

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

**Before Sh. N. K. Saini, AM And Smt. Beena Pillai, JM**

**ITA No. 575/Del/2009 : Asstt. Year : 2004-05**

**ITA No. 5533/Del/2010 : Asstt. Year : 2004-05**

M/s RS Components & Controls Ltd., 222, Okhla Industrial Estate, New Delhi-110020 <b>(APPELLANT)</b>	Vs	Dy. Commissioner of Income Tax, Circle-15(1), New Delhi <b>(RESPONDENT)</b>
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**ITA No. 3199/Del/2010 : Asstt. Year : 2005-06**

Dy. Commissioner of Income Tax, Circle-15(1), New Delhi <b>(APPELLANT)</b>	Vs	M/s RS Components & Controls Ltd., 222, Okhla Industrial Estate, New Delhi-110020 <b>(RESPONDENT)</b>
<b>PAN No. AAACR0194D</b>		

**Assessee by : Sh. Anil Bhalla, Adv.**

**Revenue by : Sh. Amrendra Kumar, CIT DR**

<b>Date of Hearing : 24.02.2016</b>	<b>Date of Pronouncement : 14.03.2016</b>
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**ORDER**

**Per N. K. Saini, AM:**

These appeals by the assessee for the assessment year 2004-05 are directed against the orders dated 26.12.2008 of the CIT(A)-XX, New Delhi and dated 20.10.2010 of the CIT(A)-XVIII, New Delhi while the appeal of the department for the assessment year 2005-06 is directed

against the order dated 30.04.2010 of the CIT(A)-XX, New Delhi.

2. First we will deal with the assessee's appeal in ITA No. 575/Del/2009 for the assessment year 2004-05.

Following grounds have been raised in this appeal:

*“1. The learned Commissioner of Income Tax (Appeals) has erred both on facts and in law in upholding the action of the learned Transfer Pricing Officer (TPO) in making an addition of Rs.98,25,957/- representing alleged difference in Arm's length price of international transactions as returned by the appellant company by following Comparable Uncontrolled Price (CUP) method of valuation in terms of Section 92C and as assessed by the learned Transfer Pricing Officer-V, New Delhi by following TNMM method of valuation vide order dated 22.11.2006 passed u/s 92CA(3) of the Income Tax Act, 1961.*

*1.1 The learned Commissioner of Income Tax (Appeals) has further erred both on facts and in law in summarily rejecting the CUP method of valuation followed by the appellant company in terms of Section 92C of the Income Tax Act, 1961 on the basis of adopting comparables from industry which were not comparable with the appellant company while following TNMM method of valuation.*

*1.2 The learned Commissioner of Income Tax (Appeals) has erred both on facts and in law in conducting of fresh transfer pricing study which was not in conformity with the provisions of section 92C(3) of the Income Tax Rules, 1962.*

*1.3 Without prejudice the learned Commissioner of Income Tax (Appeals) has erred in misunderstanding, misappreciating and miscalculating the information relied upon by him.*

*2. The learned Commissioner of Income Tax (Appeals) has erred both on facts and in law in upholding the action of the learned Assessing Officer in disallowing provision for bad debts amounting to Rs.2,55,360/- claimed in terms of Section 36(1)(vii) r.w.s. 36(2) of the Income Tax Act, 1961.*

*3. The appellant craves leave to add, alter or amend the ground of appeal at a later stage.”*

3. First issue in this appeal vide Ground Nos. 1 to 1.3 relates to the sustenance of addition made by the TPO amounting to Rs.98,25,957/- on account of difference in Armø Length Price of international transactions.

