**IN THE INCOME TAX APPELLATE TRIBUNAL**
**DELHI BENCH: 'I-1', NEW DELHI**

**BEFORE SHRI AMIT SHUKLA, JUDICIAL MEMBER**
**AND**
**SHRI O.P. KANT, ACCOUNTANT MEMBER**

ITA No.1431/Del/2015
Assessment Year: 2010-11

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| M/s. Adidas India Marketing (P.) Ltd., 5th Floor, Unitech Commercial Tower-II, Sector-45, Block-B, Greenwoods City, Gurgaon | **Vs.** | Income Tax Officer, Ward-1(3), New Delhi |
| **PAN : AAACA5313P** | | |
| **(Appellant)** | | **(Respondent)** |

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| Appellant by | Shri Ajay Vohra, Sr. Adv;<br>Ms. Shaily Gupta, CA; and<br>Mr. Ramit Katyal, CA |
| Respondent by | Shri Sanjay I. Bara, CIT(DR) |

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|---|---|
| Date of hearing | 02.07.2019 |
| Date of pronouncement | 29.07.2019 |

**ORDER**

***PER O.P. KANT, A.M.:***

This appeal by the assessee is directed against order dated 02/02/2015 passed by the Income Tax Officer, Ward 1(3), Range -1, New Delhi (hereinafter will be referred as 'the Assessing Officer') in compliance to the directions issued by the learned Dispute Resolution Panel (in short 'the DRP'). The grounds raised by the assessee in the appeal are reproduced as under:

***"General:***

*1. The impugned order of assessment framed by the assessing officer in pursuance of the directions of the Dispute Resolution Panel (hereinafter referred to as 'DRP') under Section 143(3) read with Section 144C of the Income-tax Act, 1961 ( 'Act'), is bad in law, violative of principles of natural justice and void ab-initio.*

*1.1 That on the facts and circumstances of the case, the assessing officer erred on facts and in law in completing the assessment under section 143(3) read with section 144C of the Income-tax Act, 1961 ('the Act') at total income of Rs.1,10,22,13,698, before set-off of brought forward losses, as against loss of Rs. 12,61,25,995 returned by the appellant.*

***Transfer Pricing Adjustment on AMP Expenses:***

*2. That the assessing officer erred on facts and in law in making addition of Rs. 31,90,82,215 on account of alleged difference in the arm's length price of international transactions resulting from the advertisement, marketing and sales promotion expenses (hereinafter referred to as 'the AMP expenses') incurred by the appellant on the basis of the order passed by the TPO under section 92CA(3) of the Act.*

*2.1 That the DRP/TPO erred on facts and in law in not appreciating that expenditure on advertisement and brand promotion, unilaterally incurred by the appellant, could not be regarded as a 'transaction' in the absence of any understanding / arrangement between the appellant and the associated enterprise.*

*2.2 The DRP/TPO erred on facts and in law in not appreciating that the AMP expenses, etc., unilaterally incurred by the appellant in India could not be characterized as an international transaction as per section 92B, in the absence of any proved understanding / arrangement between the appellant and the associated enterprise, so as to invoke the provisions of section 92 of the Act.*

*2.3 That the DRP/TPO erred on facts and in law in not appreciating that in the absence of any understanding / arrangement between the appellant and the associated enterprise, the associated enterprise was under no obligation to reimburse the AMP expenses incurred by the appellant for sale of its products.*

*2.4 The DRPTTPO erred on facts and in law in holding that expenditure incurred by the appellant which incidentally resulted in brand building for the foreign AE, was a transaction of creating and improving marketing intangibles for and on behalf of its foreign AE and further that such a transaction was in the nature of provision of a service by the appellant to the AE.*

*2.5 That the DRP erred on facts and in law in observing that the entire IP relating to marketing, i.e., customer list, concepts, designs, creative thinking, music, graphics, TV spots, films, etc. are owned by the associated enterprise.*

*2.6 That the DRP erred on facts and in law in observing that the expenditure on AMP creates advertisement, which creates long term asset, the ownership of which vests with the taxpayer and, therefore, the contention of the appellant that such AMP expenses were incurred on its own account, is contradicted by fact.*

*2.7 That the DRP/TPO erred on facts and in law in not appreciating that since the appellant was performing the key people/critical decision making functions with regard to advertisement and marketing activity, the risk related to such activity ought to have been borne by the applicant.*

*2.8 That the DRP erred on facts and in law in holding that in the transactions between the appellant and the associated enterprise, it is the associated enterprise which is operating as an entrepreneur.*

*2.9 That the TPO erred on facts and in law in re-characterizing the appellant as a distributor and not as a manufacturer.*

*2.10 That the DRP erred on facts and in law in holding that Adidas Salomon group of AEs are intricately associated with the manufacturing function and goods have been purchased by the appellant from contract manufacturer as per the specification provided by the AE and hence the appellant could not be regarded as an independent manufacturer.*

*2.11 That the DRP erred on facts and in law in holding that between appellant and the associated enterprise, the latter is the entrepreneur and the vital function of the marketing should actually be carried out by the associated enterprise, being the entrepreneur, which function has been assigned to the appellant.*

*2.12 That the DRP/TPO erred on facts and in law in not appreciating that adjustment on account of allegedly excess AMP expenses is unwarranted in the case of the appellant, a full risk bearing entrepreneur.*

*2.13 That the DRP/TPO erred on facts and in law in re-characterizing the appellant, a full risk bearing entrepreneur, as a limited risk service provider entitled to cost plus remuneration for its marketing efforts.*

*2.14 That TPO / DRP erred on facts and in law in not appreciating that such a Transfer Pricing adjustment could not at all be made in respect of AMP expenses which were found to constitute legitimate, bonafide and deductible business expenditure and the appellant was the economic owner of the benefit of such expenses.*

*2.15 That the DRP erred on facts and in law in holding that the marketing intellectual property such as customer list etc. is owned by the associated enterprise, not appreciating that by virtue of agreements entered into with Indian distributors, the appellant owns the distribution network in India.*

*2.16 That the DRP erred on facts and in law in holding that "the TPO has brought sufficient material on record to justify that the taxpayer had entered into the exercise of development of marketing intangibles for its AE by incurring of expenditure as well as by application of services without being suitably compensated".*

*2.17 That the DRP erred on facts and in law in holding that fall in the gross profit margin of the appellant shows that the AMP expenditure is incurred for the benefit of the associated enterprise and not the appellant.*

*2.18 That the DRP erred on facts and in law in holding that the huge AMP expenditure incurred by the taxpayer is not benefitting it in terms of GP or NP and is for the benefit of the AEs.*

*2.19 That the DRP erred on facts and in law in holding that the appellant is not operating as an independent manufacturer.*

*2.20 That the DRP erred on facts and in law in observing that the AE of the appellant was involved in formulation of AMP policy by way of its association at every stage of formulation of marketing strategy and the averment of the appellant that marketing exercise carried out by it is independent of the AE, was incorrect.*

*2.21 That the DRP erred on facts and in law in holding that the associated enterprise is involved in formulation of AMP policy of the appellant, not appreciating that such involvement of the associated enterprise is only in the nature of assistance provided by the associated enterprise and the ultimate discretion rests with the appellant.*

*2.22 That the DRP erred on facts and in law in referring to the license agreement and inferring that the appellant is carrying the marketing activity at the behest of the associated enterprise, not appreciating that the terms of the license agreement were comparable with third party agreements entered into by the associated enterprise.*

*2.23 That the DRP erred on facts and in law in drawing unwarranted inferences from the loss incurred by the appellant without substantiating as to how such losses resulted in benefit to the associated enterprise.*

*2.24 That the DRP erred on facts and in law in confirming the adjustment made by the TPO with regard to the AMP expenses holding that (i) no independent person, would forego the compensation for the additional marketing activities undertaken by the appellant, (ii) the AE needs to compensate the appellant as it had been found that the appellant had incurred excessive AMP expenses, and development and promotion of a brand in India directly benefitted the AE also.*

*2.25 That the assessing officer/ TPO erred on facts and in law in rejecting the transaction by transaction analysis undertaken by the appellant wherein closely linked transactions were benchmarked together and instead segregating closely linked transactions for the purpose of benchmarking.*

