

**IN THE INCOME TAX APPELLATE TRIBUNAL  
(DELHI BENCH 'I-2' : NEW DELHI)**

**BEFORE SHRI N.K. SAINI, ACCOUNTANT MEMBER  
and  
SHRI KULDIP SINGH, JUDICIAL MEMBER**

**ITA No.510/Del./2016  
(ASSESSMENT YEAR : 2011-12)**

Hyundai Rotem Company, vs. ACIT, Circle 2 (1)(1),  
N – 3, 3<sup>rd</sup> Floor, New Delhi.  
South Extension, Park No.1,  
Delhi – 110 049.

**(PAN : AABCK6367L)**

**(APPELLANT)**

**(RESPONDENT)**

ASSESSEE BY : Shri Salil Kapoor, Advocate and  
Ms. Ananya Kapoor, Advocete  
REVENUE BY : Shri H.K. Choudhary, CIT DR

Date of Hearing : 05.10.2017

Date of Order : 22.11.2017

**ORDER**

**PER KULDIP SINGH, JUDICIAL MEMBER :**

The Appellant, Hyundai Rotem Company (hereinafter referred to as 'the taxpayer') by filing the present appeal sought to set aside the impugned order dated 30.12.2015, passed by the AO in consonance with the orders passed by the ld. DRP/TPO under section 143 (3) read with section 144C of the Income-tax Act, 1961 (for short 'the Act') qua the assessment year 2010-11 on the grounds inter alia that :-

***“1. On the facts and circumstances of the case and in law, the Ld. Assessing Officer ('AO') erred in referring the case to the Ld. Transfer Pricing Officer ('TPO'), which was bad in law.***

***2. On the facts and circumstances of the case and in law, the assessment order/directions passed by the Ld. AO / Ld. TPO / Hon'ble Dispute Resolution Panel CORP') are bad in law.***

***3. On the facts and circumstances of the case and in law, the Ld. AO / Hon'ble DRP erred in confirming the transfer pricing adjustment amounting to INR 17,60,73,335 of the appellant.***

***4. On the facts and circumstances of the case and in law, the Ld. AO/Hon'ble DRP/Ld. TPO erred in law and in facts by not taking cognizance of the fact that the same international transactions of appellant has been accepted by revenue authorities to be at arm's length in previous years.***

***5. On the facts and circumstances of the case and in law, the Ld. AO / Hon'ble DRP/Ld. TPO erred in law and in facts by not taking cognizance of the India Korea tax treaty. The Ld. AO / Hon'ble DRP / Ld. TPO should follow consistency in approach.***

***6. On the facts and in circumstances of the case and in law, the Ld. AO / Hon'ble DRP / Ld. TPO erred in misunderstanding appellant's business model and functional and risk profile.***

***7. On the facts and in circumstances of the case and in law, the Ld. AO/Hon'ble DRP/Ld. TPO erred by not accepting the economic analysis undertaken by the appellant in accordance with the provisions of the Act read with the Rules, and modifying the economic analysis for the determination of the ALP of the appellant's international transactions and holding that the international transactions are not at arm's length.***

8. *On the facts and in the circumstances of the case and in law, the Ld. AO / Hon'ble DRP/Ld. TPO erred in considering an inappropriate set of companies as comparables to the "support services" segment of the appellant.*

9. *On the facts and in the circumstances of the case and in law, the Ld. AO / Hon'ble DRP/Ld. TPO erred in law and in facts, by using incorrect filters.*

10. *On the facts and circumstances of the case and in law, the Ld. AO / Hon'ble DRP/Ld. TPO erred in using data not existing at the time of preparation of documentation prescribed under Rule 10D ("Rule 10D documentation") of the Income Tax Rules, 1962 ("the Rules") by the Appellant.*

11. *On the facts and in the circumstances of the case and in law, the Ld. AO/ Hon'ble DRP/Ld. TPO erred in using single year data as against the multiple year data used by the Appellant, to compute the arm's length price of the international transaction of the appellant using Transactional Net Margin Method ("TNMM") method.*

