

**IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH: 'I-2' NEW DELHI****BEFORE SHRI J.S. REDDY, ACCOUNTANT MEMBER
&
SMT. BEENA PILLAI, JUDICIAL MEMBER****I.T.A .No. 4868/Del/2014
(ASSESSMENT YEAR-2007-08)**

Avery Dennison (India) P. Ltd. Block B-1, Plot No. F-2, Mohan Cooperative Industrial Estate, Mathura Road, New Delhi. AAACA6163D	vs	ACIT (OSD), CIT-1, New Delhi.
Appellant by	Shri Tarun Arora, CA Sh. Gyan P. Srivastava, Adv.	
Respondent by	Smt. Susan D. George, Sr. DR	

&**I.T.A .No. 4933/Del/2014
(ASSESSMENT YEAR-2007-08)**

ACIT (OSD), CIT-1, New Delhi.	vs	Avery Dennison (India) P. Ltd. Block B-1, Plot No. F-2, Mohan Cooperative Industrial Estate, Mathura Road, New Delhi. AAACA6163D
Appellant by	Smt. Susan D. George, Sr. DR	
Respondent by	Shri Tarun Arora, CA Sh. Gyan P. Srivastava, Adv.	

Date of Hearing	05.10.2015
Date of Pronouncement	04.12.2015

ORDER

PER BENCH:

These are cross appeals for assessment years 2007-08 arising out of the CIT(A)'s order dated 06.06.2014. The brief facts as recorded by the Ld.AO are as under;

2. The assessee is a company, and has electronically filed its return on 31.10.2007 for A.Y. 2007-08 declaring income of Rs. 17,14,90,320/-. The assessee is a manufacturer and seller of the Group's products in Indian Market. Its main business is manufacturing and trading of pressure sensitive adhesive material, self adhesive paper, self adhesive films, tap sheets and trading of self adhesive paper and tags and labels. The assessee is a subsidiary of Avery Dennison Corporation, USA. During the relevant year the assessee's business was catagorised in two business segments being, Pressure Sensitive Materials ("PSM") and Retail Information Systems ("RIS"). The assessee had debited a sum of Rs. 3,69,29,533/- to its profit and loss account towards payment of service charges. The entity wise breakup of this payment is as below:

Name of the Company	Amount (in Rs.)
Avery Dennison Hong Kong B.V.	2,03,08,841
Dennison Manufacturing Company, USA	1,66,20,692

3. The assessee had entered into following International Transactions with its AE during the relevant financial year:

S.No.	Description of transaction	Method	Value (in Rs.)
1.	Purchase of Raw Material	TNMM	236,987,158
2.	Sale of finished goods	TNMM	55,297,411
3.	Import of printers/cutter/Slitter	TNMM	2,244,918
4.	Import of software-MFG PRO	TNMM	2,075,297
5.	Service fee paid	TNMM	36,929,533
6.	Service income	TNMM	239,009
7.	Reimbursement of expenses	TNMM	4,837,792

4. The assessee has been considered as the tested party, to test the Arms Length Price ("ALP") of the service charges paid for the support services received from Avery Dennison USA, and Avery Dennison Manufacturing Company Co.USA. For the purpose of bench marking the International Transactions, Transactional Net Margin Method ("TNMM") was selected as the MAM by the assessee, with Operating Margin ("OP/TC"), as the profit level indicator to determine the ALP. The assessee received services from its AE's, in lieu of which it had made a payment of Rs. 36,929,533/-.

The Services and the benefits claimed to have been received by the assessee from its AE's include the following;

S.No.	Description of Service	Benefits derived
1.	Marketing Services	<i>Increase in sales due to customized solutions and customer relationships;</i> <i>Improvement in reliability and quality by way of ensuring compliance with safety standards/ASTM standard</i>

		<p><i>testing of products being marketed;</i></p> <p><i>Low cost high quality services provided on a need basis;</i></p> <p><i>High quality marketing material at low cost;</i></p>
2.	GVP Services	<i>Provides with list of people available on call, having intensive knowledge in Avery's products and business model</i>
3.	VIPFS Services	<p><i>Regular support from technical experts with regard to usage of the software/platforms on a need basis;</i></p> <p><i>Access to high quality training manuals which help the employees in operating the complex software/platforms</i></p>
4.	Ticketing Hub Services	<p><i>Access to critical software/platform that are used for printing and order processing. Without such software/platform, the assessee would not be able to operate;</i></p> <p><i>Ability to effectively and efficiently manage vast amount of variable data that is required for undertaking production of tags/labels;</i></p>
5.	Material Division-Marketing Services	<p><i>Received ASTM support for adhering to regulatory safety standard for products;</i></p> <p><i>Access to the conversation with college, where its employees as well as customers participate during the year.</i></p>
6.	Accounting and Administration Services	<i>High value support services from industry experts who are able to provide forecast with higher accuracy</i>