4. Facts of the case in brief are that the assessee filed the return of income on 30.10.2004 declaring loss of Rs.36,28,537/- which was processed u/s 143(1) of the Income Tax Act, 1961 (hereinafter referred to as the Act) on 30.03.2005. Subsequently, the case was selected for scrutiny. During the course of assessment proceedings, the AO noticed that the assessee had entered into international transactions with Associated Enterprises (AEs) as per following details:

<i>i. Purchase of goods for resale</i>	<i>Rs. 4,13,98,972/-</i>
<i>ii. Catalogues purchased</i>	<i>Rs. 99,80,530/-</i>
<i>Total</i>	<i>Rs. 5,13,79,502/-</i>

5. The AO in accordance with the provisions of Section 92CA(1) of the Act referred the matter to the TPO for determination of Armø Length Price. The TPO vide order u/s 92CA(3) of the Act dated 22.11.2006 computed the Armø Length Price of the international transactions entered into with AEs relating to purchase of goods and catalogues for advertisement at Rs.3,85,89,325/- against the declared value of Rs.5,13,79,502/-. The AO in terms of provisions of Section 92CA(4) of the Act asked the assessee to show cause as to why the purchase price of goods and advertisement (international transaction) from its AEs be not taken at Rs.3,85,89,325/-. The AO after considering the submissions of the assessee was of the view that TNMM was the most appropriate method for determining the Armø Length Price instead of CUP method applied by the assessee and that the selection of comparables had been done after due consideration of all material facts keeping in view OECD guidelines. Therefore, the objection raised by the assessee were rejected and an addition of Rs.1,27,90,177/- was made on account of difference in Armø Length Price of international transactions. The AO also added Rs.2,55,360/-

out of the provision of bad debts and Rs.10,553/- on account of prior period expenses. Accordingly, total income was computed at Rs.94,27,553/- instead of loss shown by the assessee at Rs.36,28,537/-.

6. Being aggrieved the assessee carried the matter to the Id. CIT(A) and submitted that the assessee was dealing in more than 30,000 products manufactured by different companies and was engaged in the business of supply of industrial components, spare parts in the nature of cables & connectors, control and automation components, electronic and electrical consumables, semiconductors, tests & measurement instruments, maintenance safety security equipment & components, mechanical products & tools and technical books. The assessee submitted to the Id. CIT(A) as under:

*“CUP is selected as the most appropriate method and the reason for selection of CUP is that*

*(a) The rates are compared on the basis of international price list of Associated Enterprise which are more than the rate charged by them to the assessee. In view of very large number of items the quantification of Arm's Length Price for each and every product is not verified. In view of above the book value of international transaction with*

*Associated Enterprise are less than the comparable price and the total price paid is the good representation of Arm's Length Price.*

- (b) The transfer rates have been compared with the international prices of R.S. Components Limited, UK. The International prices are the prices at which the products are available to the independent third parties. The analysis done shows that the international prices of the associated enterprise are more than the rate charged by it to the assessee.*
- (c) The rates have also been compared with the international rates coming on the website of R.S. Components Limited, U.K as on 26.10.2004. Copy of international rates downloaded has also been filed. The difference in the price downloaded from the website and those picked up from paper catalogue is due to updation of website on regular basis where as catalogues are issued once in every 6 months by the associated enterprise. The exercise again proves that the transfer prices are less than the international prices of associated enterprise.*
- (d) The associated enterprise also supplies the product directly of Indian customers at its international prices. The invoices raised on the Indian customers by R.S. Components Limited, UK have been filed. These prices can be compared with the international prices in the box file. The transfer prices are*

*as appearing in the box file. The international prices as appearing in the box file can again be checked with the set of 7 paper catalogue book.*

*(e) Farnell Electronic Components Ltd., UK is a competitor of the company which supplied same type of electronic products in India through its distributors like Hynetic, India and Microdevices, India etc. Brief information and evidence about type of products offered by Farnell and appointment of Microdevices, India as its distributor has been filed. The comparison of current international prices of R.S. Components Ltd., UK with current international prices of Farnell Electronic Components Ltd., UK has been filed.”*

7. The assessee further stated before the Id. CIT(A) that since the catalogue prices were not more than the prices actually charged by the parent company, therefore, the transaction was at Arm's Length. It was further submitted that the TPO selected 7 comparables companies for comparison purposes, however, those companies were not dealing with similar items and moreover were manufacturing companies. The assessee highlighted the difference on account of the comparables selected by the TPO as per following details:

*“a) Vijai Electrical Limited:  
The Company was established in 1973 and is a  
“Manufacturer” of Electrical Power and  
Distribution Transformers.*

