REPORTABLE

IN THE SUPREME COURT OF INDIA

CIVIL APPELLATE JURISDICTION

CIVIL APPEAL NO. 8463 OF 2022
(Arising from S.L.P.(Civil) No.28652/2018)

SAP LABS INDIA PRIVATE LIMITED ..APPELLANT

VERSUS

INCOME TAX OFFICER, CIRCLE 6, BANGALORE ..RESPONDENT

WITH

CIVIL APPEAL NO. 8553 OF 2022
(Arising from SLP(Civil) No. 20993/2022 @ Diary No. 1571/2019)
CIVIL APPEAL NO. 8504 OF 2022
(Arising from SLP(Civil) No. 20872/2022 @ Diary No. 25119/2019)
CIVIL APPEAL NO. 8464 OF 2022
(Arising from SLP(Civil) No. 28694/2018)
CIVIL APPEAL NO. 8682 OF 2022
(Arising from SLP(Civil) No. 11672/2019)
CIVIL APPEAL NO. 9387 OF 2022
(Arising from SLP(Civil) No. 24216/2022 @ Diary No. 25313/2019)
CIVIL APPEAL NO. 8675 OF 2022
(Arising from SLP(Civil) No. 11071/2019)
CIVIL APPEAL NO. 9401 OF 2022
(Arising from SLP(Civil) No. 24236/2022 @ Diary No. 30692/2019)

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CIVIL APPEAL NO. 9023 OF 2022
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J U D G M E N T

M.R. SHAH, J.

1. The present batch of Civil Appeals, mostly by the Revenue and few of the assessees arises out of judgments and orders passed by the various High Courts, more particularly the High Court of Karnataka, dismissing the appeals challenging the findings of the Income Tax Appellate Tribunal (for short, 'Tribunal') on 'Transfer Pricing' issues on the ground that the issues decided by the Tribunal are questions of fact and as perversity is

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neither pleaded nor argued nor demonstrated by placing material to that effect, no substantial question of law arises for consideration under Section 260A of the Income Tax Act, 1961 (for short, 'IT Act'). The High Court of Karnataka has dismissed the appeals preferred by the Revenue by relying upon its earlier judgment in the case of ***PCIT v. Softbrands India (P) Ltd., reported in (2018) 406 ITR 513 (Karnataka)***.

2. Shri Balbir Singh, learned Additional Solicitor General of India, appearing on behalf of the Revenue has vehemently submitted that the Karnataka High Court in the case of ***Softbrands India (P) Ltd. (supra)*** has erroneously held that the Tribunal is the final fact finding authority on determining the arm's length price and therefore once the Tribunal determines the arm's length price the same cannot be subject to judicial scrutiny/scrutiny in an appeal under Section 260A of the IT Act.

2.1 Shri Balbir Singh, learned ASG has submitted that there cannot be any absolute proposition of law that against the decision of the Tribunal determining the arm's length price, there shall not be any interference by the High Court in an appeal under Section 260A of the IT Act.

2.2 Shri Balbir Singh, learned ASG has taken us to the scheme of transfer pricing/arm's length price to be determined under Chapter X of the IT Act, more particularly Sections 92, 92A to 92CA, 92D, 92E and 92F and Rules 10A to 10E of the Income Tax Rules, 1962 (for short, 'IT Rules'). It is submitted that under the scheme of transfer pricing, the arm's length price is to be determined taking into consideration the guidelines stipulated under the aforesaid provisions of the IT Act and the Rules. It is submitted that therefore it is always open for the High Court to consider and/or examine, whether the guidelines stipulated under the Act and the Rules, while determining the arm's length price have been followed by the Tribunal or not.

2.3 It is submitted that if the arm's length price is determined by the Tribunal *de hors* the guidelines stipulated under the Act and the Rules, more particularly Rules 10A to 10E of the Rules, the determination can be said to be perverse which is always subject to the scrutiny by the High Court in an appeal under Section 260A of the Act.

2.4 It is submitted that therefore the view taken by the High Court of Karnataka in the case of ***Softbrands India (P) Ltd. (supra)*** is required to be corrected by this Court.

