1960, *Sales Tax Commissioner v. Modi Sugar Mills*, 1961 (048) AIR 1047.
19. IN: CBDT, 29 Jan. 2015, Instruction No. 02/2015.

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Appendix: Relevant Sections of the Income Tax Act, 1961

Section 4 – Charge of income tax

(1) Where any Central Act enacts that income tax shall be charged for any assessment year at any rate or rates, income tax at that rate or those rates shall be charged for that year in accordance with, and [subject to the provisions (including provisions for the levy of additional income tax) of this Act] in respect of the total income of the previous year of every person:

Provided that where by virtue of any provision of this Act income tax is to be charged in respect of the income of a period other than the previous year, income tax shall be charged accordingly.

(2) In respect of income chargeable under sub-section (1), income tax shall be deducted at the source or paid in advance, where it is so deductible or payable under any provision of this Act.

Section 5 – Scope of total income

(1) Subject to the provisions of this Act, the total income of any previous year of a person who is a resident includes all income from whatever source derived which:
(a) is received or is deemed to be received in India in such year by or on behalf of such person; or
(b) accrues or arises or is deemed to accrue or arise to him in India during such year; or
(c) accrues or arises to him outside India during such year:

Provided that, in the case of a person not ordinarily resident in India within the meaning of sub-section (6) of section 6, the income which accrues or arises to him outside India shall not be so included unless it is derived from a business controlled in or a profession set up in India.

(2) Subject to the provisions of this Act, the total income of any previous year of a person who is a non-resident includes all income from whatever source derived which:
(a) is received or is deemed to be received in India in such year by or on behalf of such person; or
(b) accrues or arises or is deemed to accrue or arise to him in India during such year.

Explanation 1. Income accruing or arising outside India shall not be deemed to be received in India within the meaning of this section by reason only of the fact that it is taken into account in a balance sheet prepared in India.

Explanation 2. For the removal of doubts, it is hereby declared that income which has been included in the total income of a person on the basis that it has accrued or arisen or is deemed to have accrued or arisen to him shall not again be so included on the basis that it is received or deemed to be received by him in India.

Section 92 – Computation of income from international transaction having regard to arm's length price

(1) Any income arising from an international transaction shall be computed having regard to the arm's length price.

Explanation. For the removal of doubts, it is hereby clarified that the allowance for any expense or interest arising from an international transaction shall also be determined having regard to the arm's length price.

(2) Where in an international transaction [or specified domestic transaction], two or more associated enterprises enter into a mutual agreement or arrangement for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises, the cost or expense allocated or apportioned to, or, as the case may be, contributed by, any such enterprise shall be determined having regard to the arm's length price of such benefit, service or facility, as the case may be.

[(2A) Any allowance for an expenditure or interest or allocation of any cost or expense or any income in relation to the specified domestic transaction shall be computed having regard to the arm's length price.]

(3) The provisions of this section shall not apply in a case where the computation of income under sub-section (1) [or sub-section (2A)] or the determination of the allowance for any expense or interest under [sub-section (1) or sub-section (2A)], or the determination of any cost or expense allocated or apportioned, or, as the case may be, contributed under sub-section (2) 83[or sub-section (2A)], has the effect of reducing the income chargeable to tax or increasing the loss, as the case may be, computed on the basis of entries made in the books of account in respect of the previous year in which the international transaction [or specified domestic transaction] was entered into.

Section 92B – Meaning of international transaction

(1) For the purposes of this section and sections 92, 92C, 92D and 92E, "international transaction" means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises.

(2) A transaction entered into by an enterprise with a person other than an associated enterprise shall, for the purposes of sub-section (1), be [deemed to be a transaction] entered into between two associated enterprises, if there exists a prior agreement in relation to the relevant transaction between such other person and the associ-

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ated enterprise, or the terms of the relevant transaction are determined in substance between such other person and the associated enterprise [where the enterprise or the associated enterprise or both of them are non-residents irrespective of whether such other person is a non-resident or not].

[Explanation. For the removal of doubts, it is hereby clarified that:

(i) the expression "international transaction" shall include:

(a) the purchase, sale, transfer, lease or use of tangible property including building, transportation vehicle, machinery, equipment, tools, plant, furniture, commodity or any other article, product or thing;

(b) the purchase, sale, transfer, lease or use of intangible property, including the transfer of ownership or the provision of use of rights regarding land use, copyrights, patents, trademarks, licences, franchises, customer list, marketing channel, brand, commercial secret, know-how, industrial property right, exterior design or practical and new design or any other business or commercial rights of similar nature;

(c) capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;

(d) provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service;

(e) a transaction of business restructuring or reorganisation, entered into by an enterprise with an associated enterprise, irrespective of the fact that it has bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date;

(ii) the expression "intangible property" shall include:

(a) marketing related intangible assets, such as, trademarks, trade names, brand names, logos;

(b) technology related intangible assets, such as, process patents, patent applications, technical documentation such as laboratory notebooks, technical know-how;

(c) artistic related intangible assets, such as, literary works and copyrights, musical compositions, copyrights, maps, engravings;

(d) data processing related intangible assets, such as, proprietary computer software, software copyrights, automated databases, and integrated circuit masks and masters;

(e) engineering related intangible assets, such as, industrial design, product patents, trade secrets, engineering drawing and schema-tics, blueprints, proprietary documentation;

(f) customer related intangible assets, such as, customer lists, customer contracts, customer relationship, open purchase orders;

(g) contract related intangible assets, such as, favourable supplier, contracts, licence agreements, franchise agreements, non-compete agreements;

(h) human capital related intangible assets, such as, trained and organised work force, employment agreements, union contracts;

(i) location related intangible assets, such as, leasehold interest, mineral exploitation rights, easements, air rights, water rights;

(j) goodwill related intangible assets, such as, institutional goodwill, professional practice goodwill, personal goodwill of professional, celebrity goodwill, general business going concern value;

(k) methods, programmes, systems, procedures, campaigns, surveys, studies, forecasts, estimates, customer lists, or technical data;

(l) any other similar item that derives its value from its intellectual content rather than its physical attributes.]

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