

**IN THE INCOME TAX APPELLATE TRIBUNAL "J", BENCH
MUMBAI**

**BEFORE SHRI G.S.PANNU, VICE PRESIDENT
&
SHRI RAVISH SOOD, JUDICIAL MEMBER**

**ITA No.6956/Mum/2012
(Assessment Year :2008-2009)**

M/s Videojet Technologies (I) Pvt. Limited, Unit 101 & 102, Rupa Solitaire, Building No.A-1, Sector-1, Millennium Business Park, Mahape, Navi Mumbai-400710	Vs.	ACIT, Circle-10(3), Mumbai
PAN No.AAACW0731 B		
(Appellant)	..	(Respondent)

Assessee by	Shri Ketan Ved, AR
Revenue by	Shri Nilu Jaggi & Dharm Veer Singh, DR
Date of Hearing	01/03/2019
Date of Pronouncement	28/05/2019

आदेश / ORDER

PER RAVISH SOOD, J.M :

The present appeal filed by the assessee is directed against the order passed by the A.O u/s143(3) r.w.s 144C(13) of the Income-tax Act, 1961 (for short 'I-T Act'), dated 08.10.2012 for the assessment year 2008-2009. The assessee has raised before us the following grounds of appeal:-

"The appellant objects to the order dated 08 October 2012 passed under section 143(3) r.w.s. 144C(13) of the Income-tax Act, 1961 ('the Act') passed by the Assistant Commissioner of Income Tax,

Range - 10(3), Mumbai ('learned AO ') for the aforesaid assessment year on the following among other grounds:

1. General

1.1 The learned AO / DRP erred in upholding the upward adjustment of Rs. 4,49,48,022 made by the learned Transfer Pricing Officer (,TPO,) to the value of international transaction entered into by the assessee in relation to import of finished goods.

1.2 The learned AO / DRP erred in appreciating the fact that TPO erred in passing the order without following the principle of natural justice.

2. Erroneous rejection of Resale Price method by the TPO

2.1 The learned AO / DRP erred on the facts and circumstances of the case and in law, in confirming the TPO's-stand of rejection of resale price methodology ('RPM') followed by the Appellant in benchmarking the international transaction relating to import of finished goods, as prescribed under rule 10B(1)(b) of the Income-tax Rules, 1962 ('the Rules ')

3. Erroneous selection of Transactional Net Margin Method by the TPO

3.1 The learned AO / DRP erred in confirming the use of transactional net margin method ('TNMM') as opposed to the RPM adopted by the Appellant while benchmarking the transfer price relating to import of finished goods .

4. Erroneous rejection of 2 comparables by the TPO

4.1 The learned AO/DRP erred in upholding the rejection of 2 comparable companies namely K Dhandapani & Co. Ltd. and Kusam Electrical Inds. Ltd. on the basis that they deal in different types-of electrical equipments without appreciating the fact that other comparables also deal in products different than that of the assessee which are accepted by the TPO.

4.2 The learned AO/DRP erred in not appreciating the fact that TNMM require more of functional similarity than product similarity.

5. Erroneous inclusion of expenses not pertaining to the international transaction

5.1 The learned AO I DRP erred in inclusion of expenses not pertaining to the international transaction while computing the operating margin of the assessee.

6. Erroneous computation of the margins of comparable companies

6.1 The learned AO erred in wrongly computing the margins of the independent comparable companies accepted in the transfer pricing order

6.2 The learned AO erred in not accepting the correct computation of margins of the comparable companies as submitted by the assessee in spite of the DRP's directions to verify the Appellant's contentions in this regards.

7. Disregard of Rule 10B(2) and Rule 10B(3) of the Rules.

7.1 The learned AO I DRP erred in law and facts in disregarding the comparability factors specified under rule 10B(2) of the Rules and the provisions contained in rule 10B(3) of the Rules which specifies that an adjustment should be made to account for differences between the transactions that may materially affect the price of such transactions.

7.2 The learned AO/DRP erred in not granting the adjustment in respect of amount of customs duty paid by the assessee as against the alleged comparables selected by the TPO.

8. Non-consideration by the TPO/AO that the import price has been accepted by the customs authorities.

8.1 The learned AO I DRP erred in not appreciating the fact that the price at which finished goods are imported by the assessee has been accepted by the customs authorities.

9. Erroneous rejection of multiple year data for computation of margin of Comparables.

9.1 The learned AO I DRP erred in upholding the rejection of use of multiple year data for computing the margins of the comparables.