3. S/Shri Arvind P. Datar, Tarun Gulati, Percy Pardiwala, learned Senior Advocates and other learned counsel appearing on behalf of the respective assessees have vehemently submitted that once the arm's length price is determined by the Tribunal taking into consideration the relevant guidelines, thereafter challenge to the same cannot be said to be a substantial question of law, to be considered in an appeal under Section 260A of the IT Act.

3.1 It is submitted on behalf of the assessees that Section 260A of the IT Act provides that an appeal shall lie to the High Court from every order of the Tribunal only if the High Court is satisfied that the case involves a substantial question of law. Sub-section (6) thereof provides that the High Court may determine any issue which (a) has not been determined by the Appellate Tribunal; or (b) has been wrongly determined by the Appellate Tribunal, by reason of a decision on such question of law as is referred to in sub-section(1).

3.2 It is submitted that the said provision came up for consideration in a catena of decisions. It is a settled position that jurisdiction under section 260A of the IT Act cannot be invoked unless there arises a substantial question of law. This is precisely what is held by the High

Court of Karnataka in the judgment in ***Softbrands India (P) Ltd. (supra)***, by relying on a series of judgments of this Court.

3.3 It is submitted that a substantial question of law can arise in a case only when a question of law is fairly arguable, where there is room for difference of opinion on it.

3.4 It is submitted that a finding of fact may give rise to a substantial question of law, *inter alia*, in the event the findings are based on (i) no evidence; and/or (ii) while arriving at the said finding, relevant admissible evidence has not been taken into consideration or inadmissible evidence has been taken into consideration; or (iii) legal principles have not been applied in appreciating the evidence; or (iv) when the evidence has been misread. The High Courts as well as this Court have consistently held that the Tribunal being a final fact finding authority, in the absence of demonstrated perversity in its finding, interference therewith by the High Court is not warranted. In support of his submission, learned senior counsel/counsel have relied upon the decisions of this Court in the cases of ***Vijay Kumar Talwar v. CIT, (2011) 1 SCC 673*** and ***Sir Chunilal V. Mehta and Sons Ltd. v.***

Century Spinning and Manufacturing Co. Ltd., reported in AIR 1962 SC 1314.

3.5 It is further submitted that perversity, if any, not only should be specifically alleged in the appeal before the High Court but also, as held by the High Court in the case of ***Softbrands India (P) Ltd. (supra)***, the same ought to have been demonstrated.

3.6 It is further submitted that some instances where a substantial question of law can arise in Transfer Pricing matter is where the issue relates to whether at all a transaction falls within the definition of 'international transaction', or if two enterprises are 'associated enterprises' as per the definition under the IT Act. The question of comparability of two companies or selection of filters are usually question of fact, which primarily depend on the functions performed, assets employed and risks assumed by the tested party as well as comparable transactions. Unless perversity in the findings of the Tribunal is pleaded and demonstrated, by placing material on record, no substantial question of law can arise and, therefore, there can be no interference by the High Court. To the extent there can be no dispute between the parties, in view of the settled legal proposition dealing with

sections 260A of the Act and section 100 of the Code of Civil Procedure, 1908.

3.7 It is submitted that in all the appeals filed by the Revenue before the High Court, the primary issues raised pertained to inclusion and exclusion of a few comparables and selection of filters, which are essentially questions of fact and there is a *consensus ad idem* to this extent between the parties. In none of the appeals has the Revenue pleaded, argued, or placed any material to demonstrate perversity in the order of the Tribunal. Therefore, the High Court after noting the questions raised, findings rendered by the Tribunal and noting that perversity is neither pleaded/argued nor demonstrated by placing any material, dismissed the appeals, by relying on principles laid down in ***Softbrands India (P) Ltd. (supra).*** Therefore, no error can be attributed to the orders passed by the High Court dismissing the appeals, in such circumstances.

3.8 It is next submitted that the submission of the Revenue that in each case the High Court should examine whether the guidelines laid down in the IT Act and the Rules are followed to determine the arm's length price is not correct and moreover is too farfetched, as the

High Court can only decide substantial questions of law raised and arising before it.

