

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

**BEFORE SHRI R. K. PANDA, ACCOUNTANT MEMBER  
AND  
MS SUCHITRA KAMBLE, JUDICIAL MEMBER**

**I.T.A .No. 4800/DEL/2010 (A.Y 2006-07)**

**&**

**I.T.A. NO. 5754/DEL/2011 (A.Y.2007-08)**

Honda R & D (India) Pvt. Ltd. 118 JP House 1 <sup>st</sup> Floor Shahpur Jal New Delhi AABCH3071N  <b>(APPELLANT)</b>	Vs	DCIT OSD, CIT(A)-IV New Delhi  <b>(RESPONDENT)</b>
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<b>Appellant by</b>	<b>Sh. Nageshwar Rao, Adv. Sh. Sandeep Karhel, Adv.</b>
<b>Respondent by</b>	<b>Sh. Amrender Kumar, CIT DR</b>

<b>Date of Hearing</b>	<b>08.08.2017</b>
<b>Date of Pronouncement</b>	<b>03.11.2017</b>

**ORDER**

**PER SUCHITRA KAMBLE, JM**

These two appeals are filed by the assessee against the Orders dated 21.09.2010 and 23.08.2011 passed by Assessing Officer, New Delhi u/s 143(3) r/w Section 144C of Income Tax Act, 1961 for Assessment Year 2006-07 and 2007-08 respectively.

2. The grounds of appeal are as under:-

**(ITA No. 4800/DEL/2010 A.Y. 2006-07)**

*“The following grounds of appeal are mutually exclusive of and without prejudice*

to each another.

1. *On the facts and circumstances of the case and in law, the Hon'ble Dispute Resolution Panel ("DRP") erred in confirming the draft order passed by the learned Assessing Officer ("AO"), and thereby confirming the order issued under section 92CA(3) the Income Tax Act, 1961 ("the Act") passed by the learned Transfer Pricing Officer ("TPO");*
2. *The Hon'ble DRP/AO erred in law and in circumstances by not providing any reasons for rejection of the Cost Plus Method identified as the most appropriate method by the Appellant and applying the Transactional Net Margin Method ("TNMM") for the provision of market research and testing services.*
3. *The Hon'ble DRP/AO erred in computing the net profit margin on the basis of the TNMM.*
4. *The Hon'ble DRP/AO erred in determining the Arm's Length Price for the provision of market research and testing services by the Appellant by using completely inappropriate set of companies that were engaged in a totally different line of business and industry and misconstruing the actual nature of the services provided by the Appellant.*
5. *The Hon'ble DRP/AO erred in upholding that the TPO followed all the required steps in identifying comparable companies viz. visiting the public database, use of appropriate filters and undertaking an appropriate Functions, Assets & Risks ("FAR") analysis.*
6. *That the Hon'ble DRP erred in upholding the Arm's Length Price for provision of market research and testing services as computed by the TPO by not passing a speaking order.*
7. *The Hon'ble DRP/AO erred by not awarding any opportunity to the Appellant to contest the selection of comparables selected by TPO during*

*the course of transfer pricing assessment proceedings.*

8. *The Hon'ble DRP/AO erred in stating that the market research and testing activities undertaken by the Appellant in India lead to the creation of Intellectual Property Rights, Patent, Copyrights & Trademarks, whereas the Appellant's activities do not, in any manner or circumstances, lead to creation of such intangibles.*
9. *The Hon'ble DRP/AO erred in ascertaining the risk profile of the Appellant by assuming that it undertakes substantial risk while rendering market research and testing services. Also, the Hon'ble DRP/AO did not give due cognizance to the fact that all Honda R&D group entities enjoy a "No Risk" status, i.e., all expenses incurred by the Appellant get reimbursed with a markup of 3 percent, irrespective of whether its market research and testing activities result in any commercial success or not.*
10. *The Hon'ble DRP/AO grossly erred in approving the substandard and inherently flawed analysis undertaken by TPO to arrive at the Arm's Length Price. The TPO sought to compare the Appellant to companies undertaking research and development services, however, most of these companies reported no or extremely insignificant research and development revenues.*
11. *The Hon'ble DRP/AO erred in not recognizing the fact that the TPO had grossly miscalculated the operating margin of comparable companies identified by him.*
12. *The Hon'ble DRP/Assessing officer failed to appreciate the fact that after removing the mistakes apparent from the margin computation of the comparable companies identified by the TPO, the international transactions undertaken by the Appellant would comply with the arm's length standard embodied in the Act.*