10. Erroneous rejection of the benefit of standard deduction of 5% range.

10.1 The learned AO / DRP erred in not granting the benefit of standard deduction of 5% range in computing the arm's length price as provided in the proviso to section 92C(2) of the Act as it stood prior to the amendment by the Finance Act (No.2), 2009 and Finance Act 2012.

11. Others

11.1 The appellant submits that the learned AO, TPO and DRP have erred in arriving at various unwarranted and erroneous conclusions unsupported by any relevant material in deciding the case. Further, they also failed to consider the contrary material and evidence adduced by the appellant

11.2 The learned AO erred in levying interest under section 234B of the Act.

11.3 The learned AO erred in initiating penalty proceedings under section 271 (1)(c) of the Act.

11.4 The Appellant submits that each grounds of appeal are without prejudice to one another.

11.5 The Appellant craves leave to add, alter, amend, substitute and/or modify in any manner whatsoever all or any of the foregoing grounds of appeal at or before the hearing of the appeal.

2. Briefly stated, the assessee company which is engaged in the business of trading of coding and marking equipment viz. continuous Inkjet printers, labelling equipments, Laser markers and related consumables & spares had e-filed its return of income for A.Y.2008-2009 on 29.09.2008, declaring total income at Rs.1,93,52,948/-. The return of income filed by the assessee was processed as such u/s.143(1) of the I-T Act. Thereafter, a revised return of income was filed on 30.03.2010 declaring total income at Rs.2,16,79,649/-. Subsequently, the case of the assessee was selected for scrutiny assessment u/s.143(2) of the I-T Act. The assessee is a wholly owned subsidiary of Kollmorgen India Investment Company, Mauritius, which is an ultimate subsidiary of Danaher Corporation, USA. During the year under consideration the assessee had shown sales and service receipts at Rs.36,66,81,463/- and other related income at Rs.39,17,659/-. In the course of assessment proceedings, the AO made a reference to the Additional Commissioner Income Tax (Transfer Pricing)-II(1&6), Mumbai (for short "TPO") as on 09.08.2010.

3. The TPO in the course of proceedings before him observed that as per the details discernible from the Transfer Pricing Study Report (in short 'TPSR') the assessee had during the year carried out the following international transactions :-

Nature of International Transactions	Name of Associated Enterprise	Amount (in INR)	Method used
Import of Inks & Solvents	Videojet Technologies Inc.	2,26,49,385	Resale Price Method (RPM)
Import of Printers		5,73,57,967	
Import of Spares & Thermal Ribbons		1,70,18,106	
Import of Inks & Solvents	Zhuhai SEZ Videojet Electronics Co Ltd	1,37,27,186	
Import of Printers		7,64,34,023	
Import of Spares		71,69,832	
Import of Printers	Alltec GmbH	2,54,38,284	
Import of Spares		56,66,077	
TOTAL		22,54,60,860	
Lease of property	Willet Systems Ltd.	1,50,000	Comparable Uncontrolled Price Method
TOTAL		22,56,10,860	

As such, it was noticed by the TPO that the international transactions pertaining to imports made by the assessee from its Associate Enterprises (AEs) aggregated to Rs.22,54,60,860/- viz. (i) import of printers (Rs.15,92,30,274/-); (ii) import of inks & solvents (Rs.3,63,76,571/-); and import of spares (Rs.2,98,54,015/-). It was the claim of the assessee before him that the finished goods i.e. coding and marking equipments that were imported from the foreign AEs were resold in the domestic market without any value addition in the same form in which they were imported. Further, it was stated that the finished goods purchased by the assessee from its foreign AEs for the purpose of domestic sales were exclusively manufactured by them. On a perusal of TPSR, it was observed by the TPO that the assessee had benchmarked its international transactions by taking "Resale Price Method"(for short 'RPM') as the most appropriate method. Further, taking itself as the tested party, it had adopted the gross profit margin as the appropriate Profit

Level Indicator (for short 'PLI') for the trading activities. It was noticed by the TPO that as per the TPSR the assessee had selected external comparables on the basis of the search performed on Indian Database i.e "Prowess". On the basis of the aforesaid search the assessee had selected 8 comparables in its TPSR and had computed the average gross profit margin of the same at 26.06% as under :-

Sr. No.	Name of the comparable	3 year average Gross Profit Margin
1.	Adtech Systems Ltd.	29.15%
2.	Alert Fire Protection.	29.54%
3.	Control Print Ltd.	35.57%
4.	Gemini Traze Rfid Pvt. Ltd.	26.34%
5.	K Dhandapani & Co. Ltd.	5.42%
6.	Kusam Electrical Inds. Ltd.	47.47%
7.	Mehala Machines India Ltd.	28.38%
8.	Precimax Engineers Ltd.	6.63%
Arithmetic Mean		26.06%