3.9 It is further submitted that the Revenue's submission that the judgment in ***Softbrands India (P) Ltd. (supra)*** indicates that there will be no interference even where inconsistent views are taken by the Tribunal is misconceived, because, it is quite possible that in view of the particular set of facts in one case, one Bench excludes a company and in another case includes the same in view of different set of facts, or similarly applies a filter in one and not in another. This is what is in fact held in ***Softbrands India (P) Ltd. (supra)*** (please see para 45). In almost all cases it is the Revenue which uses the same set of comparables for determining an arm's length price, thus, painting all assessees with the same brush. These are questions of facts, which would require determination on a case by case basis, and unless perversity is demonstrated in the order of the Tribunal, no interference is called for by the High Court.

3.10 It is further submitted that Transfer Pricing analysis involves benchmarking of controlled transactions with uncontrolled transactions (terms specifically defined in the IT Act and the Rules) is largely a statistical exercise using database of companies in public domain as specifically

defined in the IT Act and the Rules, referred hereinabove. In the specific facts of batch of cases wherein department has approached this Court, the exercise of application of detailed guidelines set out in the IT Act and the Rules was indeed carried out and ironed out by Tribunal with assistance of tax payers representatives and department officers by looking a publicly available information mostly in the form of audited financials etc., of companies as prescribed in the IT Act and the Rules. Contrasting the appeals/ pleadings filed before High Court of Karnataka by taxpayers and department available as part of batch of appeals filed would enable appreciation of the case made out before the High Court. This is essential to appreciate the correctness of conclusions by the High Court in this batch of appeals/petitions. Tax department is attempting to seek intervention of this Court in present batch of department's cases without reference to/*de hors* any of this relevant background facts. Over last two decades, Tribunal and various High Courts have applied the guidelines laid down in the IT Act and the Rules contributing to evolution of a process. Intervention in the department's appeals in present batch of cases and/or laying down any guidelines ignoring this background could potentially disturb the well settled principles under section

260A (equivalent to section 100 CPC). In background facts or present batch of department's appeals, acceptance of department's contention about lack of application of mind by the High Court would cast an unjust burden on the High Court to undertake a *suo moto* exploration of facts not placed before it, make out a case for the department and decide the same without any assistance from the appellant before the High Court. Any such guidelines would upset settled law not only with reference to section 260A but also impact process under section 100 CPC. Unlike the assessees cases involved in this batch of appeals, it was never the case of the department that the High Court has not considered any of its written/ oral pleadings before the High Court. It is submitted that considered view may be taken after taking into account pleadings before the High Court, pleadings in the appeals before this Court in Assessees and department appeals and not based on sweeping generalization.

3.11 It is submitted that Transfer Pricing provisions are essentially a valuation exercise involving determination of a statistical sample of comparables. Under Section 92C(2) of the IT Act, Arm's Length Price is always in a range. It is not a science but it is an art. This Court in

G.L. Sutania and Anr v SEBI and Ors. reported in 2007 (5) SCC 133 at paras 84 and 85, have unequivocally stated that valuation is a question of fact.

3.12 It is submitted that the case of the Revenue is that the proposition in ***Softbrands India (P) Ltd. (supra)*** that no question of law can arise out of the transfer pricing matters involving selection of comparables or application of filters, and the Tribunal is the final fact finding authority and all the questions decided by the Tribunal are questions of fact is too broadly stated, and as a result of this proposition, it would appear that the High Court has held that no appeal would lie to it under section 260A of the IT Act.

3.13 It is further submitted by the learned counsel appearing on behalf of the respective assessees in the appeals preferred by the Revenue that in all these cases, the High Court has found that there is no perversity by the Tribunal in determining the arm's length price and therefore no substantial question of law arises as no perversity is pleaded and demonstrated. It is submitted that therefore the impugned judgments and orders passed by the High Court dismissing the appeals preferred by the Revenue are not required to be interfered with by this Court.

4. We have heard Shri Balbir Singh, learned ASG appearing on behalf of the Revenue and learned senior counsel/counsel appearing on behalf of the respective assessees at length.