*2.26 Without prejudice that the DRP/TPO erred on facts and in law, in not appreciating that the AMP expenses incurred by the appellant was appropriately established to be at arm's length applying TNMM.*

*2.27 That the TPO/DRP erred on facts and in law in holding that at the time of introduction in the Indian market, the Adidas brand had no value in India.*

*2.28 That the assessing officer / TPO erred on facts and in law in making Transfer Pricing adjustment in respect of AMP expenses without applying any of the method prescribed under section 92C of the Act.*

*2.29 The Dispute Resolution Panel (DRP)/TPO erred on facts and in law in not appreciating that the only Transfer Pricing adjustment permitted by Chapter X of the Act was in respect of the difference between the arm's length price (ALP) and the contract or declared price, but the said provision could not be invoked to determine the 'quantum' / extent of business expenditure.*

*2.30 That the assessing officer erred on facts and in law in not appreciating that the power of the TPO is restricted to the determination of arm's length price of international transactions by applying one of the prescribed method as the most appropriate method and not to make disallowance of business expenses incurred by the appellant.'*

*2.31 The DRP/TPO erred on facts and in law in applying Bright Line Test ("BLT") for computing adjustment on account of expenditure on advertisement and brand promotion expenses, without appreciating that in absence of specific provision in the Transfer Pricing statutory provisions in India, adjustment on account of the arm's length price of the advertisement and brand promotion expenses could not be made.*

*2.32 Without prejudice, that the TPO/DRP erred on facts and in law in rejecting the analysis undertaken by the appellant by applying the Comparable Uncontrolled Price ('CUP') method.*

*2.33 That the DRP/TPO erred on facts and in holding that CUP analysis cannot be relied upon in view of difference in markets without placing on record any evidence to substantiate that difference in markets has an influence on the AMP/Sales ratio.*

*2.34 That the DRP/TPO erred on facts and in law in disregarding the CUP analysis conducted by the appellant on the basis of third party license agreements, holding that the appellant has not provided the data with respect to price at which goods are purchased from the AEs without appreciating that such transaction was accepted to be at arm's length by the Transfer Pricing Officer.*

*2.35 Without prejudice, that the DRP erred on facts and in law in not appreciating that the compensation with respect to the marketing function was built in the lower price at which the goods were purchased by the appellant from the associated enterprise.*

*2.36 That the DRP / TPO erred on facts and in law in not excluding the discounts and selling expenses aggregating to Rs. 200,507,000 from the quantum of AMP expenditure, allegedly holding that "the question being investigated is "marketing intangible' and not just "brand promotion" alone in the instant case.*

*2.37 Without prejudice that the DRP/TPO erred on facts and in law in not considering appropriate set of comparables for undertaking benchmarking analysis of the alleged international transaction arising out of AMP expenditure incurred by the appellant.*

*2.38 Without prejudice that the TPO erred on facts and in law in rejecting the following companies from the comparable set identified by the appellant holding that the appellant has not provided the search criteria:*

| *Company names* | *AMP/Sales* |
|---|---|
| *Cantabail Retail India Ltd* | *21.30%* |
| *Color Plus Fashions Ltd* | *18.32%* |
| *Cotton County retail Ltd* | *11.77%* |
| *Dollar Industries Ltd* | *20.66%* |
| *Globus Stores* | *4.88%* |
| *Kewal Kiran Clothing Ltd* | *16.11%* |
| *Koutons Retail India Ltd* | *18.73%* |
| *Liberty Shoes Limited* | *7.69%* |
| *Lux Industries Ltd* | *15.59%* |
| *Madura Garments* | *5.99%* |
| *Raymond Apparel Ltd* | *13.26%* |
| *Relaxo Footwears Limited.* | *10.42%* |
| *Rupa & Company Ltd* | *11.37%* |
| *Shoppers Stop Ltd* | *3.39%* |
| *Trent Limited* | *15.87%* |
| *Average* | *13.02%* |

*2.39 That the DRP erred in facts and in law in carrying out fresh search of comparable companies for benchmarking the AMP expenses.*

*2.40 Without prejudice, that the DRP erred on facts and in law in including following companies in the comparable set which are not owning/exploiting any domestic brand name:*

| *Company Name* | *AMP/Sales* |
|---|---|
| *Addi industries Ltd* | *12.76%* |
| *Cantabal Retail India Ltd* | *21.30%* |
| *Koutons Retail India Ltd* | *18.73%* |
| *Lux Industries Ltd* | *15.59%* |
| *Zodiac Clothing Co. Ltd* | *13.48%* |
| *Kewal Kiran Clothing Ltd* | *16.11%* |
| *Raymond Apparel Ltd* | *13.26%* |

| *Company Name* | *AMP/Sales* |
|---|---|
| *Color Plus Fashions Ltd* | *18.32%* |
| *Cotton County retail Ltd* | *11.77%* |
| *Dollar Industries Ltd* | *20.66%* |
| *Rupa & Company Ltd* | *11.37%* |

| | |
|---|---|
| *Relaxo Footwears Limited.* | *10.42%* |
| *Lakhani India Ltd* | *3.37%* |
| *Liberty Shoes Limited* | *7.69%* |
| *Sanspareils Greenland Pvt. Ltd* | *4.25%* |
| *Arithmetic Mean* | *13.27%* |

*2.41 That the TPO/DRP erred on facts and in law in holding that the appellant has rendered service to the AEs by incurring the AMP expense and by holding that markup has to be earned by the appellant in respect of the AMP expenses, alleged to have incurred for and on behalf of the AE.*

*2.42 Without prejudice, the TPO/DRP erred on facts and in law in not appreciating that markup, if at all, had to be restricted to the value added expenses incurred by the appellant for providing the alleged service in the nature of brand promotion.*

*2.43 That the /TPO erred on facts and in law in applying a markup of 14.88% on the alleged excess AMP expenditure incurred by the appellant, while computing the value of compensation to be received by the appellant on account of promotion of 'Adidas' brand.*

*2.44 Without prejudice, that the TPO erred on facts and in law in not restricting the mark up to Prime Lending Rate ('PLR') of State Bank of India ('SBI') plus a margin of 150 basis points, despite the direction of DRP to this effect.*

*2.45 Without prejudice, the assessing officer/DRP erred on facts and in law in not appreciating that markup, if at all, had to be restricted to the value added expenses incurred by the appellant for providing the alleged service in the nature of brand promotion.*

*2.46 Without prejudice, that the TPO /DRP erred in not appreciating that the associated enterprise has already compensated the appellant by allowing a royalty free use of brand 'Adidas' and by providing loans at concessional rates.*

***Corporate Tax Addition:***

*3. That the assessing officer / DRP erred on facts and in law in making addition of Rs.90,92,57,478 to total income, on account of insurance compensation received by Adidas AG, the ultimate parent/holding company of the appellant, towards erosion of financial interest held in the appellant, due to loss of appellant's stake in fire at appellant's premises in India, alleging the same to be income of the appellant for the assessment year under consideration.*

*3.1 That the assessing officer / DRP erred on facts and in law in holding that the amount of insurance compensation received by Adidas AG under an independent insurance policy taken by that company with a foreign insurance company, viz., Zurich Insurance was income of the appellant, since the amount of insurance was computed with reference to the loss of business assets suffered by the appellant in India in fire.*

*3.2 That the assessing officer / DRP erred on facts and in law in holding mat if the aforesaid amount of compensation was reflected as income of the appellant and consequently credited to its profit and loss account, there would have been no reduction in the value of financial merest held by Adidas AG in the appellant, warranting payment dependent compensation outside India.*

*3.3 That the assessing officer / DRP erred on facts and in law in holding that since the impugned amount of insurance money became due on account of loss of stock lying with the appellant in India, which constitutes a business connection or property or asset or source of income in India, such income would be deemed to accrue or arise in India in the hands of the appellant under section 5 read with section 9(1 )(i) of the Act.*

*3.4 That the assessing officer / DRP erred on facts and in law in relying upon and misconstruing certain e-mails exchanged between appellant's and Adidas AG personnel and communication of independent consultant(s), to hold that the insurance claim received by Adidas AG belonged to the appellant and was taxable in India.*

*3.5 That the assessing officer / DRP erred on facts and in law in holding that the impugned transaction/insurance contract entered between Adidas AG and an independent foreign insurance company, to cover the loss of financial interest held by Adidas AG in the appellant company and receiving the insurance money abroad was a colourable device adopted to evade taxes in India.*

*4. That the assessing officer erred on facts and in law in levying interest under Section 234B and Section 234C of the Act."*

**2.** The assessee also filed additional grounds of appeal on 22/11/2018 alongwith date chart from filing of income tax return to the date of passing the final assessment order as under:

*"That on the facts and circumstances of the case and in law, the impugned order passed by the Assessing Officer is barred by limitation and therefore, is liable to be quashed."*

**3.** However, before us, the additional ground was not pressed by the Ld. counsel of the assessee and therefore, same is dismissed as infructuous.