4. In the backdrop of the aforesaid facts it was submitted by the assessee that as its gross profit margin of 42.08% was higher than the average mean margin of 26.06% of the aforementioned comparables, hence, its international transactions were found to be at Arms Length. The TPO not being impressed by the fact that the assessee had taken three years margin in so far the aforementioned comparables were concerned, thus, directed him to submit the gross profit margin of the comparable companies by using the single year data for financial year 2007-2008. As the gross profit margin of two comparable companies was not available with the assessee, therefore, it used the single year gross profit margin data as regards the remaining six comparables, as under :-

Sr. No.	Name of the comparable	Gross Profit Margin	
		Prowess	Annual Report
1.	Adtech Systems Ltd.	29.91%	30.07%
2.	Alert Fire Protection.	27.16%	27.16%
3.	Control Print Ltd.	35.32%	34.90%
4.	Gemini Traze Rfid Pvt. Ltd.	29.18%	29.18%
5.	K Dhandapani & Co. Ltd.	5.34%	5.85%
6.	Kusam Electrical Inds. Ltd.	50.24%	50.94%
7.	Mehala Machines India Ltd.	NA	NA
8.	Precimax Engineers Ltd.	NA	NA
	Arithmetic Mean	29.53%	29.68%

5. As such, it was claimed by the assessee that as its gross profit margin of 42.08% was more than the average mean margin of 29.53% (as per "Prowess") and 29.68% (as per annual reports), therefore, its international transactions were within the ALP.

6. The TPO in the course of proceedings was not persuaded to accept the 'Resale Price method' (for short 'RPM') that was adopted by the assessee for bench-marking its international transactions for multiple reasons viz. (i) that, the assessee had failed to demonstrate that uniform accounting norms were followed in the accounting of "cost of goods sold" by the assessee as in comparison to the aforementioned comparables selected by it; (ii) that, in absence of the accounting norms which were followed by the comparables selected by the assessee the gross profit margin could not be adopted as a reliable PLI; (iii) that, in the absence of the complete details of comparables, difference in accounting of certain items such as freight, transportation cost, insurance, discounts, rebates, packaging, duties etc under the 'cost of goods sold' or as 'operating expenses' would affect the reliability of gross profit margin as profit level indicator for the purpose of comparison; (iv) that, in view of the elaborate functions performed and risk undertaken, it would be necessary to examine whether the assessee had obtained appropriate returns as regards the various functions performed while determining of ALP its

international transactions; (v) that, there was no thumb rule that RPM was the most appropriate method insofar resale transactions were concerned; (vi) a perusal of the FAR analysis of the assessee revealed that unlike the case of other comparables where the goods were imported on CIF basis, in case of the assessee the insurance in transit was borne by the AEs; (vii) that, a perusal of the FAR analysis revealed that the assessee did not make any separate payments for use of trade names and trade marks, which was not so in the case of the other comparables; (viii). that, the goods were procured by the assessee from the AEs for a credit period of one month which was normally extendable upto 180 days, however, the details as regards the credit period in case of the comparables was not discernible from the records; and (vii) that in the case of the assessee the warranty was provided by the AEs, which however was not so in the case of the comparables.

7. The TPO was further of the view that as the assessee carried on elaborate functions of distribution, marketing, sales promotion, inventory management, personnel management, training, development of training materials etc in the course of its business of trading in coding and marketing equipment and rendering of allied services, and also did bear substantial risks in the form of inventory risk, market risk and credit risk, thus, it could not be considered as a limited risk distributor as claimed in FAR analysis. As such, the contention of the assessee that as it was involved in the business of purchase and re-sale without any value addition, therefore, the RPM was most appropriate method for benchmarking its international transactions with its AEs, was rejected by the TPO. Apart therefrom, it was also observed by the TPO that a perusal of "Schedule 16" to the balance sheet of the assessee for the year under consideration revealed that the average cost price of the goods imported during the year was substantially more as in comparison to the last year, as under :-

Purchases items	Year ended 31.3.2008	Year ended 31.3.2007
Ink & solvents	87,297 Litres	46,609 Litres
	Rs.3,63,76,571/-	Rs.1,72,75,234/-
Average price per unit	Rs.417/-	Rs.371/-
Machines	804 Nos	420 Nos
	Rs.15,93,58,274/-	Rs.2,56,25,031/-
Average price per machine	Rs.1,98,207/-	Rs.61,012/-

8. In the backdrop of the aforesaid observations, it was concluded by the TPO that the assessee's business model clearly revealed that it was not merely purchasing goods and immediately reselling the same to its customers, but in fact, it was also carrying on the functions as that of distributing the goods, stocking the goods in various warehouses, adopting certain market strategies for sale for which it had engaged 140 sales/service/back office employees. Accordingly, the TPO was of the view that it would be appropriate to examine the returns for its various functions while determining the ALP of the transactions under consideration. As such, on the basis of the aforesaid observations, the TPO rejected the RPM method and adopted the Transaction Net Margin Method (TNMM) at entity level as the most appropriate method for benchmarking the international transactions of the assessee.