5. In the present batch of Civil Appeals preferred by the Revenue, the respective High Courts, more particularly the Karnataka High Court have/has dismissed the appeals preferred by the Revenue in which the Revenue challenged the determination of the arm's length price by the Tribunal, relying upon and/or considering the decision of the Karnataka High Court in the case of ***Softbrands India (P) Ltd. (supra)***. In the case of ***Softbrands India (P) Ltd. (supra)*****,** the High Court has taken the view that the determination of arm's length price by the Tribunal shall be final against which an appeal under Section 260A of the IT Act is not required to be entertained.

Therefore, the short question which is posed for the consideration of this Court is, whether in every case where the Tribunal determines the arm's length price, the same shall attain finality and the High Court is precluded from considering the determination of the arm's length price determined by the Tribunal, in exercise of powers under Section 260A of the Act?

6. While determining the aforesaid issue, the relevant provisions for determining the arm's length price under the IT Act are required to be referred to.

Section 92-C which is relevant, for the purpose of determining ALP *inter alia,* reads as follows:

> *"92C. (1) The arm's length price in relation to an international transaction [or specified domestic transaction] shall be determined by any of the following methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe, namely : -*
>
> *(a) comparable uncontrolled price method;*
>
> *(b) resale price method;*
>
> *(c) cost plus method;*
>
> *(d) profit split method;*
>
> *(e) transactional net margin method;*
>
> *(f) such other method as may be prescribed by the Board.*
>
> *(2) The most appropriate method referred to in sub-section (1) shall be applied, for determination of arm's length price, in the manner as may be prescribed:*
>
> *Provided that where more than one price is determined by the most appropriate method, the arm's length price shall be taken to be the arithmetical mean of such prices:*
>
> ** ** **
>
> *(3) Where during the course of any proceeding for the assessment of income, the Assessing Officer is, on the*

basis of material or information or document in his possession, of the opinion that-

(a) the price charged or paid in an international transaction [or specified domestic transaction] has not been determined in accordance with sub-sections (1) and (2); or

(b) any information and document relating to an international transaction [or specified domestic transaction] have not been kept and maintained by the assessee in accordance with the provisions contained in sub-section (1) of section 92D and the rules made in this behalf; or

(c) the information or data used in computation of the arm's length price is not reliable or correct; or

(d) the assessee has failed to furnish, within the specified time, any information or document which he was required to furnish by a notice issued under sub-section (3) of section 92D, the Assessing Officer may proceed to determine the arm's length price in relation to the said international transaction [or specified domestic transaction] in accordance with sub-sections (1) and (2), on the basis of such material or information or document available with him:

Provided that an opportunity shall be given by the Assessing Officer by serving a notice calling upon the assessee to show cause, on a date and time to be specified in the notice, why the arm's length price should not be so determined on the basis of material or information or document in the possession of the Assessing Officer."

20. Section 92C(1) thus visualizes determination of the "arms-length price" (ALP) by any of five enumerated methods, "*being the most appropriate method*", having

regard to the "*nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the board may prescribe, namely (a) comparable uncontrolled price method, (b) resale price method, (c) cost + method, (d) profit split method, (e) transactional net margin method, (f) any such other method as may be prescribed by the board. Where more than one price is determined by the most appropriate method, the arm's length price shall be taken to be arithmetical mean of such prices*."

21. Rule 10B of the Rules prescribes the determination of arm's length price under Section 92C. The first step in all methods is evaluation of differences between the international transaction undertaken with the "*unrelated enterprise performing the comparable functions*" in similar circumstances. Rule 10B of the Income-tax Rules *inter alia,* provides for various methods for determination of the arm's length price. Rule 10B(1)(e) prescribes the "transactional net margin method" (TNMM) with which the present case is concerned. Rule 10B(1)(e) (i) is as under:

> *"10B. (1) Determination of arm's length price under section 92C:— . .*
>
> ********** *********
>
> *(e) transactional net margin method, by which,—*
>
> *(i) the net profit margin realised by the enterprise from an international transaction entered into with an associated enterprise is computed in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise or having regard to any other relevant base."*

