

आयकर अपीलीय अधिकरण, मुंबई न्यायपीठ, K, मुंबई।

**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCHES "K", MUMBAI**

**Before ShriG.S. Pannu, Accountant Member, and
ShriRavishSood, Judicial Member**

**ITA No. 5189/Mum/2015
Assessment Year: 2011-12**

S.B. & T Designs Ltd. 9, Yusuf Bldg, R.No. 15, 1st Floor, A.R. Street, Pydhonie Mumbai-400 003	बनाम / Vs.	Asstt. Commissioner of Income Tax, 8(1)(2) AayakarBhavan, Maharishi Karve Road, Mumbai - 400 020.
(APPELLANT)		(Respondent)
PAN AAICS6223L		

Appellant by	Mr. P. Daniel
Respondent by	Mr. N.K. Chand
सुनवाई की तारीख/Date of Hearing:	03/02/2017
आदेश की तारीख /Date of Order:	03/05/2017

आदेश / ORDER

PERRAVISH SOOD, J.M:

The present appeal is directed against the order passed by the AO u/s. 143(3) r.w.s 144C(13) of the Income Tax Act, 1961 (for short 'Act'). The assessee assailing the order of the AO had therein raised the following grounds of appeal before us:-

"1. On the facts and in the circumstances of the case, the order passed by the Learned Assessing Officer u/s. 143(3) r.w.s. 144C (13) of the Act is bad both in the eye of law and on facts.

2. *On the facts and circumstances of the case, the Learned Assessing Officer has erred, both on law and on facts in assessing the loss at Rs. 1,09,38,700/- as against the loss declared by the appellant of Rs. 2,51,24,840/-.*

3. (i) *On the facts and in the circumstances of the case, the Learned A.O. has erred both on facts and in law in making an addition of Rs. 1,27,40,219/- as difference in arm's length price determined by the Transfer Pricing Officer (TPO) and in pursuance of DRP's order in r/o sale of goods to Associated Enterprise.*

(ii) *That on the facts and in the circumstances of the case and in law, the Learned A.O./TPO erred in rejecting the economic analysis undertaken by the assessee for determination of the arms length price of international transaction entered into by the Appellant with its Associated Enterprise. ("AE's")"*

(iii) *That on the facts and in the circumstances of the case and in law, the Learned A.O./TPO erred in rejecting the segmental profit and loss for AE and Non AE segment, relying on the Tax Audit Report to conclude that the Appellant is not maintaining separate audited financials for these segmental information as disclosed in the transfer pricing report had been created to artificially allocate costs and thereby reducing losses.*

(iv) *That on the facts and in the circumstances of the case and in law, the Learned A.O./TPO, erred in not taking into consideration that the assessee has reported the segment information as per AS-17 and identified the geographical segment.*

(v) *That on the facts and in the circumstances of the case and in law, the Learned A.O./TPO, erred in rejecting the internal TNMM as the most appropriate method and benchmarked the international*

transaction of the Appellant with its AES at entity level by using external comparables.

(vi) That on the facts and in the circumstances of the case and in law, the Learned A.O./TPO, erred in its choice of comparables based on such search, which were not functionally comparable with the appellant, having regard to their risk and functional profile.

It is prayed that the additions made may please be deleted or in the alternative, the assessment be set aside.

2. Briefly stated, the facts of the case are that the assessee company which is engaged in the business of manufacturing and export of studded jewellery had e-filed its return of income on 14/10/2010 declaring total loss of Rs. 2,51,24,840/-, which was processed as such u/s. 143(1) of the 'Act'.

3. The case of the assessee company was taken up for scrutiny assessment u/s. 143(2). That during the course of the assessment proceedings the AO taking cognizance of the international transactions entered into by the assessee company with its Associate Enterprises (AE's) during the year, as under:-

- | | |
|--|---------------------|
| (i). Export of studded jewellery to AE's | :Rs. 11,55,92,714/- |
| (ii). Import of raw material from AE's | :Rs. 5,74,74,683/- |

,thereinreferred the matter to the Transfer Pricing Officer, Mumbai (TPO) for determining the Arms Length Price (ALP) in respect of the said transactions. The TPO during the course of the proceedings before him therein observed that the assessee had used internal TNMM as the Most Appropriate Method (MAM) to determine the ALP of the export of goods to the AE's and had considered itself as the tested party. The