9. The assessee on being called upon by the TPO to give its working of net profit margin as well as that of the comparables, therein furnished the requisite details. As per the details placed on record by the assessee the average mean margin of the comparables worked out at 10.66%, while for that of the assessee was 9.89%. It was submitted by the assessee that as its margin was within $\pm 5\%$ range, hence, the aforesaid transaction was to be considered at ALP. The TPO after deliberating on the working given by the assessee made certain modifications viz. (i) that, the claim of the assessee as regards certain extraordinary expenses of

Rs.2,67,79,283/- which were excluded while computing its margin, was not accepted by the TPO and were characterized as regular business expenses. As such, the TPO re-worked out the net margin of the assessee at 2.65%. Further, the TPO in the absence of any details supporting the claim of the assessee that the revenue of Rs.2.82 crores was on account of sale of spares, thus, inferred that the entire sales revenue of Rs.36.66 crores pertained to the sale of AE products. On the same footing, it was observed by the TPO that now when the revenue of Rs.2.82 crores was not being excluded, therefore, the claim for exclusion of expenditure of Rs.1.63 crores and proportionate depreciation from the operational expenditure would also not arise. As regards six comparables, which were selected by the assessee for benchmarking its international transactions, the TPO excluded two comparables viz. (i) M/s K. Dhandapani & Co.; and (ii) M/s Kusam Electrical Industries Ltd. from the final list of comparables. Insofar M/s. K. Dhandapani & Co. was concerned, it was observed by the TPO that while for the assessee was carrying on the business of trading in high ended technology related products, while for the aforesaid comparable was dealing in routine electrical items, fuses, meters, switch gears etc. As such, the aforesaid comparable was held by the TPO to be functionally incomparable. As regards the other company viz. M/s Kusum Electrical Industries Ltd., it was observed by the TPO that the same could not be selected as a comparable for benchmarking the international transactions of the assessee for two reasons viz. (i) that, the turnover of the said comparable was only Rs.2.07 crores as against the turnover of the assessee of Rs.36.99 crores; and (ii) that, as the said comparable was dealing in routine electrical equipments such as meters and testing equipments, hence in view of the entirely different line of products dealt by it as in comparison to the high ended technology related products traded in by the assessee, it could not feasibly taken as a comparable for benchmarking the international transactions of the assessee. Accordingly, on the basis of his aforesaid deliberations the TPO worked out the

average mean margin of the remaining four companies at 14.80%, as against the assessee's margin of 2.65%. As such, the TPO worked out TP adjustment of Rs.4,49,48,022/- in the hands of the assessee as under :-

Particulars	Amount (in Rs.)
Sales and service income	36,66,81,463
Operating revenue	36,99,00,959
Operating expenses	36,01,03,640
AE expenditure	22,54,60,960
Non AE expense	13,46,42,680
OP/sales %	2.65%
ALP OP/sales ratio	14.80%
ALP profit	5,47,45,341
ALP expenses	31,51,55,618
ALP of AE transaction	18,05,12,938
5% TP	23,67,34,008
-5%	21,41,87,912
Adjustment to be made	4,49,48,022

10. The AO on the basis of the order passed by the TPO u/s.92CA(3) of the I-T Act, dated 25.07.2011 passed the draft assessment order u/s.143(3) r.w.s.144C, dated 20.12.2011, therein proposing the aforesaid TP adjustment of Rs. 4,49,48,022/-.

11. Aggrieved, the assessee filed its objections before the Dispute Resolution Panel-II, Mumbai (for short the 'DRP'). The DRP after deliberating at length on the contentions advanced by the assessee, however, did not find any infirmity in the order of TPO and upheld the view therein taken by him.

12. The AO after receiving the order passed by the DRP passed the final assessment order u/s.143(3) r.w.s.144C(13), dated 08.10.2012 and, inter alia, after making the aforesaid TP adjustment of Rs.4,49,48,022/- assessed its income at Rs.6,43,00,970/-.