7. Therefore, while determining the arm's length price, the Tribunal has to follow the guidelines stipulated under

Chapter X of the IT Act, namely, Sections 92, 92A to 92CA, 92D, 92E and 92F of the Act and Rules 10A to 10E of the Rules. Any determination of the arm's length price under Chapter X *de hors* the relevant provisions of the guidelines, referred to hereinabove, can be considered as perverse and it may be considered as a substantial question of law as perversity itself can be said to be a substantial question of law. Therefore, there cannot be any absolute proposition of law that in all cases where the Tribunal has determined the arm's length price the same is final and cannot be the subject matter of scrutiny by the High Court in an appeal under Section 260A of the IT Act. When the determination of the arm's length price is challenged before the High Court, it is always open for the High Court to consider and examine whether the arm's length price has been determined while taking into consideration the relevant guidelines under the Act and the Rules. Even the High Court can also examine the question of comparability of two companies or selection of filters and examine whether the same is done judiciously and on the basis of the relevant material/evidence on record. The High Court can also examine whether the comparable transactions have been taken into consideration properly or not, i.e., to the extent non-

comparable transactions are considered as comparable transactions or not. Therefore, the view taken by the Karnataka High Court in the case of ***Softbrands India (P) Ltd.*** that in the transfer pricing matters, the determination of the arm's length price by the Tribunal is final and cannot be subject matter of scrutiny under Section 260A of the IT Act cannot be accepted.

8. Thus, in each case, the High Court should examine whether the guidelines laid down in the Act and the Rules are followed while determining the arm's length price. Therefore, we are of the opinion that the absolute proposition of law laid down by the Karnataka High Court in the case of ***Softbrands India (P) ltd. (supra)*** that in the matter of transfer pricing, determination of the arm's length price by the Tribunal shall be final and cannot be subject matter of scrutiny and the High Court is precluded from examining the correctness of the determination of the arm's length price by the Tribunal in an appeal under Section 260A of the IT Act on the ground that it cannot be said to be raising a substantial question of law cannot be accepted. As observed hereinabove, within the parameters of Section 260A of the IT Act in an appeal challenging the determination of the arm's length price, it is always open for the High Court to examine in each case

whether while determining the arm's length price, the guidelines laid down under the Act and the Rules, referred to hereinabove, are followed or not and whether the determination of the arm's length price and the findings recorded by the Tribunal while determining the arm's length price are perverse or not.

9. In view of the above, the impugned judgments and orders passed by the High Court dismissing the Revenue's appeals and even the appeals preferred by the assessees are required to be quashed and set aside and the matters are required to be remitted back to the concerned High Courts to decide and dispose of the respective appeals afresh in light of the observations made hereinabove and examine in each and every case whether the guidelines laid down under the Act and the Rules, referred to hereinabove, are followed while determining the arm's length price by the Tribunal or not and to that extent whether the findings recorded by the Tribunal while determining the arm's length price are perverse or not.

10. In view of the above and for the reasons stated above, all these appeals are allowed. The impugned judgments and orders passed by the respective High Courts are hereby quashed and set aside. The matters

are remitted back to the respective High Courts to decide and dispose of the appeals afresh in light of the observations made hereinabove and to examine whether in each case while determining the arm's length price the guidelines laid down under the Act and the Rules, referred to hereinabove, are followed or not and whether the findings recorded by the Tribunal while determining the arm's length price are perverse or not. The aforesaid exercise be completed, preferable within a period of nine months from the date of receipt of the present order by the respective High Courts. It is specifically observed that we have not entered into the merits of the cases at all and we have not expressed anything on the determination of the arm's length price in case of respective assessees, either in favour of the assessees or in favour of the Revenue. It is ultimately for the concerned High Court to take a fresh decision, as observed hereinabove.

11. All these appeals stand allowed in terms of the above. No costs.

……..J.
[M.R. SHAH]

NEW DELHI;
APRIL 19, 2023.

……..J.
[M.M. SUNDRESH]

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