13. *The Hon'bleDRP erred in law and in facts and in circumstances by not giving due cognizance to the information submitted by the Appellant on May 28, 2010, in context of the FAR analysis.*
14. *The Hon'bleDRP erred in law by not evaluating the rejection/acceptance of TNMM method, used as a method of secondary choice applied by the Appellant for the purpose of establishing the arm's length nature of the market research and testing services.*
15. *The Hon'ble DRP erred in law and in facts by not giving due cognizance to the new set of appropriate comparable companies submitted by the Appellant with the Hon'ble DRP.*
16. *The Hon'ble DRP/AO erred in law and in facts by not giving due cognizance to the working capital adjustment under taken by the Appellant for establishing arm's length nature of the international transaction, and also not allowing any adjustment for risk.*
17. *On the facts and in the circumstances of the case and in law, the Hon'ble DRP erred in not directing TPO to allow a variation of 5 percent in determining the arm's length price as amended proviso to section 92C of the Act is not applicable to A.Y. 2006-07.*
18. *The Hon'ble DRP passed directions to the AO who denied natural justice to the Appellant by not providing an opportunity of being heard in connection with certain matters critical with the final outcome of the assessment proceedings, which finally led to an adverse conclusion against the Appellant, including failing to issue a speaking order.*

*The Appellant prays for leave to add, alter, amend and / or modify any of the grounds of appeal at or before the hearing of the appeal.*

*The Appellant prays for appropriate relief based on the said grounds of appeal and the facts and circumstances of the case.*

**(ITA No. 5754/DEL/2011 A.Y. 2007-08)**

*“The following grounds of appeal are mutually exclusive of and without prejudice to each another.*

*1. On the facts and circumstances of the case and in law, the Hon’ble Dispute Resolution Panel (“DRP”) erred in confirming the draft order passed by the learned Assessing Officer (“AO”), and thereby confirming the order issued under section 92CA(3) the Income Tax Act, 1961 (“the Act”) passed by the learned Transfer Pricing Officer (“TPO”).*

*2. The Hon’ble DRP and the Learned AO erred in facts and in law by not recognizing that the statutory onus on the TPO to establish that an Appellant’s case is covered ,under any of (a) to (d) clause of Section 92C (3) of the Act has not been discharged by him.*

*3. The Hon’ble DRP and Learned TPO have erred on facts and in law by not accepting the economic analysis conducted by the Appellant, for the transaction pertaining to provision of market research and testing services, which is in accordance with the provisions of the Act read with the Income-tax Rules, 1962 (“the Rules”), for the determination of the arm’s length price (“ALP”).*

*4. The Hon’ble DRP and Learned TPO have adopted a flawed approach by using single year data as against the multiple year data used by the Assessee, to compute the ALP of the international transaction of the Appellant using the Transactional Net Margin Method (“TNMM”).*

*5. The Hon’ble DRP and Learned TPO have erred in not accepting the*

*economic adjustments (such as working capital adjustment and risk adjustment) undertaken by the Appellant in order to improve the comparability of the comparable results and that of the Appellant.*

*The Appellant prays for leave to add, alter, amend and / or modify any of the grounds of appeal at or before the hearing of the appeal.*

*The Appellant prays for appropriate relief based on the said grounds of appeal and the facts and circumstances of the case.”*

3. For the sake of convenience the facts for A.Y. 2006-07 are taken hereunder as the issue relating to AMP is identical in both the Assessment Years.