12. *On the facts and circumstances of the case and in law, the Ld. AO/ Hon'ble DRP/Ld. TPO erred in adding the amount pertaining to reimbursement of expenses by AE to the operating revenue and operating costs of the appellant even though the same was in the nature of pass through cost.*

13. *On the facts and circumstances of the case and in law, the Ld. AO/ Hon'ble DRP/Ld. TPO erred in not excluding third party expenses while calculating operating profits/operating costs as profit level indicator ("PLI").*

14. *On the facts and circumstances of the case and in law, the Ld. AO/ Hon'ble DRP/Ld. TPO erred in not making suitable adjustments to account for*

*differences in the risk profile of the appellant vis-a-vis the comparables.*

**15. On the facts and circumstances of the case and in law, the Ld. AO/ Hon'ble DRP/Ld. TPO erred by not applying the Proviso to section 92C of the Act and has failed to allow the appellant the benefit of variation of 5 percent in determining the Arm's Length Price."**

2. Briefly stated the facts necessary for adjudication of the controversy at hand are : M/s. Hyundai Rotem Company is a South Korean part of the Hyundai Motor Group providing total rail business solutions throughout the world ranging from manufacturing of rolling stock to the supply of turnkey rail systems. The taxpayer is also into advanced defence industry products and supply of industrial plants and environment-friendly facilities. The taxpayer has reputation of an integrated heavy industry company. Major international transaction of the taxpayer is qua provision of administrative support services. During the year under assessment, the taxpayer entered into international transactions as under :-

<b>Sl. No.</b>	<b>Nature of transaction</b>	<b>Value (Rs.)</b>
<b>1</b>	<b>Rendering of administrative support services</b>	<b>63829826</b>
<b>2</b>	<b>Reimbursement of expenses to AE</b>	<b>2354284</b>
<b>3</b>	<b>Reimbursement of expenses by AE</b>	<b>388153141</b>

3. The taxpayer in order to benchmark its international transaction used Transactional Net Margin Method (TNMM) as Most Appropriate Method (MAM) and Operating Profit / Operating Cost (OP/OC) has been chosen as Profit Level Indicator (PLI). The taxpayer chosen 11 comparables in its transfer pricing report, but subsequently on ground of updated financial data available for FY 2010-11, 5 comparables have been rejected on ground of passing the filters used by the taxpayer and one additional comparable was taken and as such, total 7 comparables have been taken. However, Transfer Pricing Officer (TPO) proposed 6 comparables having average mean of 18.22% as against OP/OC of tested party at 9.01%. However, on the basis of objection raised by the taxpayer, TPO selected 7 comparables having average of 16.38% as against OP/OC of the taxpayer at 9.01%. The taxpayer also claimed risk adjustment which has been rejected by the TPO on failure of the taxpayer to discharge its onus. Consequently, TPO proceeded to calculate the Arm's Length Price (ALP) of international transaction qua provision of support services as under:-

<b>Total Cost</b>	<b>Rs.1,221,612,094</b>
<b>ALP at a margin of 16.38%</b>	<b>Rs.1,421,712,154</b>
<b>Price received</b>	<b>Rs.1,245,638,819</b>
<b>Adjustment u/s 92CA</b>	<b>Rs.176,073,335</b>

and thereby enhanced income of the taxpayer by Rs.17,60,73,335/- on account of transfer pricing adjustment.

4. The taxpayer carried the matter before the Id. DRP by way of raising objections which are rejected by the Id. DRP. Feeling aggrieved, the taxpayer has come up before the Tribunal by way of filing the present appeal.

5. We have heard the Id. Authorized Representatives of the parties to the appeal, gone through the documents relied upon and orders passed by the revenue authorities below in the light of the facts and circumstances of the case.