TPO observed that the assessee had computed the PLI as "Operating Profit/Total Cost". It was further observed by the TPO that the assessee had computed the PLI as the arithmetic mean of the comparables (i.e. Non-AE transactions by the assessee) at (7.70%), and had computed its own PLI (i.e. AE transactions only) at (2.78%), and in the backdrop of the same had therein concluded that PLI as Operating Profit/Total cost earned by the assessee was better than that of the arithmetic mean of the PLI of the comparables, and as such the international transactions so carried out by it were found to be at arms length.

4. The TPO on a perusal of the aforesaid facts therein concluded that the allocation of various costs done by the assessee to its AE and Non-AE transactions was not proper, as well as the base taken by it was incorrect. The TPO thus being of the view that the profit figure arrived by the assessee was not reliable, thus in light of his aforesaid conviction rejected the self-serving allocation exercise done by the assessee. The TPO further on the basis of search done in capital line database and using various filters identified 25 comparable companies, which as per him were doing the same business as that of the assessee. That during the course of the proceedings before the TPO, the list of companies alongwith the working of Operating Margin (OP/OC) was given to the assessee, and the latter was called upon to show cause as to why the internal TNMM should not be rejected and the External TNMM may not be adopted as the Most Appropriate Method (MAM) for determining the ALP of the transactions of the assessee with its AE's. The TPO further observing that the sale transactions were more than the purchase transactions, therefore took the PLI as OP/OC, as against OP/OI. The TPO further considering the objections of the assessee,

wherein the latter after accepting the selection of 17 comparable companies had therein restricted his objections in respect of the remaining 8 comparable companies only, therein came up with the final set of comparables, as under:-

Sr. No.	Name of the comparable company	OP/OC
1.	Winsome Diamonds (Seg.)	3.41
2.	Titan Company (Seg.)	9.63
3.	Goenka Diamond & Jewels Ltd. (Seg.)	10.10
4.	Goldiam Intl. (Seg.)	6.19
5.	SJ Corporation Ltd.,	4.97
6.	Swarnsarita Gems Ltd.,	6.83
7.	Shantivijay Jewels Ltd.	2.19
8.	Rajesh Exports Ltd.	1.73
9.	Deep Diamond India Ltd.	11.9
10.	Shree Ganesh Jewellery House (I) Ltd.	6.61
11.	Thangamayil Jewellery Ltd.	9.67
12.	Kanani Industries Ltd.	12.22
13.	TribhovandasBhimjiZaveri Ltd.	8
14.	PC Jeweller Ltd	11.17
15.	InterjewelPvt. Ltd.	3.79
16.	Gili India Ltd.	6.54
17.	Brightest Circle Jewellery Pvt. Ltd.	7.48
18.	Kays jewels Pvt. Ltd.	4.93
19.	Kalyan Jewellers India Pvt. Ltd.	1.96
20.	A B Jewels Pvt. Ltd.	0.71
21.	Gitanjali Export Corp (Seg.)	6.26
22.	Classic Diamond (Seg.)	4.59
	Average	6.40

, and computed the average mean of the PLI of the aforesaid comparables at 6.40%, as against the PLI (OP/OC) of the assessee which was worked out by him at (4.37%). The TPO thus observing that the PLI of the assessee was (4.37%) was lower than the arithmetic mean of the PLI of the comparables, therein computed the ALP of the transactions carried out by the assessee with its AE's, as under:-

ALP of the Transaction	
Export Sale to AE	11,55,92,714
Operating Profit / Cost Ratio of the Assessee	-4.37%
Operating cost of the assessee on AE export	12,08,74,949
Operating Profit/Cost Ratio of the comparable	6.40
ALP of the Export Sale to AE	12,86,10,946
Difference ALP & Export sale to AE	1,30,18,232
(+5%) of export sale to AE	57,79,609

5. The TPO observing that since the exports carried out by the assessee to its AE's (i.e.Rs. 11.56 crores) were more than the imports made from the AE's (i.e Rs.5.74 crores), he thus for the purpose of benchmarking of both the purchase and sale transactions with the AE's, therein took the export transactions as the base. The TPO thus in the backdrop of his aforesaid observations being of the view that since the PLI of the assessee was lower than the PLI of comparables, therefore did not accept the ALP computed by the assessee as regards the sales and purchases to and from the AE's, and thus proposed an upward adjustment of Rs. 1,30,18,232/- to the total income of the assessee.