**4.** The brief facts of the case are that:

(i) The assessee company is engaged in the business of sourcing, distribution and marketing of products of brand-name "Adidas" in India. The assessee company was incorporated in the year 1995 under the Companies Act, 1956 with 98.99 percentile shares of the assessee company held by the Adidas India Private Limited, which is in turn is a subsidiary of M/s. Adidas AG, Germany.

(ii) The assessee filed its original return of income on 15/10/2010 declaring a loss of Rs.12,61,27,241/-. The return of income was revised on 27/03/2012 declaring loss of Rs.12,61,25,995/-. The case was selected for scrutiny and a notice under section 143(2) of the Income-tax Act, 1961 (in short 'the Act') was issued and complied with.

(iii) During the course of assessment proceeding, the Ld. Assessing Officer observed following international transactions carried out by the assessee with its Associated Enterprises (AEs):

| *International transactions* | *Method* | *Value (Rs.)* |
|---|---|---|
| *Receipt of Commission by Adidas International Trading –ABV* | *CUP* | *2,56,55,345* |
| *Receipt of Commission by adidas* | *CUP* | *6,96,807* |

| | | |
|---|---|---|
| *International Trading –sample purchase* | | |
| *Import of Finished Products for Resale in India (traded goods by adidas International Trading)* | *CUP* | *40,02,92,546* |
| *Other than adidas International Trading BV* | | *7,31,18,713* |
| *Purchase of other products* | *No Bench-marking required* | *10,70,552/-* |
| *Reimbursement of Expenses by Associated Enterprises* | *No Bench* | *41,24,636* |

(iv) The Ld. Assessing Officer referred the matter of determination of Arm's Length Price (ALP) of those international transactions to the learned Transfer Pricing Officer (TPO). The learned TPO after taking into consideration submission of the assessee, was of the view that the assessee was engaged in brand building and marketing of "Adidas" products in India and thus incurred a cost in connection with the benefit and the services provided to the 'AEs' under a mutual agreement with the Indian entity i.e. Adidas India Private Limited, but the same being merely a shell entity, the benefit of the expenditure incurred on advertising, marketing and promotion (AMP) is flowing to "Adidas" Germany. The AMP expenditure incurred by the assessee was held by the learned TPO /AO to be an international transaction within the meaning of section 92B(1) of the Act alongwith Explanation (i)(b) introduced by way of Finance Act 2012. According to the Assessing Officer, the assessee who is in the business of distribution of goods manufactured by its foreign controlling parent, without owning any trademark or Brand, has performed significant functions like brand

development, market development, marketing customer support, technical and administrative support on behalf of its AEs in India bearing cost, investing huge sum, and using its skilled manpower and time, which has clearly developed marketing intangible for "Adidas" brand and goods manufactured by its foreign AEs and thus the assessee was entitled to get reimbursement of the cost incurred by it, which was in excess of routine distributor and is entitled to retain intangible income in India. The learned TPO observed that the assessee by way of expenditure on promoting " Adidas " brand , developing and maintaining network of sub distributor, dealers, retailers etc., developing efficient after sale service network in creating customer awareness and loyalty by advertisement, organizing events, education, trade shows etc has developed local marketing intangible for its AE. The learned TPO issued show-cause the assessee as why the expenditure over and above (Bright Line Test) the routine marketing promotion and advertisement expenditure should not be held as the services rendered to the AE for development of marketing intangible. The internal CUP proposed by the assessee to benchmark the AMP expenditure incurred by it, was analyzed by the learned TPO and rejected. Before the TPO, the assessee furnished a set of 30 comparables, out of which 15 were rejected by the learned TPO for the reason that those companies were engaged in brand development also. Out of the balance 15 comparables, the learned TPO rejected 3

companies for the reason that the business of those companies was mainly into export market, having the export to total sales exceeding 75% and retained the 12 companies as comparables. The learned TPO considered an expenditure of Rs.23.006 crores as a routine AMP expenditure and expenditure over and above, i.e. (48.55 - 23.006= 25.54 crores), was held to be the expenditure for development of marketing intangibles for the AE. Over this, the learned TPO applied a markup of 14.88%, which was on account of opportunity cost of time and money used (prime lending rate of SBI+3%). Accordingly, the learned TPO applying the "bright line test" proposed adjustment of Rs.25,54,99,511/-on account of international transaction of advertising, marketing and promotion (AMP) expenditure incurred for AEs.

(v) During assessment proceeding, the Assessing Officer also proposed an addition of Rs.90,92,57,478/- on account of insurance compensation pertaining to loss due to fire, received by the "Adidas AG, Germany.

(vi) The Assessing Officer issued draft assessment order, wherein he included the additions proposed for transfer pricing adjustment of AMP expenditure as well as reimbursement of insurance amount received by the AE.

(vii) Aggrieved by the draft assessment order, the assessee filed objection before the Ld. Dispute Resolution Panel (DRP). Before the learned DRP, the assessee contended that the AMP expenditure was incurred wholly and exclusively for the purpose of the business of the assessee

and in absence of any specific provision determination of sufficiency/excessiveness of the AMP expenditure would be arbitrary and prejudicial to the assessee. In view of the submission of the assessee, the learned DRP held that in view of section 92F(v) the transaction include an arrangement, understanding or action in concert, whether or not such arrangement, understanding or action is formal or in writing, the expenditure incurred on AMP for benefiting the AE brand is an international transaction. As far as selection of the comparables for benchmarking the routine AMP expenditure in the line of the business of the assessee, the learned DRP carried out search of few new comparable companies and directed the assessee to verify the result of the said search from the Annual Reports of those comparable companies and provide the same to the learned TPO for verification. The TPO was directed to exclude the companies which were promoting foreign brands. The learned DRP also approved the Bright Line Test for determination of arm's length price of the International transactions of AMP. The learned DRP, accordingly upheld the AMP adjustment proposed by the learned TPO. The learned DRP also upheld the amount of insurance received by the AE as income of the assessee. The learned DRP accordingly issued directions in the order dated 30/12/2014.

(viii) The Ld. Assessing Officer in compliance to the order of the learned DRP passed the final assessment order on 02/02/2015 incorporating addition of Rs.29,35,17,838/-

on account of transfer pricing adjustment and addition of Rs.90,92,57,478/- on account of insurance compensation pertaining to loss due to fire received by the M/s. Adidas AG, Germany.

(ix) Aggrieved with the additions made by the Assessing Officer in the final assessment order, the assessee is before the Tribunal raising the grounds as reproduced above.

**5.** The learned Senior Counsel of the assessee Sh. Ajay Vohra, submitted that ground No. 1 to 1.1 are general in nature and not required to be adjudicated specifically, accordingly same were dismissed as infructuous.

**6.** In respect of ground No. 2 to 2.46, the Ld. Sr. counsel submitted that all these grounds are in respect of transfer pricing adjustment for AMP expenditure. The learned counsel submitted that identical issue of transfer pricing adjustment on account of AMP expenditure has been deleted by the coordinate bench of the Tribunal in the case of the assessee for assessment year 2006-07 in IT No. 3727/del/2014. Accordingly, he submitted that issue in dispute in the year under consideration being identical, the AMP adjustment during the year might also be deleted.