6. At the outset, Id. AR for the taxpayer to cut short his arguments contended that he only presses relevant grounds no.3, 12 & 14 and all other grounds are academic and general in nature.

### **GROUND NO.3 & 12**

7. The taxpayer by using TNMM and OP/OC as PLI worked out its net margin on cost as under :-

<i>Operating revenue</i>	<i>Rs.290,606,669</i>
<i>Operating expense</i>	<i>Rs.266,579,944</i>
<i>Operating income</i>	<i>Rs.24,026,725</i>
<i>OP/OC</i>	<i>9.01%</i>

8. Out of the international transactions, the taxpayer reported to have spent an amount of Rs.96,71,69,164/- on account of payment

of arbitral award on behalf of the AE and the same have been reimbursed by the AE to the taxpayer. This transaction has not been benchmarked by the taxpayer on the ground that it is a cost to cost reimbursement. Major component of this transaction is reimbursement made by the AE to the tune of Rs.95,50,32,150/- being the payment made by the taxpayer on behalf of its Associated Enterprises (AE) on account of arbitral award.

9. Undisputedly, the taxpayer paid an amount of Rs.95,50,32,150/- to DMRC out of remittance received from the Head Office and the balance amount of Rs.15,43,13,697/- has been adjusted by DMRC against offshore payment in compliance to the arbitration award dated 22.07.2010. TPO taken the view that the AE has made reimbursement to the taxpayer as a support that Head Office would provide to its Project Office, but the payment arose in the course of business which the taxpayer carried out in India and as such, this transaction should form part of the margin calculation and would be added to the revenue and cost. Consequently, the TPO proposed to calculate the net margin as under :-

<b><i>Operating revenue</i></b>	<b><i>Rs.1,245,638,819</i></b>
<b><i>Operating expense</i></b>	<b><i>Rs.1,221,612,094</i></b>
<b><i>Operating income</i></b>	<b><i>Rs.24,026,725</i></b>
<b><i>OP/OC</i></b>	<b><i>1.96%</i></b>

10. In the backdrop of the aforesaid undisputed facts and circumstances of this case, the sole question arises for determination in this case is :-

***“as to whether the transaction of making payment of Rs.95,50,31,150/- (on account of arbitral award) by the taxpayer to the DMRC made on behalf of its AE and consequently reimbursed forms part of the margin calculation to be added to revenue and cost for benchmarking the international transaction?”***

11. The Id. AR for the taxpayer drew our attention towards order passed by Id. DRP under Rule 13 of the Income-tax Rules, 2009, the operative part of which is reproduced as under for ready perusal:-

***“Decision of the Panel***

***After considering the rectification request of the assessee the relevant paragraph is corrected and is replaced with the following paragraph :***

***The Panel has carefully examined the matter. The arbitration award was in respect of payment of customs and excise duty exemptions granted by the Government of India in relation to RS1 project. The perusal of the Audit Report in respect of RS1 project shows***

***Ia(a) the project office is regulate in depositing with appropriate authorities undisputed statutory due including provident fund, income tax, sales tax, wealth tax, service tax, custom duty, cess and other material statutory dues applicable to it.***

***From this it appears that the customs duty and service tax are liabilities of the project office. If so these should form part of the cost base of the assessee. The TPO/assessing officer is however directed to verify from record the facts as to whether the liabilities of payment of custom duty and service tax are of the assessee or the head office. In case the liabilities of payment of***

*custom duty and service tax are of the project office, then the amount spent on payment of custom duties and service tax and thus also the expense on payment of Arbitration award, will be part of cost base of the assessee for purpose of mark-up, if not then it would not be so included. The Panel accordingly disposes the objection of the assessee.*

*In the light of above directions, the TPO should also examine whether the following expenses reimbursed by the AE as detailed in the TP Study report have been included in the cost base.*

*ROTEM Pos incurred miscellaneous operating expenses on behalf of ROTEM and charged back these expenses to ROTEM. The value of the charge back of these expenses is as follows :-*