4. The assessee company was established as a domestic company in June 2003 to undertake research and development activity in relation to Honda Auto Mobile Power Equipment Companies in India. The Company is engaged in Research & Development of any product involved service/review/pasting of the product in the local conditions and to undertake such activities. The domestic company was loaded by Honda R & D Company Ltd. Japan as a 100% subsidiary with 100% equity being held by the above company. The research and development activity is conducted in house for the sole use of such research in the development of products in the auto mobile sector and also barely in the power product sector. The major international transactions reported in Form No. 3CEB are summarized as under:-

- (1) Sale of services - cost plus -17,29, 83,179/-
- (2) Re-imburement of lodging, conveyance and Air Ticket-CUP-1,91,940/-
- (3) Re-imburement of medical expenses – CUP - 3347/-.
- (4) Import of Gosoline Handy Can – CUP - 53,460/-

- (5) Import of variable residences – CUP - 5,53,777/-
- (6) Re-imburement of custom duty and clearance charges-CUP-2,28,473/-.
- (7) Imported Machinery-CUP-6,30,702/-
- (8) Imported Consumables – CUP - 1,04,691/-.

In the form No. 3 CEB enclosed with the return of income it was mentioned that TNMM was applied for determining the Arms Length Price of the International Transaction related to the purchase of testing equipments and cost plus method has been applied for sale of services. During the course of proceedings report entitled 'an Analysis of Transfer Pricing Arrangement with Associated Enterprises' was filed. The assessee used cost plus method to bench mark its major international transaction relating to provisions of services with respect to R & D ( sale of services; Rs.17,29,83,179/-). The TPO observed that as per agreement dated 1/8/2003, only part of services rendered by the assessee gets remunerated and the agreement did not stipulate payment in lieu of transfer of IPR, Patent and copyright to Parent Company. It is an admitted fact that the assessee is customizing Honda Technology used in four & two wheelers to suit the requirement of Indian Customer, but benefit of such customized technology earned by the Parent Company from Indian Subsidiaries has not been shared with the assessee. Thus, Honda Motor Company Ltd. has earned income from license, technological assistance and product development of Rs.174.94 crores from M/s Hero Honda Motors Ltd. India alliance in Assessment Year 2005-06. However, no part of such benefit was actually transferred to the assessee which is responsible for conducting research and development activities in India to customize and develop technology suitable to Indian conditions and people. Thus, the TPO concluded that the assessee company which is generating specific R & D for modification of Honda Products to suit the Indian/local conditions and also for transfer of Patent IPR and copyright is not being compensated at Arm's Length Price. The draft order u/s 144C of the Income Tax Act, 1961 was passed and served on

the assessee on 24/11/2009 against which the assessee filed objection before the Dispute Resolution Panel (DRP, New Delhi). The DRP vide its order dated 30/8/2010 upheld the additions/disallowances made by the Assessing Officer , wherein the Assessing Officer has made an addition of Rs.1,77,51,768/-. The Assessing Officer while passing assessment order dated 21/9/2010 held that in the order, the TPO has dealt in detail with each aspect for the determination of correct Arm's Length Price for the international transaction undertaken by the assessee. Thus, an addition of Rs.1,77,51,768/- is made to the income of the assessee being difference between the Arm's Length Price.

5. The Ld. AR submitted that this Assessment Year is already covered by the Hon'ble Delhi High Court's decision in the assessee's own case for Assessment Year 2005-06 (ITA No. 616/15, dated 2/8/2016 wherein in Para 12,13 & 26, the same is discussed and the matter was restored to the ITAT. For Assessment Year 2005-06 the ITAT passed order dated 29.01.2015. The Hon'ble High Court clearly mentioned in Para 25 that Honda R & D India Pvt. Ltd. was not into Core Research & Development Activity. Thus, the TPO's as well as DRP's finding that it is at Arm's Length Price will not sustain. As related to working capital issue, the Hon'ble High Court's order was not available before the DRP as well as TPO. Therefore, the said issue should be remanded back to the TPO after taking into consideration the order of the Hon'ble High Court.