**6.1** The Ld. DR, on the other hand, submitted that the international transaction of AMP exists in the case of the assessee and which may be benchmarked either in the aggregated or segregated manner, if the Bright Line Test is rejected. He accordingly submitted that issue in dispute may be restored to the file of the learned AO/TPO for benchmarking the transaction of AMP in view of the decision of the Hon'ble Delhi High Court in

the case of Sony Ericsson Vs. Dy.CIT, ITA No. 638/2015, dated 28.01.2016

**6.2** We have heard the rival submission of the parties on the issue in dispute. We find that the coordinate bench of the Tribunal (supra) in the case of the assessee itself has discussed the issue of transfer pricing adjustment on account of AMP expenditure and its benchmarking. The relevant finding of the Tribunal is reproduced as under:

> *"8.1.2. We don't deny that there would be incidental benefit to foreign AE, being, Adidas-Saloman AG, which is ultimate parent of assessee. However, expenditure towards advertisement and marketing incurred by assessee in India is mainly for its own benefit to market products manufactured by it in India. Main purpose of incurring of such huge AMP expenses has largely benefited assessee in India, with an incidental benefit arising to foreign AE. Unless Ld.TPO can establish direct benefit accruing to foreign AE, it is very difficult to accept existence of international transaction, under present facts of the case. We rely upon decision of Hon'ble Delhi High Court in case of Sony Ericson Mobile Communication India Pvt. Ltd (supra) in support of afore-stated observations.*
>
> *8.2. Further it has been submitted by both sides that facts and circumstances in present appeal are no manner different with that of Maruti Suzuki India Ltd. Reported in 381 ITR 117; and Soney Ericson Mobile Communications (supra), wherein Hon'ble High Court has held that existence of international transaction must be established de hors the Bright Line Test before undertaking bench marking of AMP expenses. We therefore respectfully follow the view taken by this Hon'ble Delhi High Court in Sony Ericson Mobile Communications (supra), and delete adjustment made in respect of AMP expenses.*
>
> *8.3. However, we appreciate the concern raised by Ld. Sr.DR that decision of Hon'ble Supreme Court will be binding upon assessee as well as revenue.*
>
> *"19. After considering the legal position as discussed in the preceding paragraphs, we are of the considered opinion that the ALP of an international transaction involving AMP expenses, the adjustment made by the TPO/DRP/AO is not sustainable in the eyes of law. At the same time, we cannot ignore the submission of the*

*learned DR that the matter is pending before Hon'ble Apex Court and the decision of Hon'ble Apex Court would be binding upon all the authorities. In view of the above, we set aside the orders of authorities below and restore the matter to the file of the Assessing Officer. We hold that as per the facts of the case and the legal position as of now and discussed above in this order, the adjustment made by the TPO/DRP/AO in respect of AMP expenses is not sustainable. However, if the above decisions of Hon'ble Jurisdictional High Court which is under consideration before the Hon'ble Apex Court is modified or reversed by the Hon'ble Apex Court, then the Assessing Officer would pass the order afresh considering the decision of Hon'ble Apex Court. In those circumstances, he will also allow opportunity of being heard to the assessee."*

*Accordingly Grounds 2 to 2.24 stand allowed for statistical purposes."*

**6.3** The issue in dispute involved in present appeal before us being identical to the issue decided by the Tribunal, we, respectfully following the said decision of the Tribunal, set aside the orders of the Authorities below and restore the matter to the file of the AO/TPO to take action in the instant year following the direction of the Tribunal (supra) in para 8.3 for assessment year 2006-07. The grounds of appeal from 2 to 2.46 are accordingly allowed for statistical purposes.

**7.** In ground Nos.3 to 3.5, the assessee has raised issue of addition of Rs.90,92,57,478/- made by the AO in respect of amount of 'insurance compensation' pertaining to fire, received by the Adidas AG.

**7.1** The brief facts in respect of the issue in dispute are that a survey action under section 133A of the Act was carried out by the Investigation Wing of Income Tax Department, New Delhi on 20/12/2010 at the premise of assessee's company located at plot

No. 93, Sector 32, Institutional Area, Gurgaon. In the survey, it was observed that in a fire accident in one of the go-down of the assessee on 22/06/2009, the assessee lost stock costing Rs.72 crores approximately, besides fixed assets such as racks, computers etc. The assessee was having fire insurance policy with M/s Bajaj Allianz General Insurance (in short 'Bajaj Allianz') having coverage of Rs.50 crores for stock-in-trade and Rs.24 crores for all fixed assets lying in the warehouse etc. Bajaj Allianz settled the claim of the assessee at approximately Rs.47 crore for stoc-in-trade and Rs.1.25 crores for the fixed assets. During the survey, it was also observed that the Adidas AG, Germany, the ultimate holding company of the assessee, was having a Global Insurance Policy (GIP) with M/s Zurich Insurance. Total claim of Euro 2,08,91,604/- was sanctioned to M/s Adidas AG, out of which Euro 1,37,52,599/- (approximately Rs. 91 crore) was received by M/s Adidas AG after subtracting the claim of Euro 71,39,005 (approximately Rs. 47 crore) by the assessee in India from the Indian insurer (i.e. Bajaj Allianz).

**7.2** According to the Assessing Officer, this overseas policy (GIP) was also in respect of the stock of the assessee. It has been mentioned by the Assessing Officer that insurance in India in respect of the stock was on cost, whereas the insurance taken by the Adidas AG with the overseas insurer on the stock of the assessee was at the selling price. However, this fact has been disputed by the assessee and according to the assessee, this policy was to cover loss of financial interest due to erosion of economic values of subsidiaries and thus the claim received by

the assessee and the overseas entity were for different interest insured.

**7.3** The learned Assessing Officer also referred to documents found during the course of survey indicating exchange of emails between the officials of the overseas insurer and the officials of Adidas AG. The Ld. Assessing Officer has referred to email dated 21/04/2010 from Mr. Schmitt Dieter to Mr. Felix with CC to Mr. Andreas Geliner and Mr. Marcus Reichel, wherein it is written that from the insurance prospective all payments relating to physical loss, business interruption and mitigation cost belongs to Adidas India (i.e. the assessee). An another email written by Mr. Sonja Dachacher to Mr. Andreas Gellner, MD of the assessee company has been referred by the Assessing Officer, which contained an attachment mentioning that the entire claim excluding the tax levied needs to be reflected in Adidas India (i.e., the assessee). There is another email from Mr. Gaurav Mehndiratta, partner in KPMG to Mr. Andreas Gellner, MD of the assessee company, according to which the Adidas AG wanted to transfer the compensation amount in question to the assessee and was looking for the possible option for infusing those funds in Indian subsidiary. In view of these emails, the Assessing Officer was of the view that the money received in insurance claim abroad by the Adidas AG was the money of the assessee as this was the compensation for loss suffered by the assessee. According to the Assessing Officer, there is a direct business relationship of the overseas compensation received with the business activities of the assessee in India and the insurance claim received abroad should have been offered for taxation by the assessee in India.

The submissions filed by the assessee in this respect were rejected by the Assessing Officer with detailed reasoning given in his order. Those reasons are summarized as under:

1. According to the email correspondence found during the course of the survey, the compensation received as insurance claim is the money belonging to the assessee being compensation for loss of the goods of the assessee.
2. Any compensation received from the insurer in respect of the stock of the assessee destroyed in fire should be added to the income of the assessee.
3. The separate insurance policy was taken by the parent company to avoid any tax incidence in India on the portion received abroad.
4. The compensation received by Adidas AG has its genesis in India.
5. According to section 5 of the Act, total income of tax resident, including the income accrue or arise outside India is required to considered for taxability in India and mere fact that assessee could not receive ultimately the money in India due to some internal discussion or issues that may come up, would not be a ground against income being accessible in India.

**7.4** Before the Ld. DRP, the assessee made detailed submissions contesting that insurable interest into two policies, one taken by the assessee and another taken by 'Adidas AG' are different. It

was contended that the assessee had never been a contracting party to the GIP and therefore, due to privity of contract between two foreign parties, no contractual legal right inures to the assessee company. It was also submitted that no inter-company charges or cost allocation was made by the Adidas AG towards the assessee and the Adidas AG had borne the entire cost of GIP while the assessee has born cost of the local insurance with Bajaj Allianz. It was further submitted that compensation received by the Adidas AG outside India has been included in the taxable income of the Adidas AG in Germany. The assessee submitted that the expression "accrue" means to become a present and enforceable right and to become present right of demand. According to the assessee income accrues only when the taxpayer acquires the right to receive it and in the present case there is no actual or constructive receipt of income in the hands of the assessee. The assessee submitted that email correspondence cannot justify taxability of the compensation and the tax liability is based on accrual and arising of income and receipt is not the only test to tax an income. Relying on the decision of Sutron Corporation Vs Director of Income Tax (2004) 268 ITR 156 (Del), the assessee submitted that place of accrual depends on the place of formation of the contract and the place where contract is carried out. Further, relying on the decision in the case of CG Krishnaswami Naidu Vs. CIT (1968) 62 ITR 686 ( Mad.), it was submitted that income accrues at a place where right to receive the same arises. In view of the decisions relied, the assessee submitted that there is no right to receive income in the hands of the assessee and income if any has been received, earned,

accrued and taxed in the hands of the Adidas AG in Germany and the assessee did not have any right to receive the compensation from the same in India and the said compensation cannot by any stretch of imagination brought to tax in the hands of the assessee in the garb of section 5(1)(c) of the Act.