<b>Associated Enterprise</b>	<b>Paid by</b>	<b>Description of Services</b>	<b>Amount (INR)</b>
<b>ROTEM</b>	<b>ROTEM RS 3 PO</b>	<b>Amount paid to vendors on behalf of head office</b>	<b>1,928,052</b>
<b>ROTEM</b>	<b>ROTEM RS 3 PO</b>	<b>Service tax paid on behalf of Head Office</b>	<b>10,798,567</b>
<b>ROTEM</b>	<b>ROTEM RS 3 PO</b>	<b>Expenses reimbursed to DMRC on behalf of Head Office</b>	<b>276,166</b>
<b>ROTEM</b>	<b>ROTEM RS 3 PO</b>	<b>Custom Duty paid on behalf of Head Office</b>	<b>35,049,817</b>
<b>ROTEM</b>	<b>BMRCL PO</b>	<b>Taxes and duties paid on behalf of the AE</b>	<b>388,153,141</b>
<b>Total</b>			<b>436,205,743</b>

*As the Citations mentioned against these expenses show that they relate to payment of service tax, custom duty, and other taxes and duties, therefore, the treatment to be meted out to these expense would be the same as to the arbitration award. If the assessee has already included these expenses in the cost base for purpose of margin calculation, it would clarify the treatment in regard to the payment on account of arbitration award, since, the nature of expenses in respect of the arbitration award and above reimbursements are the same. If not then following a consistent policy their treatment should be the same as in respect of Arbitration Award i.e. these should also form part of the cost base or otherwise depending on findings by the TPO as discussed above.*

*The TPO is directed to follow consistent policy in respect of treatment of these reimbursement and the reimbursement of the arbitration award.*

*The issue raised by the assessee in the application for rectification is rectified as above.”*

12. Ld. DRP has taken the view that, “*the nature of expenses in respect of arbitration award is the same with regard to the payment of service tax, customs duty and other taxes and dues but directed the TPO to follow consistent policy in respect of arbitration award i.e. these should also form part of the cost based or otherwise depending on the findings of the TPO as discussed above*”. However, the ld. AR for the taxpayer contended that in AY 2012-13, no such addition on account of this income has been made in the subsequent years (order available at pages 1119 to 1148 of the paper book Vol.3).

13. Ld. TPO while deciding the identical issue in AY 2012-13 called upon the taxpayer vide letter dated 12.01.2016 to explain the following information :-

- (a) The nature of these transactions between you and your AE.
- (b) The parties involved in these transactions for the payment of custom duties and other taxes.
- (c) Why these should not be considered in your cost base for the calculation of margins as held by the TPO in the AY 2011-12 which was upheld by the Ld. DRP vide order dated 05.11.2015?

14. Sub-para (c) of preceding para 13 covers the controversy at hand. Perusal of the TP order passed by Id. TPO for AY 2012-13, available at pages 1119 to 1148 of the paper book, goes to prove that the only addition has been made on account of addition of TP adjustment by accepting the PLI of the taxpayer without including the expenses in the cost base for the purpose of margin calculation.

15. Even otherwise, perusal of the table drawn by Id. DRP in its order passed under Rule 13 of the Income-tax Rules, 2009 at page 970 of the paper book vol.2 shows that the DRP has taken the amount of Rs.43,62,05,743/- as value of the charged pack of expenses which is not the actual fact because as per financial statement, available at page 418 of the paper book vol.1, total cost is Rs.26,66,92,467/- which goes to prove that Rs.43,62,05,743/- is not part of the cost base. This issue was required to be resolved by the Id. DRP by passing order under Rule 13 of the Rules by following the rule of consistency.

16. So, following the rule of consistency and in view of the facts and circumstances of the case, we are of the considered view that payment on account of arbitration award cannot form part of the cost base for purpose of margin calculation. Id. TPO is to examine the issue on factual basis by following the rule of

consistency in the light of its order passed in AY 2012-13. So, grounds no.3 & 12 are determined in favour of the taxpayer for statistical purposes.

