
TRANSFER PRICING ALERT

# N. A. SHAH BULLETIN

June 2016

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## EXECUTIVE SUMMARY

For valuation of an intangible asset, only the future projections alone can be adopted and such valuation cannot be reviewed with actuals after 3 or 4 years down the line.

Once Intellectual Property Rights ("IPR") sold at arm's length price ("ALP") to Associated Enterprise ("AE"), IPR becomes property of AE. Any subsequent transaction by way of exploitation of such IPR between AE and third party does not rise to international transaction between the assesse and AE.

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**DQ Entertainment (International) Ltd V Assistant Commissioner of Income Tax (ITAT Bench of Hyderabad) ITA No. 151/Hyd/2015**

**Facts:**

i. DQ Entertainment (International) Ltd, ("the assesse" or "DQE India"), is one of the leading producers of animation visual effects, game art and entertainment content for the Indian as well as global media and entertainment industry.

ii. The DQE (Mauritius) Ltd ("DQE Mauritius") is the holding company of DQE India and DQE India is the holding company of DQE (Ireland) Ltd ("DQE Ireland").

iii. During the A.Y. 2010-11, DQE India sold the IPR of the Jungle Book Animation series to DQE Ireland. It was sold at the development stage for an amount of Rs.5,36,20,000/- which was based on average of the value's arrived at by 2 independent valuers using Relief from Royalty Method and discounted cash flow method.

iv. In order to arrive at the ALP, the Ld. TPO has replaced the projected cash flows with the actual total revenues of DQE Ireland for the year 2009-10 and 2010-11 and arrived at value of Rs.12,35,18,271/- as compared to Rs. 5,36,20,000/- determined by the assessee and proposed the transfer pricing adjustment of Rs 6,98,98,271/- to the AO.

v. In addition to the above adjustment, the Ld. TPO decided that even though the legal ownership of IPR of Jungle Book has been transferred to DQE Ireland, economic ownership remained with DQE India and accordingly proceeded to apply profit split method to apportion the appropriate profit to DQE India which was otherwise lying with DQE Ireland.

vi. Aggrieved, the assessee raised objections before the DRP. DRP rejected the objection raised by the assessee on this issue and confirmed the order of the Ld. TPO.

vii. Aggrieved, the assessee has preferred an appeal before the ITAT, Hyderabad.

**Issue:**

a. Whether for valuation of an intangible asset, the future projections alone be adopted or can such valuation be reviewed with actuals after 3 or 4 years down the line?

b. Whether profit can be attributable to Indian Entity even after sale of IPR by Indian entity to its AE?

**Held:**

**On the issue of Valuation of IPR:**

i. The ITAT has relied on the ruling of ***Social Media India Ltd v ACIT ( ITA No. 1711/Hyd/2012)*** wherein it was held that valuation submitted by independent valuers has to be adopted without any modification.

ii. The revenue had no problem with the valuation but they are replacing the projected values with actual values. ITAT has relied on the ruling of ***ITAT Bangalore in case of Tally Solutions Private limited*** where it was held that valuation method adopted for determining future years cannot be replaced with actuals down the line, the valuation will go either way.

iii. What is important is the value available at the time of making business decision. It should be left to the wisdom of the businessman, he knows what is good for the organization.

iv. The review does not mean replacing the projection with actuals. In rational decision making, the actual results are irrelevant. When the values are replaced subsequently, it is not valuation but evaluation i.e. moving the post of result determined out of projections.

v. For valuation of an intangible asset, only the future projections alone can be adopted and such valuation cannot be reviewed with actuals after 3 or 4 years down the line.

Accordingly, the grounds raised by assessee are allowed.

**On the issue of profit attributable to Indian entity:**

i. The ITAT has held that the assessee had sold the IPR at the development stage itself and it was not even fully developed to generate revenue. When the Ld. TPO himself has agreed to the fact that there is an outright sale, there ends the international transaction.

ii. There is no international transaction after the outright sale and hence, no international transaction exists as per section 92B of the Act.

iii. Once IPR is sold and ALP is determined, IPR becomes the property of AE. Accordingly, the Assessee has no locus standi to claim any benefit neither the revenue.

iv. Further, with regards to Revenue's grievances on arrangements and existence of group companies, ITAT has held that Revenue did not bring any cogent evidence to prove tax avoidance motive.

Accordingly, the grounds raised by the Assessee are allowed.

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