6. The AO on receiving the order of the TPO therein passed the draft assessment order u/s. 143(3) r.w.s. 144C(1) on 03/03/2015. The assessee aggrieved with the adjustments proposed by the AO in the assessment order, therein filed objections before the DRP in respect of the upward adjustment of Rs. 1,30,18,232/- proposed by the TPO in respect of the international transactions of the assessee with its AE's. The DRP being of the view that the segmental accounts furnished by the assessee were not authentic due to the reason that the expenses have been artificially allocated to AE and Non-AE segment and were not shown on actual basis, as well as that the expenses pertaining to

marketing efforts and various risks associated with the sale to Non-AE transactions have been bifurcated to AE segment and were not shown on actual basis, therefore, concluded that the proportional allotment of other costs on the basis of sales to AE and Non-AE being not correct, thus could not be accepted as such. It was further observed by the DRP that as the Non-AE segment pertaining to local sales in India had different FAR as compared to AE segment, therefore the said respective segments were not comparable due to different FAR. The DRP thus being of the view that as adopting of internal TNMM required a very high degree of accuracy of financial results as there is only one comparable to which AE transactions are to be tested, thus holding a conviction that the assessee had wrongly resorted to testing the transactions of AE segment as against the Non-AE segment pertaining to local sales in India, as the respective segments had different FAR, thus concluded that the AO/TPO had correctly rejected internal TNMM and applied external TNMM in the case.

7. That as regards the challenge by the assessee in respect of the comparables selected by the TPO, the DRP found favor with the contention of the assessee that in the case of 3 comparables, viz. M/s. Brightest Circle Jewellery Private Limited, M/s. Gili International Limited and M/s. Goldiam International Limited, the related party transactions (RPT) were more than 25%, thus in the backdrop of the said factual position directed the AO/TPO to exclude the said 3 companies from the final list of comparables. The DRP further observed that M/s. Thangamayil Jewellery Ltd. which was a comparable selected by the TPO was functionally different as against the assessee company, therefore, on the said count directed the AO/TPO to exclude the said concern from the final list of comparables. The DRP in the backdrop of

the fact that the assessee had not objected to the inclusion of M/s Goenka Diamonds and Jewels Limited as a comparable, despite the fact that objection in respect of selection of the same as a comparable was raised by the assessee during the course of the proceedings before the TPO, therefore, in the backdrop of the aforesaid observations directed the AO/TPO to exclude only the aforesaid 4 comparables from the final set of comparable companies.

8. The AO giving effect to the directions to the DRP, therein passed the impugned order u/s. 143(3) r.w.s. 144C(13) and computing the average mean PLI of the 22 comparable companies at 6.17%, computed the PLI (OP/OC) of the assessee as under:-

Particulars	Adjustment as per DRP Directions
Export sale to AE	11,55,92,714
OP/OC of Assessee	-4.37%
Operating Cost of the Assessee on AE export	12,08,74,949
OP/OC of Comparable	6.17
ALP of the Export Sale to AE	12,83,32,933
Difference ALP & Export Sale to AE	1,27,40,219
(+5%) of export sale to AE	57,79,609

The A.O thus observing that the difference in ALP of the Export sale to the AE's and the Export Sales made by the assessee to its AE's amounted to Rs. 1,27,40,219/-, which was more than 5% of the export sales made to the AE's, therefore, going by the direction of the DRP carried out an upward adjustment of Rs. 1,27,40,219/- in respect of the international transactions undertaken by the assessee company with its AE's during the year under consideration.

9. The AO further observing that the assessee had defaulted to credit the payments relating to employees contribution to PF, ESIC and labour welfare fund on or before the prescribed due date, therein made an addition of Rs. 14,45,925/- u/s. 36(1)(v)(a) r.w.s. 2(24) (x) of the 'Act' in the hands of the assessee company. The AO thus deliberating on the aforesaid issues assessed the total loss of the assessee at (-) Rs.1,09,38,700/-, as against the returned loss of (-)Rs. 2,51,24,840/-.