		<p><i>by analyzing industry trends, demand trends etc. on a need basis;</i></p> <p><i>Based on the periodic review of actual performance with budgeted/forecasted performance, the appellant is able to identify and rectify the reasons for the variations;</i></p> <p><i>Improved efficiencies and lowering of cost leading to increased margins;</i></p>
7.	Financial Services	<p><i>High level support services from industry experts who are able to manage ADIPL's finances efficiently on a need basis;</i></p> <p><i>Cost savings in terms of loan/insurance facilities due to higher bargaining power of AEs;</i></p> <p><i>Identify areas where cost escalation is happening and suggesting strategies for lowering product cost including renegotiation with vendors, suggesting alternative materials etc.</i></p>
8.	Product Research And Development	<p><i>High level support services from technical experts who are able to resolve the technical issues faced by the appellant or its customers on a need basis</i></p>
9.	Operations and Logistic Support	<p><i>High value operational support services from personnel of the AEs who have significant experience in handling the similar operations in various jurisdictions, worldwide on a need basis;</i></p> <p><i>Reduction in cost by way of</i></p>

		<p><i>identification of safety / quality hazards and their timely rectification;</i></p> <p><i>Reduction in cost of sourced raw materials and freight services due to higher bargaining power of the AEs through global vendor relationships;</i></p> <p><i>Ensuring timely supply of raw material;</i></p>
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The assessee determined the mean OP/TC at 3.51% in its TP Study on the basis of 17 comparable companies selected by it. As the assessee achieved an operating profit at 10.99% for the relevant year, it was concluded by the assessee, in its TP Study that, the international transaction with its AE's are at Arm's Length.

5. The ld. AO made a reference u/s 92CA(i) to the ld. Additional Commissioner of Income Tax Transfer Pricing Officer, 1(1) ("Ld. TPO"). The ld.TPO disagreed the TP Study prepared by the assessee. The ld. TPO held that the assessee has not been able to show that, the service rendered by the AE have actually resulted in any benefit to the assessee He held that, no independent party would have made a payment of Rs. 3,69,29,533/- to its AE's on account of such service in uncontrolled circumstances. The Ld.TPO held that CUP as the most appropriate method (MAM), for arriving at the ALP of the international transaction, for payment of service fee. The Ld.TPO determined the ALP at -NIL- by applying CUP, thereby making an adjustment of Rs.3,69,29,533/-.

6. On the basis of the ld.TPO's order, the Ld.AO, passed final assessment order u/s. 143(3) r.w.144C(3) of the Act. Aggrieved by the order of the ld.AO, the assessee preferred an appeal before the ld. CIT(A).

7. Before the ld. CIT(A), the assessee submitted various arguments to substantiate its claim that, it has received services and benefits in lieu of payments of service fee to its AE's. The ld. CIT(A) reduced the TP adjustment. He held that, in the case of some of the services being marketing services, VIPFS Services, Operational and Logistics services, research and development services, there is no benefit derived by the assessee. In respect of remaining services being Ticketing Hub services, GVP services, Accounting and Administration services and Financial services, the ld. CIT(A) held that the assessee has received benefits. The ld. CIT(A), restricted the TP adjustment to Rs. 1,66,18,290/-.

8. Aggrieved by the order of the ld. CIT(A) both the assessee as well as the Revenue are in appeal before us.

9. The grounds of appeal raised by the assessee are as under:

1.1 *"The the Hon'ble CIT(Appeals) erred in fact and law by upholding the order of the ld. AO/ld. TPO wherein the AO/TPO has held the Appellant's international transaction of Receipt of Services with its Associated Enterprises does not satisfy the arm's length principle envisaged under the Act and thereby partly upholding an adjustment of INR 1,66,18,290 and in doing so have grossly erred by not appreciating the commercial wisdom/expediency of the appellant;*

1.2 *not appreciating the business model of the appellant and also rejecting the appellant's economic analysis of*

benchmarking closely interlinked transactions using Transactional Net Margin Method (TNMM). Further, the AO/TPO/CIT(A) grossly erred by applying comparable uncontrolled price (CUP) method without providing any comparable uncontrolled transactions/data for the computation of the ALP;