*b) Zicom Electronic Security Systems Ltd.  
Zicom are providers of Electronic Security Systems  
for small, medium and large establishments and  
Government Projects.*

*c) Roop Telesonic Ultrasonix Ltd.  
Roop telesonic is an Ultrasonic machine  
manufacturer for welding, cleaning, sieving, non  
destructive testing, sonochemistry and specialized  
applications.*

*d) Akasaka Electronics Ltd.  
Akasaka Electronics is a manufacturer of Printed  
Circuit Boards for Consumer Electronics and  
Industrial Electronic Applications.*

*e) Videocon Communications:  
Videocon is an Indian Multinational Company and  
is a Global force in Display Technologies and a  
manufacturer of Home Appliances.*

*f) MIRC Electronics  
MIRC is the maker of Onida brand of consumer  
durables and is a television manufacturer.*

*g) Bharat Electronics Limited  
Bharat Electronics is a Public Sector Unit (PSU)  
and was incorporated in 1954. BEL meets the needs  
of the Indian Defence, Electronic Systems like*

*Communications including radars and strategic components.”*

8. It was also stated that CUP method was the comparables method and the TNMM method followed by the TPO was flawed because he had compared the percentage with companies which had no similarity in the product range, in the business model and the commercial operations. It was also stated that the assessee company had achieved higher net profit rate in the subsequent year because of increased turnover which resulted in higher absorption of the overhead. Therefore, the lower net profit margin was because of lower turnover and extra ordinary charges to profit and loss account.

9. The Id. CIT(A) after considering the submissions of the assessee observed that the TPO was right in holding that the CUP method was not most appropriate method in the assessee's case to determine the Arm's Length Price in respect of the transactions entered into between the assessee and its AE, he mentioned that what the assessee did was that it had compared the prices listed in AE's catalogue at which AE allegedly sold the goods to the third parties, with the prices paid by the assessee for goods purchased from its AE and this type of comparison cannot be termed as using

internal CUP, as envisaged by Indian Transfer Pricing Regulation or even by OECD guidelines. According to the Id. CIT(A) the TNMM was the most appropriate method. He also observed that even if the comparables chosen by the TPO were not correct, the assessee failed to bring the probable comparables. The Id. CIT(A) conducted a fresh search by revisiting databases namely *ProWessö* and 7 new comparables were selected. The Id. CIT(A) worked out adjustment of Rs.98,25,957/- by selecting the following 7 new comparables wherein average net operating margin of comparables was 8% as per the following details:

S.No.	Company Name	Sales	Total expenses	Net profit	Net Profit as a percentage of sales
1.	<i>Aishwarya Telecom Ltd.</i>	5.71	4.86	1.01	18%
2.	<i>K Dhandapani &amp; Co. Ltd.</i>	22.13	20.51	1.78	8%
3.	<i>Karuna Cables Ltd.</i>	8.01	8.43	-0.26	-3%
4.	<i>Salzer Exports Ltd.</i>	1.88	1.89	0.15	8%
5.	<i>V H A L Industries Ltd.</i>	95.04	87.03	8.01	8%
6.	<i>V Guard Industries Ltd.</i>	129.12	120.26	8.86	7%
7.	<i>Voltaire Leasing &amp; Finance Ltd.</i>	3.09	2.81	0.28	9%
				<i>Average</i>	8%

10. Accordingly, the Id. CIT(A) sustained the addition of Rs.98,25,957/- on account of difference in the Arm's Length Price as under:

<i>Total Sales</i>	<i>Rs. 11,27,07,978</i>
<i>Operating Profit</i>	<i>Rs. (-) 8,09,319</i>
<i>Operating Profit margin</i>	<i>0.71%</i>
<i>Arm's Length Operating Profit Margin</i>	<i>8%</i>

*Arm's Length Operating profit*  
*Actual Operating Profit*  
*Difference being Adjustment required*

11. The Id. CIT(A) also sustained the addition on account of bad debts by observing that no details had been provided, so as to show, how the assessee reached to the conclusion that the debt had really gone bad. Accordingly, disallowance of Rs.2,55,360/- was also sustained.