**7.5** The Ld. DRP examined the ownership structure of the assessee and activities carried out by the assessee as well as the group companies. The Ld. DRP also analyzed the claim of insurance received by the Adidas AG. The Ld. DRP observed that 'Zurich Insurance' has accepted the claim based upon the value of the asset destroyed in the fire. The Ld. DRP further observed that taxability of compensation for lost profit or income receipt is based upon the "Surrogatum Principal", which provides that the character of receipt or an award of damages or an amount received in settlement of a claim as a capital or income receipt is depends on what the amount was intended to replace, so that if the replaced amount would have been taxable in the recipient hands, the award settlement amount will also be taxable. The Ld. DRP accordingly concluded that amount received against insurance policy is chargeable to tax under the Act as income, as it is inseparably connected with the conduct of the business, the assets employed therein and the compensation for the loss of the profit from the business. The Ld. DRP referred to section 5(1)(c) of the Act and section 9(1), which prescribed the income which shall be deemed to accrue or arise in India. The learned DRP observed that the income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or

source of income in India, or through the transfer of the capital asset situated in India, is would deem to accrue or arise in India. The learned DRP held that compensation was through or from any business connection in India because the impugned income has been due to the loss sustained on the fire of the stock, profit which could have been earned on such a stock when sold, the loss suffered on other assets and other incidentals. According to the learned DRP, the property in ordinary sense includes both movable and immovable and thus the income of compensation was also through or from any property in India. The learned DRP also held that the income was through or from any asset or source of income in India due to the reason that loss sustained on fire of the stock, profit which could have been earned on such a stock when sold, the loss suffered on other assets and other incidentals, which are part and parcel of the business carried on by the assessee in India. The learned DRP accordingly concluded in para 5.5.9 on the taxability of income in the hands of the assessee as under:

> *"5.5.9 From the, discussion made above, it is evident that the impugned receipts are clearly covered under section 5(1 )(i) of the Act and when read in association with section 5(1)(b) of the Act, the impugned receipt will be a part of the total income chargeable to tax in the hands of the taxpayer. The obligation to pay such amount by the Insurance Company has arisen with the very source of income, namely, the stock in goods held by AIMPL (and not by 'adidas AG') and therefore, the amount paid constitutes income of AIMPL. Moreover, in the e-mail from Schmitt Dieter to Felix with cc to Andreas Gellner and Marcus Reichel dated 21.4.2010, it has been clearly mentioned by Schmitt Dieter that:*
>
> > *'from the insurance perspective, all payments relating to the physical loss, business interruption and mitigation cost belong to Adidas India.'*

*It is relevant to mention that Mr. Andreas Gellner is the Managing Director of the taxpayer company whereas Mr. Schmitt Dieter is an executive in the Global Insurance Department of adidas Group based in Germany. The Panel holds that when Mr. Schmitt Dieter has been narrating and intimating that from the insurance perspective such payments belong to adidas India/ AIMPL, the view of the taxpayer that these belong to' 'adidas AG' is not correct. Under these facts the Panel holds that the reliance placed by the taxpayer or decision of the Canadian Supreme Court and on the'-Insurance law (referred in para 5.3.1 above) has no significance in so far as the facts and circumstances of the case are concerned."*

**7.6** The learned DRP rejected the contention of the assessee that section 25 of the General Insurance Business Act, 1972, prohibits insurance of properties in India by an insurer, located outside India. According to the learned DRP with prior permission from the government, the foreign insurer can also insure properties in India. The learned DRP emphasized that this fact could not be decisive factor for conclusion that the consideration received could not be taxable in India in the hands of the entity which is actually carrying out the relevant business. The learned DRP brought on record that the compensation was computed with reference to the actual loss sustained and not with reference to the reduction in values of investment of Adidas AG. The Ld. DRP is also of the view that the financial interest of Adidas AG or the value of the shares of the assessee would have been protected if the amount of compensation had been transferred to the assessee. The learned DRP is in agreement with the finding of the AO that the assessee devised a mechanism of tax evasion. In view of the above discussion, the learned DRP upheld the finding of the Assessing Officer.

**7.7** Before us, the learned Senior Counsel of the assessee filed a paper-book containing pages 1 to 717 and reiterated the facts

related to the issue in dispute. The learned senior counsel referred to a copy of General Insurance Policy taken by the assessee with M/s Bajaj Allianz, which is available on pages 559-588 of the paper book. He also referred to the insurance claim received of Rs. 47 crores towards loss of stock and Rs. 1.25 crores received towards loss of fixed asset from Bajaj Allianz (BA). The Ld. Senior Counsel also referred to a copy of Global Insurance Policy (GIP) covering loss of financial interest due to erosion of economic value of its investment in subsidiary companies across the globe including the assessee with an overseas insurance company, i.e, M/s. Zurich insurance, which is available on page 272 to 556 of APB-II. The learned Senior Counsel also referred to details of insurance claim received by Adidas AG under the GIP of Euro 1,37,52,599 (approximately Rs.91 Crores) from Zurich insurance, available on pages 592 to 606 of the APB-II. The learned Sr. Counsel also filed a written synopsis in the case.

**7.8** The learned Sr. counsel submitted before us that two insurance policies, i.e., the policy taken by the assessee and the policy taken by the Adidas AG are in respect of two different interest insured. According to the learned counsel, the GIP covered financial interest of the Adidas AG in subsidiary and not the assets owned by the subsidiary. The learned counsel referred to various features of the GIP. He submitted that as per Germany Law: "a subsidiary situated in a country which does not permit Zurich to be a coinsurer will have to take an independent local policy with a domestic insurer. In such a case, the GIP does not cover the assets owned by a subsidiary but the financial interest

of Adidas AG in such a subsidiary. The extent of obligation for payment of compensation, under GIP, in such a case is computed after excluding the value of risk covered under the local policy from the total value of erosion of financial interest of Adidas AG in subsidiary.

**7.9** Regarding the insurance policy taken by the assessee, the learned counsel submitted that it was exclusively to cover the risk arising out of loss of stock and fixed assets owned by it. According to him, premium for the local insurance policy is borne and payable/paid by the assessee to BA in Indian rupees within India. BA's obligation is only to compensate the assessee for cost of stocks destroyed and not for 'loss of profits' or loss on account of disruption of business. Further, the said insurance policy in place is subject to maximum cover of Rs. 50 crores even if the cost of goods destroyed in fire exceeds the limit of Rs. 50 crores. Compensation was payable by BA exclusively to the assessee in Indian rupees only and Adidas AG was not a party to the contract between BA and the assessee and no right or liability accrues to it. Adidas AG does not have any right to receive any part of compensation either from the assessee or from BA. BA has no obligation to compensate any diminution in the value of insurable interest of Adidas AG.

**7.10** The learned counsel submitted that the Adidas AG had over the years made substantial financial investment in the assessee, which as on 31/03/2010 stood of equity (through the subsidiaries) of Rs. 54.96 crores and interest-free loan (ECB) of Rs. 29 crores. In addition, the Adidas AG had also provided

guaranteed to Indian banks for granting overdraft/working capital loan to the assessee of Rs. 293 crores.

**7.11** It was submitted that the insurable interest of the assessee and Adidas AG under two separate and district contracts of insurance with independent unrelated third-party insurers, for which premium was separately paid by each of the two entities, was distinct and separate. It was submitted that any business loss suffered by the assessee had a direct impact on the various investment made by the Adidas AG in the assessee, including loans and guarantees and it was the aforesaid loss in economic value of the financial interest, considering insurable interest in the case of Adidas AG, which was computed with reference to loss of stock by fire in the hands of the assessee.