- 1.3 failing to appreciate that based on the acceptance of “whole entity approach” selected by the Appellant for application of the most appropriate method for benchmarking the international transactions, which has also been accepted by the ld. TPO (for all the other international transactions), the margins earned by the Appellant have been determined including international transaction of Receipt of Services;*
 - 1.4 ignoring sufficient evidences provided by the appellant and thereby, based on his own conjectures and surmises, concluding that the services availed by the Appellant from its AE were in nature of ‘duplicate’ and ‘shareholder’ services which have not conferred any commercial benefit upon the Appellant;*
 - 1.5 by not considering that the cost allocation methodology adopted by the AEs for allocation of costs with respect to rendering of services was in line with internationally accepted methodologies and by adopting adhoc basis of appropriating the service charges paid by the appellant amongst various services availed from the AEs.*
- 2. The CIT(A) has erred in law by upholding the reference made by the AO to the TPO by not appreciating that such a reference suffers from jurisdictional error as the AO has not recorded any reasons in the assessment order based on which he reached the conclusion that it was ‘necessary or expedient’ to refer the matter to the TPO for computation of the arm’s length price (ALP), as is required u/s 92CA(1) of the Act.*

3. *The CIT(A) has erred in law by upholding the adjustment made by the TPO/AO thereby by not appreciating that while making the said adjustment the TPO/AO have not satisfied the conditions set out in section 92C(3) of the Act.*

4. *That the AO has erred both in facts and in law, in initiating penalty proceedings u/s 271(1)(c) and 271G. The above grounds of appeal are mutually exclusive & without prejudice to each other. The Appellant prays for leave to add, alter, amend and/or modify any ground of appeal at or before the hearing of the appeal.”*

10. The grounds of appeal raised by the Revenue are as under:

1. *“On the facts and in the circumstances of the case, the ld. CIT(A) has erred in holding 55% of the total service paid during the year pertained to Marketing service (RVL-Sell) VIPFS services, Marketing service (Material segment), operational and logistics service, R&D service and ticketing hub services thereby determining the ALP of the transactions of service fee at Rs. 2,03,11,243/- against Nil computed by the TPO and restricting transfer pricing adjustment to Rs. 16,61,828/- against Rs. 3,69,29,533/- as computed by the TPO.*

2. *The appellant craves leave for reserving the right to amend, modify, alter, add or forego any grounds of appeal at any time before or during the hearing of this appeal.”*

11. We shall first deal with the ITA no.4868/Del/2014, being appeal filed by the assessee.

ITA no.4868/Del/2014

12. The ld. AR for the assessee contended before us that:

- The ld. CIT(A)’s approach is against the well settled TP principles, as on the one hand, he has accepted the overall TNMM analysis using aggregation approach conducted by the assessee and on the other hand, has rejected one

element of cost which is also a part of the overall TNMM analysis, thereby adopting a contradictory approach.

- The assessee's case, TNMM is the most appropriate method for bench marking of the international transactions undertaken by the assessee during the year.
- the ld.CIT(A) did not appreciate the arm's length justification submitted by the assessee, demonstrating the substantial cost-benefit derived by it of intra-group services;
- the ld. CIT(A) disregarded the contemporaneous evidences submitted by the Assessee demonstrating the receipt of the intra-group services and the benefit received from them.

13. It is submitted by the ld. AR that the services received from the AE's have helped the assessee in increasing its sales, increasing its customer base, increase in higher selling price received assistance towards the order processing provided to the customers, capturing customer data etc. The services from the AEs have also lead to the reduction in the cost incurred towards purchase of raw materials and logistics etc. It has been submitted by the Ld.AR that, the receipt of services was not disputed by the ld. CIT(A)/AO/TPO. The ALP was determined at NIL by adopting CUP as the MAM, on the ground that no benefit has accrued to the assessee due to those services. The Ld.AR submitted that such rejection is not in accordance with law.

14. The Ld.AR further submitted that the international transactions entered into by the assessee are intrinsically linked to

the business operations of the two segments of the assessee and that the nature of the activities undertaken by the assessee under the two segments, being PSM and RIS, are closely linked with each other and played a critical role for delivering the intra group services received from the AE's in the business operations of the segments.

15. The AR placed his reliance on the jurisdictional Delhi High Court in the case of Sony Ericson Mobile Communication India Pvt. Ltd., reported in TS-96-HC-2015(DEL)-TP.