12. Now the assessee is in appeal. The Id. Counsel for the assessee reiterated the submissions made before the authorities below and further submitted that the Id. CIT(A) did not allow any opportunity to the assessee while selecting the 7 new comparables. It was further submitted that the assessee followed the CUP method which was most appropriate method but no cogent reason was given while rejecting the said method and adopting TNMM. It was stated that the comparables selected by the assessee were rejected by the TPO who selected his own 7 comparables which were not at all applicable to the facts of the assessee's case and that the Id. CIT(A) also adopted another 7 comparables without confronting the same to the assessee, so there was the violation of the principles of natural justice. He requested to set aside the issue back to the file of the TPO/AO.

13. In his rival submissions the ld. CIT DR strongly supported the impugned order passed by the ld. CIT(A) and reiterated the observations made in the impugned order.

14. We have considered the submissions of both the parties and carefully gone through the material available on the record. In the present case, it is noticed that the assessee followed CUP method and selected 7 comparables in respect of international transaction to work out the Arm~~ø~~s Length Price. However, the TPO adopted TNMM instead of CUP method and rejected the comparables adopted by the assessee. He selected 7 new comparables and worked out the Arm~~ø~~s Length Price adjustment. The ld. CIT(A) although accepted that the comparables chosen by the TPO were not to be considered, however, he adopted 7 new comparables but had not given any reason while rejecting the comparables selected by the assessee. In the present case, it also appears that a proper opportunity of being heard was not given by the ld. CIT(A) while adopting 7 new comparables to work out the adjustment on account of Arm~~ø~~s Length Price. We, therefore, by considering the totality of the facts, deem it appropriate to set aside this issue back to the file of the ld. CIT(A) to be decided afresh in accordance with law after providing due and reasonable

opportunity of being heard to the assessee. The Id. CIT(A) is also directed to decide by passing a speaking as to whether the CUP or RPM or TNMM was the most appropriate method in respect of the international transaction entered by the assessee with its Associated Enterprises (AE).

15. As regards to the another issue relating to the bad debts, it is noticed that the Id. CIT(A) confirmed the disallowance made by the AO only on this issue that the assessee could not furnish any detail to substantiate that the debts in fact became bad. However, he has not considered this fact as to whether the assessee had written off the debts in its books of account which is the basic requirement to claim the bad debts. Therefore, this issue is also set aside to the file of the Id. CIT(A).

16. As regards to the appeal in ITA No. 5533/Del/2010 is concerned, it is an admitted fact that it relates to the penalty levied by the AO and sustained by the Id. CIT(A) u/s 271(1)(c) of the act, which is directly connected with the quantum addition in ITA No. 575/Del/2009, which we have restored to the file of the Id. CIT(A). Therefore, the issue relating to the penalty u/s 271(1)(c) of the Act is also

restored to the file of the Id. CIT(A) to be decided afresh alongwith the appeal on quantum addition after providing due and reasonable opportunity of being heard to the assessee.

17. In the departmental appeal in ITA No. 3199/Del/2010 for the assessment year 2005-06, the issue relates to the deletion of transfer pricing adjustment made by the TPO/AO.

18. The facts related to this year are identical to the facts involved in the earlier assessment year 2004-05, which we have adjudicated in the former part of this order and the matter has been restored to the file of the Id. CIT(A) who had substituted comparables selected by him by discarding the comparables selected by the TPO. Therefore, by considering the similarity in the facts for the assessment year under consideration vis-à-vis the assessment year 2004-05 (supra) this issue is also restored back to the file of the Id. CIT(A) to be decided afresh in accordance with law after providing due and reasonable opportunity of being heard to both the parties.

19. In the result, appeals of the assessee as well as department are allowed for statistical purposes.

(Order Pronounced in the Court on 14/03/2016)

Sd/-

**(Beena Pillai)**

**JUDICIAL MEMBER**

**Dated: 14/03/2016**

\*Subodh\*

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

Sd/-

**(N. K. Saini)**

**ACCOUNTANT MEMBER**

**ASSISTANT REGISTRAR**