**7.12** On the issue that loss of stock of the assessee was not covered under the insurance policy of Zurich insurance is due to regulatory prohibitions, the Ld. senior counsel submitted as under:

> *"The GIP specifically stipulates that Zurich does not cover Adidas Group entities, which are residents in countries where there is a strict prohibition on the domestic insurance laws for a German/foreign insurer to operate. It needs to be borne in mind that in terms of provisions of section 25 of the General Insurance Business (Nationalization) Act, 1972 it was not possible for the Appellant to take out fire insurance policy with Zurich Insurance for the goods lying in stock in the Indian warehouse. The same was also not permitted in terms of Foreign Exchange Management (Insurance) Regulations, 2000 notified vide Notification No. FEMA 12/2000-RB dated 3rd May, 2000. Consequently, Zurich is not permitted to, and therefore, could not, cover the goods owned by appellant in India due to the provisions of the General Business (Nationalization Act), 1972 and Foreign Exchange Management (Insurance) Regulations, 2000. It would have been illegal for it to do so because it would have been in contravention of the Indian laws. The Appellant, therefore, was not covered under the GIP and is not entitled to any benefits therefrom. This is clearly mentioned in*

*Clause D.1 & D.1.1 on page 202 of the English translation of the GIP. The said clause reads as under:*

*D MASTER COVER FOR GROUP COMPANIES OUTSIDE GERMANY (See however special regulation for USA/Canada and France)*

*D.1 Object of insurance*
*Co-Insured are*

*D.1.1 All foreign Yours sincerely, of the Adidas Group*

*No co-insured are all subsidiary companies, which have their headquarters in counties, which prohibit the operating of the insurance business through an insurer not permitted there (permit reservation).*

*So far due to this reason a co-insurance cover over this GIP is not allowed, the insurance cover exists in favour of the insurant according to the conditions for "insurance of financial interest" according to pat IV.*

*It was, thus, not possible for Adidas AG to insure goods that it did not own directly. This was because the German company had no insurable interest in those goods under German law. Adidas AG cannot procure a policy that directly covers loss of property owned by another company, even its subsidiaries. However, Adidas AG had an insurable interest in its own capacity for the value of its financial interest in AIMPL. It therefore obtained financial loss insurance in the form of liability insurance that covers Adidas AG's financial interest in AIPL.*

*Accordingly, it cannot be held that the GIP was a contract taken out by Adidas AG with Zurich Insurance (for which premium was undisputedly paid by Adidas AG), for and on behalf of the Appellant, in violation of Indian regulations."*

**7.12** Regarding the substantial financial interest of Adidas AG in assessee, which was insurable interest as per insurance law in Germany, the learned counsel submitted as under:

*"The SIP specifically stipulates in Part IV of GIP that the insured is solely Adidas AG. Zurich provides cover to Adidas AG in the event its financial interest in an overseas subsidiary is adversely affected. The compensation settled under the GIP is for diminution in the*

*financial interest of Adidas AG in AIMPL after adjusting the loss compensated by BA. It is in accordance with the German law.*

*Furthermore, the GIP stipulates a measurement approach of Adidas AG's financial loss by reference to AIMPL's loss. This "agreed value" approach, in which Zurich and adidas AG agree, in advance, on the value of Adidas AG's financial interest in AIMPL, is legally enforceable in Germany.*

*In view of the above, it is clear that Adidas AG had substantial financial interests in the Appellant, which was insurable interest as per insurance laws in Germany, the diminution in which could have been insured by Adidas AG in its own right with an insurer in Germany."*

**7.13** The Ld. counsel in support of his contention relied on the decision of the Court of Appeal for Ontario, Canada in the case of Kossmopoulos Vs, Constitution insurance company (1987) 1 SCR 2 and decision of Authority for Advance Ruling in the case of Aker contracting FP ASA, In Re. 381 ITR 489.

**7.14** According to the learned counsel, the GIP was entered between Adidas AG and Zurich insurance, and the preview of contract was between the said two parties, without assessee being a party at the 1st place, not having any right or obligation under that insurance policy. The learned counsel submitted that it was Adidas AG, who was responsible for paying the premium in respect of Zurich Insurance policy which was renewed from year-to-year.

**7.15** The Ld. counsel relying on the decision of the Hon'ble Supreme Court in the case of ED Sassoon & Co. Ltd Vs CIT 26 ITR 27 (SC) submitted that an income can be said to have accrued to an assessee only when that is vested in the recipient unconditional aned absolute right to receive such income from the person liable to make the payment. The learned counsel

submitted that applying the aforesaid principle of accrual of income, in the present case since the GIP was between the Adidas AG and Zurich insurance company, the assessee had not acquired any right to receive claim of compensation in the GIP and thus question of accrual of income in the hands of the assessee does not arise.

**7.16** The learned counsel further argued that the assessee was not entitled to receive more than the sum insured and submitted as under:

> *"Further, it is settled that the contract of insurance cannot be a source of profit, i.e., the insured cannot be compensated in excess of the loss suffered. It is for that reason that the insurer is subrogated to the rights and remedies of the insured, once the claim is settled by the insurer. The aforesaid proposition has been lucidly laid down by the Constitution bench of the apex Court in Economic Transport Organization, Delhi vs. Charan Spinning Mills Private Limited and Another : (2010) 4 SCC 114 @ Page 132 of the judgment, the Hon'ble Supreme Court observed as under:*
>
> > *"15. A contract of insurance is a contract of indemnity. The loss/damage to the goods covered by a policy of insurance, may be caused either due to an act for which the owner (assured) may not have a remedy against any third party (as for example when the loss is on account of an act of God) or due to a wrongful act of a third party, for which he may have a remedy against such third party (as for example where the loss is on account of negligence of the third party). In both cases, the assured can obtain reimbursement of the loss, from the insurer. In the first case, neither the assured, nor the insurer can make any claim against any third party. But where the damage is on account of negligence of a third party, the assured will have the right to sue the wrongdoer for damages; and where the assured has obtained the value of the goods lost from the insurer in pursuance of the contract of insurance, the law of insurance recognizes as an equitable corollary of the principle of indemnity that the rights and remedies of the assured against the wrongdoer stand transferred to and vested in the insurer.*
> >
> > *16. The equitable assignment of the rights and remedies of the assured in favour of the insurer, implied in a contract of*

*indemnity, known as "subrogation", is based on two basic principles of equity:*

*(a) No tortfeasor should escape liability for his wrong;*
*(b) No unjust enrichment for the injured, by recovery of compensation for the same loss, from more than one source.*

*The doctrine of subrogation will thus enable the insurer, to step into the shoes of the assured, and enforce the rights and remedies available to the assured.*

*17. The term "subrogation" in the context of insurance, has been defined in Black's Law Dictionary thus:*

*"The principle under which an insurer that has paid a loss under an insurance policy is entitled to all the rights and remedies belonging to the insured against a third party with respect to any loss covered by the policy."*
*.....*
*26. Subrogation, as an equitable assignment, is inherent, incidental and collateral to a contract of indemnity, which occurs automatically, when the insurer settles the claim under the policy, by reimbursing the entire loss suffered by the assured. It need not be evidenced by any writing. But where the insurer does not settle the claim of the assured fully, by reimbursing the entire loss, there will be no equitable assignment of the claim enabling the insurer to stand in the shoes of the assured, but only a right to recover from the assured, any amount remaining out of the compensation recovered by the assured from the wrongdoer, after the assured fully recovers his loss. To avoid any dispute with the assured as to the right of subrogation and extent of its rights, the insurers usually reduce the terms of subrogation into writing in the form of a letter of subrogation which enables and authorises the insurer to recover the amount settled and paid by the insurer, from the third-party wrongdoer as a subrogee- cum-attorney."*

*Drawing support from the aforesaid judgment, it would be appreciated that the Appellant could not have recovered the sum of Rs.47 crores from Bajaj Allianz General insurance (Indian insurer) and also Rs.90.92 crores from Zurich Insurance for the loss of stock due to fire - the same would amount to unjust enrichment to the insured by recovery of compensation in excess of the loss sustained (for the same loss) from more than one source.*