16. The Ld.DR on the other hand relied on the orders passed by the authorities below. She argued that cost has been allocated in a blanket fashion on the basis of the sales without any specific nexus to the services received. The Ld, DR places reliance on the decision of Bangalore bench in the case of Gems Plus bearing ITA no. 352/Bang/2009 and submitted that the order of the Ld.TPO has to be restored by holding CUP as the MAM. She further submitted that, as no benefit was derived by the assessee in these transactions, the ALP has rightly been determined at -NIL-. She further submitted that huge payments have been made to AE without any rhyme or reason and that no assessee would have made such payments to unrelated parties.

17. We have heard the rival contentions. On a careful consideration of the facts and circumstances of the case and perusal of the papers on record and the orders of the authorities below and case law cited, we hold as follows. The issues before us are;

A. Whether on the facts and circumstances of the case, the Ld. CIT(A) is right in holding that the services rendered under the

agreement entered into between the assessee with its AE's is partly at arms length?;

B. Whether on the facts and circumstances of the case, the Ld. CIT(A) is right in upholding the TPO's finding that the MAM, for benchmarking the international transactions, must be at CUP and not TNMM as done by the assessee ?

C. Whether on the facts and circumstances of the case, the Ld. CIT(A) is right in holding that, the transactions entered into by the assessee with the AE's are not interlinked and cannot be aggregated?

18. During the relevant year under consideration we notice that the assessee had entered into an Intercompany Service Agreement with its AE's being "Dennison Manufacturing Company, USA" and "Avery Dennison Hong Kong B.V" to carry out International Transactions being Purchase of Raw Material, Sale of finished goods, Import of printers/cutter/Slitter, Import of software-MFG PRO, Service fee paid, Service income, Reimbursement of expenses.

19. The assessee had conducted FAR analysis as a part of TP documentation, wherein it had aggregated the international transactions pertaining to PSM segment and RIS segment and had determined the ALP, by applying TNMM as MAM and selecting OP/Sales as the relevant PLI.

20. On perusal of the TP Study, we observe that each transaction are interlinked with each other. We notice that the assessee has treated the agreement as a whole, and has applied TNMM, in respect of the services received to arrive at the ALP. It is observed that the

ld. CIT(A) accepted the contentions of the assessee that, intra group services were received by the assessee as per the agreement, and that these are critical, and linked to the core business operations of the assessee. However, the Ld.CIT(A) held that certain services specified in the agreement did not result in any benefit to the assessee.

21. All the services received are part of composite contracts/agreements which in our view cannot be unbundled. IN this context, Hon'ble Delhi High Court in the case of Sony Ericson Mobile Communication India Pvt. Ltd. (supra) has observed as under;

“93.....These anomalies arise on account of fact that there was no apportionment and division of the transactional compensation, but the packaged transaction has been bifurcated and divided into two. This position is not acceptable as it is irrational and unsound.

“137. The question of aggregation and disaggregation of transactions when the TNM Method or even in other methods is sought to be applied, must have reference to the strength and weaknesses of the TNM Method or the applicable method. Aggregation of transactions is desirable and not merely permissible, if the nature of transactions taken as a whole is so inter-related that it will be more reliable means of determining the arm's length consideration for the controlled transactions. There are often situations where separate transactions are intertwined and linked or are continuous that they cannot be evaluated adequately on separate basis.....”

(Emphasis supplied)

22. Similarly, in the case of Maruti Suzuki India Limited vs. Additional Commissioner of Income Tax (I.T.A. No. 5237/Del/2011), it was held that:

11. The another purpose for which the royalty has been paid to the SMC is the use of license information for the engineering, design and development, manufacture, testing quality control, sale and after sales service of products and parts. Thus, we agree with the submission of the ld. Counsel of the assessee that royalty thus paid by the assessee to SMC constitute a single/inserverable/indivisible contract/package which provided assessee the exclusive right and license to manufacture and to sell the licensed product for a specified limited duration. All others rights vested in the license agreement including technology, technical know how and trade mark are linked to the core right to manufacture and sell licensed products....

13.....we place reliance upon the decision of the Hon'ble Apex Court in the case of Vodafone International Holdings B.V. vs. UOI (Civil Appeal No. 733 of 2012) wherein the Hon'ble Court held that it is not open to revenue authorities to split an agreement when the parties to the agreement themselves have not contemplated a split up in the agreement and have considered the agreement as an entire package. The relevant citations in this regard has been brought out in detail in the assessee's submission above. Thus, we find that for the purpose of computing the arm's length price, The TPO has re-written the agreement/transaction undertaken by the assessee by artificially segregating the single transaction of payment of royalty into two transactions of payment of royalty for use of brand name and for use of technology. We agree with such re-writing of transaction undertaken by the assessee is inconsistent with the factual realities of the case and is also contrary to the various judicial pronouncements. In this regard, the following case laws referred by the assessee's counsel are germane and supports the case of the assessee.