6. The Ld. DR relied upon the order of the TPO and DRP.

7. As relates to ITA No. 5734/Del/2011 for Assessment Year 2007-08 the Ld. AR submitted that Ground No. 1, 2, & 4 are not pressed. As relates to Ground No. 3 & 4 the Ld. AR submitted that the Transfer Pricing Study has been accepted by the TPO and the same are identical with the earlier year.

8. The Ld. DR once again relied upon the orders of the TPO & DRP.

9. We have heard both the parties and perused the material available on

record. Firstly we take up the appeal for A.Y. 2006-07, since the finding of the Hon'ble High Court for Assessment Year 2005-06 has clearly concluded that for Assessment Year 2007-08 the assessee has not carried out any research and development activity, the same cannot be taken into account for rendering services as per international transactions. The High Court in assessee's case for A.Y. 2005-06 held as under

*“24. Strangely the ITAT again picked up three comparables, i.e., National Research Development Corporation Limited, Panacea Biotech and Suven Life Sciences, which had been rejected as comparables by the TPO in its remand report for AY 2005-2006. The CIT(A) has given cogent reasons why the TPO's report ought to be acted upon. The ITAT also appears to have overlooked the fact that an order of another Co-ordinate Bench of ITAT in HRDPs own case for AY 2004-2005 had remanded the matter to the CIT(A), acting on the remand report of the TPO for AY 2005-06. By taking a different view and by again sending to the CIT(A) the entire issue of determining which comparables were best suited for the exercise of determination of ALP, the ITAT was adding to the confusion resulting from contradictory orders.*

*25. The Court is of the considered view that the ITAT did not have sufficient material before it to come to the conclusion that HRDI was into core R&D activity. That finding of the ITAT would only cause confusion before the CIT(A) in the remand proceedings. On the other hand there was sufficient material in the form of the remand report of the TPO for AY 2005-2006 as well as DRP's order for 2007-2008 to show that HRDI was not into core R&D activity.*

*26. Accordingly Question (i) is answered in the negative by holding that the ITAT was not justified in concluding that HRDI was involved in R&D activity and not provision of market support services. The order of the CIT(A), which was reversed by the ITAT, is restored.”*

The ITAT has decided the issues vide order dated 29.01.2015 for A.Y. 2005-06. Thus, the assessee company has not carried out any international transaction.

10. As related to working capital adjustment the Hon'ble High Court decision was not available before the TPO as well as before the DRP. Therefore, the same should be verified by the TPO/A.O. Needless to say, that the assessee be given full opportunity of hearing.

11. In respect of the Appeal for A.Y. 2007-08, Ground No. 1, 2 and 4 are not pressed by the Ld. AR during the hearing hence, the same are dismissed. As relates to Ground No. 3 and 5, the issues are similar to the A.Y. 2006-07, hence the same are partly allowed for statistical purpose.

12. In result, both the appeals of the assessee are partly allowed for statistical purposes.

**Order pronounced in the Open Court on 03rd November, 2017.**

Sd/-

**(R. K. PANDA)**  
**ACCOUNTANT MEMBER**

Sd/-

**(SUCHITRA KAMBLE)**  
**JUDICIAL MEMBER**

Dated: 03/11/2017  
*R. Naheed \**

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	11/08/2017	PS
2.	Draft placed before author	14/08/2017	PS
3.	Draft proposed & placed before the second member	.2017	JM/AM
4.	Draft discussed/approved by Second Member.		JM/AM
5.	Approved Draft comes to the Sr.PS/PS	.11.2017	PS/PS
6.	Kept for pronouncement on		PS
7.	File sent to the Bench Clerk	.11.2017	PS
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.		