*It is further pertinent to point out that the Appellant had insured its stock for a value of Rs.50 crores. The claim from the insurance company for loss of such stock could, at the highest, be in the*

*amount of Rs.50 crores. The Appellant could not have expected to receive anything more and above the amount of Rs.50 crores for such loss sustained. In that view of the matter, too, receipt of Rs. 90.92 crores received by Adidas AG from Zurich Insurance which is sought to be imputed as belonging to the Appellant (alleged to be received by Adidas AG on behalf of the Appellant) would be impermissible in terms of the insurance taken out by the Appellant."*

**7.17** On the issue of emails correspondence impounded during the survey from the premises of the assessee, the Ld. Senior counsel submitted as under:

*The first e-mail dated 21.4.2010 which is written by Mr. Dieter Schmitt/Marcus Reichel, being the Executives of Insurance Department of Adidas AG to the Appellant.*

*The aforesaid e-mail was written by Insurance Department of Adidas AG to the executives of the Appellant, in relation to the settlement of insurance claim of Adidas AG under GIP, after the settlement of insurance claim of the Appellant with BA. Accordingly, the aforesaid correspondences were exchanged with reference to the claim under GIP to be settled by Zurich Insurance Co. in favour of Adidas AG in respect of insurable interest of Adidas AG, i.e., financial exposure in Appellant. Since the amount of compensation under the GIP was the loss of profit remaining after compensation received by the Appellant in India, which compensation could have been determined only after the exact figure of compensation payable by BA was finally known references to compensation paid by BA to the appellant have been made in the correspondences.*

*It was in the aforesaid context, i.e., to determine amount payable in Germany after reducing the amount paid in India out of the total loss that the e-mail was written. The reference made to the accrual of income in India or Germany or tax liability were out of context and were in any case not determinative of the accrual of income and tax liability thereon as per laws of Germany and India. As pointed above, the e-mail was written by officers of Adidas AG, who may be expert in insurance laws but not expert in taxation laws, much less Indian tax laws.*

*The Supreme Court in Saraswati Industrial Syndicate: 237 ITR 1 held that opinion of a person who is an expert on the subject can alone be relied on. Therefore, the 'understanding' of the executives of Adidas Risk GMBH that "the entire claim excluding the tax liability*

*needs to be reflected in Adidas India P&L" is merely an understanding or opinion of persons who are not experts in tax laws much less of Indian tax laws. Therefore, the aforesaid contents of the e-mail has no evidentiary value.*

*The next e-mail is an email written by Mr. Gaurav Mendiratta of KPMG, attached at Pg. 629-631 of paper book. The aforesaid email, it is submitted, was advice rendered in the event Adidas AG were to pass on the amount of insurance claim, after payment of taxes in Germany, as financial aid to the Appellant. This would be clearly a case of application of income. This, however, does not mean that the Appellant had acquired a right to receive compensation either from Zurich or from Adidas AG.*

*In view of the above, it is submitted that the assessing officer has erroneously drawn adverse inference from the aforesaid communications and it cannot, be alleged, on the basis of such communication that the impugned amount of insurance compensation admittedly received by Adidas AG from Zurich Insurance in terms of the GIP taken out by Adidas AG and of which premium was paid by Adidas AG, was, in law, income of the Appellant liable to tax in India."*

**8.** On the issue, whether there is deemed accrual of income in India in accordance with section 9(1)(i), the learned counsel submitted that said section has no application insofar as assessee is concerned, who is resident in India.

**8.1** As regard to allegation of the Assessing Officer that GIP was a scheme for tax evasion, the learned counsel submitted that GIP was taken out by the Adidas AG as a global policy with Zurich insurance company, which is a legal and valid contract under the German law. He submitted that this policy was taken by the Adidas AG not only for protecting the rights in its subsidiary in India, in particular, but for investments in subsidiaries companies anywhere in the globe. Even prior to the formation of the assessee, the Adidas AG had been taking GIP for a purpose of ensuring its global financial interest in group companies and by way of this policy the Adidas AG is covering its risk in investment

in more than hundred subsidiaries across the word. Further the learned counsel submitted that the intent behind the decision to take insurance policy can never be to evade taxes. The insurance policies taken by way of paying huge premiums to cover the contingent losses that may or may not arise in future. The insurable event may or may not arise in any country. The learned counsel further referred to the decision of the Hon'ble Supreme Court in the case of Union of India Vs. Azadi Bachao Andolan (2003) 263 ITR 706.

**8.2** In view of the arguments, the learned counsel submitted that the action of the Assessing Officer in taxing the receipt of insurance claims by the Adidas AG under the GIP taken out by the Adidas AG is contrary to the facts of the case.

**8.3** The learned DR, on the other hand, relied on the order of the lower authorities and submitted that the learned DRP has given detailed finding on the issue that in view of the income having business connection in India, it was deemed to accrue in India in view of the section 9(1)(i) of the Act.

**8.4** We have heard the rival submissions and perused the relevant material on record including the paper-book filed by the assessee. As far as factual matrix of the case are concerned, there is no dispute between the parties. The dispute is in respect of application of provisions of law over those facts. The dispute whether in the facts of the case, the claim of insurance received by the 'Adidas AG' under GIP is income accrued in the hands of the assessee or not? We proceed to decide the controversy in view of records and argument of the parties as under:

**8.5** The various clauses of the Global Insurance Policy (GIP), available on page 272 -556, makes it clear that under the policy financial interest of the Adidas AG was insured. The relevant part of the insurance policy (translated version) available on page 279 of APB is reproduced as under:

> *"part 1 general provisions, applicable for all types:*
> *1……*
> *2……*
> *3. Additional insured business/additional business venture:-*
>
> *All business venture that are included in the last annual report are insured included by Adidas AG.*
>
> *All other and newly added business ventures are also insured, if they are legitimately led by the policyholder or additionally insured business or defect or controlled (direct or indirect interest) or if they are entrepreneurial.*
>
> *These business venture hereinafter referred to a subsidiary*
> *…… "*

**8.6** Further, on page 548 of the paper-book, the subject matter of the insurance, event covered by the insurance and insurance benefit has been mentioned as under:

> ***"2. SUBJECT MATTER OF THE INSURANCE***
>
> *The Adidas AG has investments in the subsidiary companies with headquarters in those countries, which prohibit the operating of the insurance business through in an insurer not permitted there (countries with permit reservation)*
>
> *Object of this insurance is the interest of Adidas AG, to sustain the economical value of its investment in such subsidiary companies in case of a property/BU, liability-or*

*transport damages and be protected from the thus resulting, own financial losses. The insurance therefore exclusively refers to the purely financial interests of Adidas AG.*

*Insured investments are*
*In subsidiary companies, which fulfill the pre-requisites of the additional insured companies in the sense of a master contract and which have their headquarters in countries with permit reservation;*

*In subsidiary companies, which are newly formed or acquired in the sense of an insurance contract as well as were inadvertently not announced and have their headquarters in countries with permit reservation. On the inclusion of such companies in the insurance protection, the regulations of this insurance contract are correspondingly valid in the framework of this part of the contract.*

*For the subsidiary company of Adidas AG there exist risk adequate local policies coordinated with the insurance programme or integrated in the GIP. The subsidiary companies are neither entitled nor obligated by this part of the contract and are not additionally insured companies.*

## *3. EVENT COVERED BY INSURANCE*

*The claim is present, if the value of investment is reduced in case of a loss or damage.*

*-The claim is not integrated in the GIP or is not or not sufficiently covered with this coordinated local policy,*

*-The claim which would fulfill the prerequisites for a covered property/BU-liability – or transport damages in the sense of a GIP.*

*-And thus for the Adidas AG, there exists the commercial need, for balancing the reduction of value from its own finances, to negotiate the expenditures in favour of the subsidiary companies. Irrelevant is whether the Adidas*

*AG negotiates the actual expenditures for the subsidiary companies.*

*The event covered by insurance is valid as occurring at that point of time, at which after the ascertainments of the Master cover, the occurrence of the event of loss or damage would be taken into account for the subsidiary company.*

***4. INSURANCE BENEFIT (TAXES)***

*The insurer provides the Adidas AG a compensation for the value reduction of the investment.*

*As reduced value, that amount is valid, which would be replaced by the insurer, if the coverage difference insurance of the master contract could have been effectively combined to the local policies of the subsidiary companies integrated in the insurance programme or coordinated with them.*

*For the measurement of the Insurance benefit it is irrelevant, if the Adidas AG holds less than 100% of the shares in the subsidiary company.*

*As far as the local liability insurance of the concerned subsidiary company guarantees none or no extensive insurance protection for legal defense costs (defense covering), the Adidas AG has to take care in the framework of its influences for an appropriate defense or legal representation for checking of the issue of liability and for defense/clearance of unjustified claims. In this case the Adidas AG is compensated for the costs required for the legal defense."*

**8.7** After considering arguments of the parties and available records, the factual position in our view is that the policy of insurance against loss of stock by fire taken by the assessee from Bajaj Allianz (BA) was to secure stock in trade, which is a tangible asset, whereas the Global Insurance Policy (GIP), taken by the

Adidas AG from Zurich insurance was for securing investment made in subsidiaries or say financial interest, which is an intangible asset.