- i) *Hon'ble Delhi High Court decision in the case of Sony India (P) Ltd. vs. DCIT (ITA No. 1189/D/2005)*
- ii) *Hon'ble Delhi High Court decision in the case of CIT vs. EKL Appliances (ITA No. 1068/2011 and 1070/2011).*

(Emphasis supplied)

23. From the above discussion we are of the considered opinion that the agreement is an intrinsic one and that it is wrong to split the same and hold that some services are at arm's length and some services are not.

24. The Ld.CIT(A) accepted TNMM to arrive at the ALP, in respect of certain services received by the assessee and in the same breath, has rejected the analysis undertaken by the assessee under the TNMM in respect of other services. We are informed by the assessee that, the authorities have accepted TNMM as MAM in the subsequent years. The Revenue has to be consistent in its approach. In our view, the TPO analysis of the assessee using TNMM as the MAM has to be accepted. When there is an agreement for services and certain services out of a bundle of services are undisputedly rendered, the entire agreement has to be viewed as a whole. Whether the services have actually resulted in a benefit to the assessee or not is not material. The conclusion of the Ld.TPO that the services have not resulted in any benefit and that no independent entity would have made such a payment is in the realm of surmises and conjunctures and not backed by any material. Thus the ALP

determined by the assessee company is accepted and the TPO adjustment is deleted.

25. In alternative, the OECD guidelines has quoted by the ld. TPO in the draft assessment order. The Ld.TPO, states that, for ascertaining the ALP of intra-group services, CUP method or cost plus method should be applied. The ld.AR submits that, CUP method would be applicable where there is a comparable service provided between independent enterprises, or by the AE providing the services to an independent enterprise. In the absence of such transactions or data, the Ld. AR submitted that if the said international transaction has to be benchmarked, under cost plus method. The Ld.AR submitted that the services received by the assessee are charged by the AE's as below;

- Cost Plus Method may be adopted for arriving at the ALP in the assessee's case. The AE in respect of the PSM segment of services being marketing, accounting and administration, financial services product research and development and operations and logistics have charged the service fees by allocating the full cost incurred in providing support service. The allocation is based on budgeted sales and the AE applies mark-up of 5% on cost.
- In respect of RIS segment, the AE (Dennison Manufacturing Company, USA) performed various services. The AE has charged a mark-up of 4% on the cost incurred in providing Marketing support services under RIS segment. And,

- in respect of GVP services, VIPFS services and Ticketing Hub services at was charged without margin.

26. It is stated at the Bar that, for A.Y. 2010-11, the DRP has accepted the ALP determined by the assessee, in respect of GVP services, VIPFS services and Ticketing Hub Services.

27. In view of the above discussion, we are of the considered opinion that with regard to PSM and RIS segments, even if cost plus method is taken as the MAM, the markup charged by the AEs is within the +/-5% range, allowed under second proviso to section 92C of the Indian Income Tax Act, 1961, these services can be considered to be at arm's length;

Regarding GVP services, VIPFS services and Ticketing Hub Services, the service charges paid by the Assessee, represents the actual cost incurred by the AEs, without any markup. Hence these can be considered to be at arm's length.

28. Based on the above discussion, we are of the opinion that the services received by the assessee should be considered to be arm's length.

29. Accordingly, assessee's appeal is allowed.

In ITA no. 4933/Del/14

The grounds raised in the appeal filed by the Revenue, has been discussed at length by us above. In view of the discussions in the preceding paragraphs, we dismiss the grounds raised by the Revenue.

We therefore dismiss the appeal filed by the Revenue.

**The order is pronounced in the open court on
04/12/2015**

Sd/-

(J.S. REDDY)

ACCOUNTANT MEMBER

Dated: 04/12/2015

**Kavita, P.S.*

Sd/-

(BEENA PILLAI)

JUDICIAL MEMBER

Copy forwarded to:

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

ASSISTANT REGISTRAR
ITAT NEW DELHI

		Date
1.	Draft dictated on	05.10.2015/12.10.15
2.	Draft placed before author	12.10.15
3.	Draft proposed & placed before the second member	
4	Draft discussed/approved by Second Member.	
5.	Approved Draft comes to the Sr.PS/PS	09.12.15
6.	Kept for pronouncement on	04.12.15
7.	File sent to the Bench Clerk	09.12.15
8.	Date on which file goes to the AR	
9.	Date on which file goes to the Head Clerk.	
10.	Date of dispatch of Order.	