#### **GROUND NO.14**

17. The taxpayer claimed risk adjustment on the ground that companies operating in an uncontrolled environment will earn a risk premium whereas the taxpayer does not face some risks which are faced by the comparables, the taxpayer being a captive unit. However, the ld. TPO rejected the taxpayer's claim for risk adjustment.

18. Ld. DRP for the Revenue contended that the risk has to be explained in case of each comparable and economic analysis cannot be the basis for risk adjustment in the absence of complete data provided by the taxpayer. However, the ld. AR for the taxpayer contended that the risk adjustment is required to be given on each comparable as has been held by the coordinate Bench 'A', Pune Bench of the Tribunal in case of *Honeywell Turbo Technologies (India) Pvt. Ltd. vs. DCIT in ITA No.2584/PUN/2012 order dated 10.02.2017* by following the case of *Sony India Pvt. Ltd. cited as 114 ITD 448* by making following observation :-

***“33. Further, the Delhi Bench of Tribunal in the case of Sony India Pvt. Ltd. reported in 114 ITD 448 has allowed 20% risk adjustment considering the fact that it may not be possible to quantify risk adjustments. The assessee applying the said ratio in the case of Sony India Pvt. Ltd. (supra) has worked out the risk adjustment on the operating margins of comparables to be allowed when computed @ 20%. We direct the Assessing Officer to allow the risk adjustment and re-compute the margins of comparables by applying the ratio laid down by Delhi Bench of Tribunal in the case of Sony India Pvt. Ltd. (supra) and compute the TP adjustment, if any, in the hands of assessee.”***

19. Similar view has been taken by the coordinate Bench of the Tribunal in case of *ITO vs. M/s. Supportsoft India Pvt. Ltd. in IT (TP) A.No.1372/Bang/2011 order dated 28.03.2013* by returning following findings :-

***“27. Having heard both the parties and having considered the rival contentions, we find that the Tribunal in the case of M/s. Intellinet Technologies India Pvt. Ltd. vs. ITO in ITA 1237/Bang/2007 dated 30-3-2012 has considered this contention of the assessee and has held that the single customer risk attributable to the assessee is only an anticipated risk whereas the risk attributed by the assessee to the comparables is existing risk and in such situation the TPO ought to have given the risk adjustment to the net margin of the comparable for bringing them on par with the assessee-company. In the said case also, the assessee had claimed risk adjustment at 5.5% and the Tribunal has directed the TPO to consider the contention of the assessee and decide the percentage on risk adjustment to be made in accordance with law. As both of us are Signatories to the said order, we respectfully following the decision in the case of M/s.Intellinet Technologies India Pvt. Ltd. (supra) remit this issue also to the file of the AO/TPO for re-***

*consideration of the issue in accordance with law and in the light of our observations above.”*

20. So, following the decision rendered by coordinate Bench of the Tribunal in case of *M/s. Supportsoft India Pvt. Ltd* (supra), we are of the considered view that the taxpayer in this case is entitled for risk adjustment to the net margin of comparables for bringing them at par with the taxpayer. So, ground no.4 is determined in favour of the assessee.

21. Resultantly, appeal filed by the assessee is allowed for statistical purposes.

**Order pronounced in open court on this 22<sup>nd</sup> day of November, 2017.**

**Sd/-  
(N.K. SAINI)  
ACCOUNTANT MEMBER**

**sd/-  
(KULDIP SINGH)  
JUDICIAL MEMBER**

**Dated the 22<sup>nd</sup> day of November, 2017  
TS**

Copy forwarded to:

- 1.Appellant
- 2.Respondent
- 3.CIT
- 4.CIT (A)
- 5.CIT(ITAT), New Delhi.

**AR, ITAT  
NEW DELHI.**