**8.8** Thus, the interest insured by the assessee and the interest insured by the Adidas AG are two different interest, the later one is larger than the earlier one. After considering the submission of the parties, we are of the firm view that loss in economic value of the financial interest, constituting insurable interest in the case of Adidas AG, which though has been computed with reference to loss of stock by the fire in the hands of the assessee, it is distinct and separate from the insurance claimed by the assessee from the Bajaj Allianz. The Adidas AG has paid premium separately for the Global insurance policy and no part of the same has been allocated to the assessee or reimbursed by the assessee. Under the Global insurance policy, which was entered between Adidas AG and Zurich insurance, privity of contract was between the said two parties, without assessee being a party. We agree with contention of the learned counsel that the assessee was not having any right or obligation under the said GIP. The Adidas AG, has shown the said compensation received under the GIP from the Zurich insurance as its income and paid taxes accordingly. We may like to emphasize here that the compensation settled under the GIP is for diminution in the financial interest of Adidas AG after adjusting the loss compensated by Bajaj Allianz, which is in accordance with German Law in existence which prohibit the Adidas AG to directly insure assets of subsidiary in India. In view of no right or

obligation of the assessee in the GIP, prima facie said income cannot be assessed in the hand of the assessee.

**9.** The another issue of contention is whether the compensation received by the Adidas AG has accrued under section 5 of the Income Tax Act and deemed to accrue as per section 9(1)(i) of the Act. For ready reference, the section 5 (1) of the Act is reproduced as under :

***"Scope of total income.***

***5.*** *(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.*ò

**9.1** Apparently the clause 5(1)(a) is not applicable over the assessee as the amount in question was not received by the assessee. The second clause 5(1)(b) says that income which accrues or arises or is deemed to accrue arise in India during such year to the said resident is included in the total income. The third clause 5(1)(c) includes the income under the total income, which accrues or arise to an resident assessee outside India during such year. Thus, here the main issue arises is whether the income 'accrued' or arises to the assessee. In this respect, we may like to refer to the decision of the Hon'ble Supreme Court in the case of ED Sassoon & Co Ltd (supra) as under:

> ***"48**. What has, however, got to be determined is **whether the income, profits or gains accrued to the assessee and in order that the same may accrue to him it is necessary that he must have acquired a right to receive the same or that a right to the income, profits or gains has become vested in him though its valuation may** be postponed or though its materialisation may depend on the contingency that the making up of the accounts would show income, profits or gains. The argument that the income, profits or gains are embedded in the sale proceeds as and when received by the company also does not help the transferees, because the managing agents have no share or interest in the sale proceeds received as such. They are not co-sharers with the company and no part of the sale proceeds belongs to them. Nor is there any ground for saying that the company are the trustees for the business or any of the assets for the managing agents. The managing agents cannot, therefore, be said to have acquired a right to receive any commission unless and until the accounts are made up at the end of the year, the net profits ascertained and the amount of the commission due by the company to the managing agents thus determined [See IRC vs. Lebus (1946) 1 All E.R. 476 : 27 Tax Cas. 136]."*
>
> ***(Emphasis supplied externally by us)***

**9.2** Thus, for to accrue or arise income in the hands of an assessee, he must acquire right to receive that income or that income must vest in him. In present case, the Zurich insurance has allowed the claim of insurance under GIP insured by M/s Adidas AG. The insured interest under the general insurance policy is financial interest in investment made worldwide by the Adidas AG. As the premium for the insurance policy was incurred by Adidas AG, the said entity was only having right to receive the claim of insurance and the assessee not being party to the said insurance policy in any manner, the assessee was not having any right to receive the said claim of insurance on or the said claim was not vested in the assessee. Thus, the contention of the lower authorities that the income by way of the claim of GIP accrued in favour of the assessee is devoid of any merit.

**9.3** Further, it is contended by the lower authorities, that the income was deemed to accrue or arise in view of provisions of section 9(1)(i) of the Act. It is contended that impugned income was due to loss sustained in the fire of the stock, profit which could have been earned on such stock when sold and the loss suffered on other assets and other incidentals and, therefore, it was through or from any business connection in India. In our opinion, this conclusion of the lower authorities is not correct. The claim of GIP was in respect of insured financial interest of the Adidas AG in its subsidiaries and compensation was also settled for diminution in financial interests of computing of the claim with reference to loss on fire of the stock or profit which could have been earned if such stock was sold etc in any manner cannot lead to conclusion that the claim was in respect of loss of tangible property in the form of stock of the assessee. The claim was certainly in respect of the intangible asset in the form of financial interest of the Adidas AG and thus the claim of insurance cannot be said to have any business connection in India. Similarly, the insured interest of Adidas AG in its subsidiaries cannot be said to have through or from any property in India or through or from any asset or source of income in India. The Adidas AG has entered into contact in Germany for insuring the intangible asset in the form of financial interest in its subsidiaries, which is quite distinct from the physical stock-in-trade of the assessee, which lost in fire. Thus, the claim received by Adidas AG cannot be treated as income deemed to accrue or arise in the hands of the assessee in India.

**9.4** We also do not find any substance in the finding of the lower authorities that in email correspondence between employees of Adidas AG and Zurich insurance indicated as claim of GIP belongs to the assessee. The Assessing Officer in draft assessment order has reproduced gist of correspondence made through emails. On perusal of the said correspondence, we find that same is related more to explore mode of transfer of money from the Adidas AG to the assessee, because the Adidas AG was interested in restoring the loss in its financial interest in Indian subsidiary i.e. assessee. Thus, correspondence in emails was related to application of the income and not as under whose hand it would be taxable. Further, the issue as to whether the income by way of claim under GIP from Zurich insurance is liable to be taxed in the hands of the assessee, cannot be decided by either the employees of the Adidas AG or Zurich insurance. Merely, expressing some advice or opinion by them as how this amount of claim received can be transferred to the assessee, should not be treated as admission by the assessee of claim money taxable in its hand. Further, we agree with the contention of the Ld. counsel of the assessee that insuring the financial interest in the subsidiary by M/s Adidas AG is not a tax avoidance scheme and the policy was taken to cover the contingent losses that may or may not arise in future. We find that M/s Adidas AG has paid premium in respect of the policy from time to time and also paid tax in Germany in relation to the amount in question of insurance claim. We reject the observation of the lower authorities alleging that colourable device was adopted by the assessee for evading taxes in India.

**9.5** In view of above discussion, we are of the opinion that claim of insurance received by M/s Adidas AG is not taxable in the hands of the assessee either under section 5 or under section 9(1)(i) of the Act. The grounds of the appeal raised by the assessee are accordingly allowed.

**10.** The ground No. 4 raised by the assessee is consequential in nature and accordingly, we are not required to adjudicate. The ground is accordingly dismissed as infructuous.

**11.** In the result, the appeal of the assessee is allowed.

***Order is pronounced in the open court on 29th July, 2019.***

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| Sd/- | Sd/- |
| **[AMIT SHUKLA]** | **[O.P. KANT]** |
| **JUDICIAL MEMBER** | **ACCOUNTANT MEMBER** |

Dated: 29th July, 2019.
RK/-[d.t.d.s]
Copy forwarded to:
1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR

Asst. Registrar, ITAT, New Delhi