10. The assessee company being aggrieved with the order of the AO passed u/s. 143(3) r.w.s. 144C(13) had therein carried the matter in appeal before us. During the course of hearing of the appeal it was submitted by the Ld. AR that it was the first year when the case of the assessee had been referred to the TPO, as the earlier years were accepted without making any such reference to the TPO. It was further submitted by the Ld. AR that in the subsequent years also the assessee company had suffered losses and additions had been made in its hands by rejecting the internal TNMM method adopted by the assessee to compute the ALP in respect of international transactions carried with its AE's. It was further averred by the Ld. AR that the TPO without assigning any reasoning had therein most arbitrarily rejected segmental allocation of cost done by the assessee in respect of its AE and Non-AE transactions. The Ld. AR further submitted that the observation of the DRP that the expenses pertaining to marketing efforts and various risk associated with the sale as regards Non-AE transactions had been bifurcated by the assessee to AE segment and not shown on actual basis, was absolutely misconceived and no material had been placed on record to disprove and dislodge the allocation of the expenses by the assessee to its AE and Non-AE segment. The Ld. AR in order to fortify his aforesaid contention had therein submitted that though the

local/domestic sales are included in its total sales, but however for the purpose of benchmarking the transaction the local/domestic sales had specifically been treated as incomparable, and as such had been bifurcated and shown separately. The Ld. A.R therein drew our attention to **Page 52** of its 'Paper book' (APB), wherein in **Col. No. 3**, the assessee had categorically earmarked the expenses in three segments, viz. AE segment, Non-AE (Comparable) segment and Non-AE (Uncomparable) segment. The Ld. A.R in the backdrop of the aforesaid submissions therein submitted that the DRP had misconceived the facts and therein wrongly observed at **Page 5 - Para 5.2.2** of its order that the Non-AE segment pertained to local sales in India and as such have different FAR as compared to AE segment, therefore the assessee and erred in failing to appreciate that the said respective segments were not comparable. The Ld. A.R referring to **Page 52** and **Page 13** of its APB therein submitted that the same were the part of its 'Annual report' wherein the segmental reporting containing the aforesaid factors stood mentioned. Per contra, the Ld. DR heavily relied on the orders of the lower authorities.

11. We have heard the authorized representatives of both the parties, perused the orders of the lower authorities and the material produced before us. We have given a thoughtful consideration to the facts of the case and are of the considered view that the adverse inferences drawn by the DRP in the hands of the assessee company are primarily backed by the following factors:

- i) That as per the DRP the segmental accounts furnished by the assessee are not authentic due to the reason that the expenses

have been artificially allocated to AE and Non-AE segment and are not actual.

ii) That as per the DRP the expenses pertaining to marketing efforts and various risks associated with the sale to Non-AE transactions have been bifurcated to AE segment and not shown on actual basis.

iii) That as per the DRP the Non-AE segment pertains to local sales in India and as such have different FAR as compared to AE segment, and in view of the same this segment is not comparable due to different FAR.

12. We have given a thoughtful consideration to the aforesaid observations of the DRP in the backdrop of the contentions raised by the assessee before us. We are of the considered view that the lower authorities except for alleging that the segmental accounts of the assessee are not authentic due to the reason that expenses have been artificially allocated to AE and Non-AE segment and are not actual, had however failed to substantiate the said observation by placing on record any concrete material or an irrebutable reasoning in support of its aforesaid observation. We rather after giving a thoughtful consideration to the facts of the case are of the considered view that no reasoning has been given by the lower authorities for rejecting the segmental accounts of the assessee and fortifying its observations as stood recorded to the contrary. We have further perused the observations of the DRP, wherein as per him the expenses pertaining to marketing efforts and various risks associated with the sales as regards the Non-AE transactions have been bifurcated to AE segment and as such not shown by the assessee on actual basis, as a result where of the said

proportional allotment of other costs on the basis of sale to AE and Non-AE, as per him was found to be incorrect. We are unable to persuade ourselves to be in agreement with the aforesaid observations of the DRP, and as matter of fact find that except for arriving at the aforesaid hollow and unsubstantiated observations in respect of bifurcation of the expenses pertaining to marketing efforts, nothing has been placed on record which could go to dislodge the aforesaid claim of the assessee and therein prove to the contrary that the assessee had allocated the expenses pertaining to marketing efforts and various risks associated with the sales carried out in respect of Non-AE transactions to its aforesaid AE segment, on a perusal of which we could persuade ourselves to conclude that the observations of the lower authorities did merit acceptance. That still further we find that the adverse inferences drawn by the DRP in the hands of the assessee by observing that the Non-AE segment of the assessee pertaining to local sales in India is not comparable to its AE segment due to different FAR, can safely be concluded to be misplaced in context of the adverse inferences so drawn by the DRP in the hands of the assessee on the basis of misconceived facts, because the fact as it so remains is that no such comparison between the Non-AE segment pertaining to the local sales in India had ever been put across as against the AE segment of the assessee. We after a perusal of Page 52 of the 'APB' to which our attention was drawn are persuaded to be in agreement with the contention of the Ld. A.R that the DRP had proceeded with on the basis of incorrect facts that the assessee had embarked on an infeasible comparison between Non-AE segment pertaining to local sales in India, as against its international transactions with its AE's, as the facts as they so emerge from the record therein reveals beyond any scope of doubt

that the assessee had specifically categorized and earmarked such Non-AE segment pertaining to local sales in India as 'Uncomparable', as a fall out of which it can safely and inescapably be concluded that the aforesaid observation arrived at by the DRP are devoid of any force and thus do not merit acceptance and cannot be sustained.

13. We have given a thoughtful consideration to the facts of the case, findings of the revenue authorities and the contentions raised by the representatives of both the parties before us. We are unable to persuade ourselves to subscribe to the view arrived at by the DRP in respect of the authenticity of the segmental reporting, veracity of the bifurcation of the expenses pertaining to marketing efforts and various risks associated with the sales pertaining to the Non-AE transactions, which as alleged by the DRP had been bifurcated to the AE segment and not shown on actual basis, as well as the misconceived observation that the assessee had resorted to a comparison between the Non-AE segment local sales of India, as against the AE segment, which we find is absolutely incorrect. We are absolutely not at all impressed by the observations of the lower authorities, as we find that the latter except for raising hollow and unsubstantiated allegations in their attempt to dislodge the claim of the assessee, had however miserably failed to prove on the basis of any concrete material as to how the said claim of the assessee is not found to be in order and is liable to be rejected, nor pointed out as to what as per the lower authorities would have been the correct allocation of expenses and other such factors on the basis of which fair results could be arrived at in the hands of the assessee. We are afraid that a claim of an assessee cannot be dislodged merely on the basis of allegations and surmises, but can only be so done on the basis of substantial material which could go to irrebutably disprove and

consequently dislodge the claim of the assessee, with a clear observation as to what fairly could be held to be the correct state of affairs. We thus not being persuaded to subscribe to the observations of the lower authorities, therein set aside the order of the AO passed u/s 143(3) r.w.s 144C(13), to the extent the latter had given effect to the order of the DRP and therein set aside the rejection of the internal TNMM as the most appropriate method adopted by the assessee for benchmarking the international transactions of the assessee with its AE's, and restore the matter to the file of the AO to give consequential effect to the same.

14. The appeal of the assessee is thus allowed for statistical purpose.

Order pronounced in the open court on 03/05/2017.

Sd/-
(G.S. Pannu)

लेखा सदस्य / ACCOUNTANT MEMBER

Sd/-
(Ravish Sood)

न्यायिक सदस्य / JUDICIALMEMBER

मुंबई Mumbai; दिनांक Dated : 03/05/2017

Rahul Dhoke, P.S./नि.स.

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. आयकर आयुक्त(अपील) / The CIT, Mumbai.
4. आयकर आयुक्त / CIT(A)- , Mumbai
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, मुंबई / DR,
ITAT, Mumbai
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

उप/सहायक पंजीकार (Dy./Asstt.Registrar)

आयकर अपीलीय अधिकरण, मुंबई / ITAT, Mumbai