13. The assessee being aggrieved with the order passed by the AO u/s.143(3) rw.s.144C(13), dated 08.10.2012, has carried the matter in appeal before us. The Ld. Authorized Representative (for short 'A.R') for the assessee at the very outset of the hearing of the appeal, took us through the observations of the lower authorities in context of the issue under consideration. It was submitted by the Id. AR that as the assessee was engaged in the business of importing of coding and marking printers, consumable and accessories from its AEs and selling the same without making any value addition, hence, it had adopted RPM as the most appropriate method for benchmarking its international transactions. It was submitted by Id. AR that the AO/TPO had most arbitrarily proceeded on the basis of misconceived facts and substituted the RPM by TNMM for benchmarking the international transactions of the assessee. It was vehemently submitted by Id. AR that as per the rule 10B(1)(b) of the Income-tax Rules, 1962, RPM is the best suited method for determining the ALP of the international transactions in a case where the assessee purchases goods from AE which are resold as such to the unrelated parties. In support of his contention, Id. AR relied on the certain judicial pronouncements, as under:-

- i) Burberry India Pvt. Ltd. Vs. ACIT, Circle-5(1), New Delhi, ITA No.758/Del/2017, dated 22.06.2018;
- ii) Horiba India (P.) Ltd. vs. DCIT (81 taxmann.com 209 (Delhi - Trib);
- iii) Fresenius Kabi India Pvt. Ltd. vs. DCIT (ITA No. 235/Pun/2013);
- iv) ACIT vis. Kobelco Construction Equipment India Ltd (ITA No.6401/0el/2012);
- v) Systems Pvt. Ltd. vs. DCIT & vice versa (ITA No. 683/Hyd/2014); and
- vi) Frigoglass India (P.) Ltd. vs. DCIT (2014) 149 ITO 429 (Delhi).

14. It was submitted by the Id. AR that in all the aforementioned orders it had consistently been concluded that in a case where goods are purchased and sold without any value addition, the RPM would be the

most appropriate method for benchmarking the international transactions. The Id. AR submitted that the view taken by the TPO that as the assessee had not demonstrated that uniform accounting norms were followed in the accounting of "cost of goods sold" by the assessee and the comparables selected by it, therefore, the RPM could not be accepted for benchmarking the international transactions of the assessee was not only backed by misconceived facts, but all the more was devoid and bereft of any force of law. It was submitted by Id. AR that in case the TPO was of the view that the comparables were not found appropriate, then the appropriate remedy available with him was to search for fresh comparables and the method adopted by the assessee for benchmarking the international transactions could not have been rejected merely for the said reason. In support of his aforesaid contentions, the Id. AR relied on the order of the ITAT Delhi Bench of the Tribunal in the case of Burberry India Pvt. Ltd. Vs. ACIT, Circle 5(1), New Delhi (ITA No. 758/Del/2017; dated 22.06.2018). Apart therefrom, it was submitted by the Id. AR that the aforesaid observation of the TPO that the assessee and the comparables were not demonstrated to be following uniform accounting norms was in itself an incorrect observation. It was submitted by the Id. AR that both the assessee and the comparables used Indian GAAP and accordingly followed the uniform accounting norms. In fact, it was submitted by him that no specific discrepancy was pointed out by the TPO/DRP while dislodging the said claim of the assessee. Further, on facts it was the claim of the Id. AR that the TPO while drawing adverse inference as regards the method of benchmarking adopted by the assessee had relied upon wrong facts and figures. The Id. AR taking us to Para 6.15 of the order of the TPO, submitted, that the latter while observing that the average cost price of goods imported during the year was more as in comparison to that of last year, had based such view on wrong facts and figures. It was averred by the Id. AR that while for the assessee in the immediately preceding year had imported 420 machines for a consideration of Rs.12,56,25,031/-, however, the value of the same

on account of an inadvertent mistake had wrongly been stated at Rs.2,56,25,031/-. It was submitted by him that in case the correct figure for purchase of 420 machines was taken, then the average purchase price per machine worked out at Rs.2,99,107/- (i.e. Rs.12,56,25,031/420), which was more as in comparison to the average purchase price amounting to Rs.1,98,207/- for the year under consideration. It was, thus, the contention of Id. AR that the AO/TPO had misconceived both the settled position of law as well as the facts of the case. Insofar the observation of the TPO that the assessee was found to have carried out multiple functions of distribution, marketing, sales promotion, inventory management, personnel management, training, development of training materials, as well as had borne substantial risk in the form of inventory risk, market risk and credit risks, it was submitted by Id. AR that such functions would be carried out by any assessee engaged in the business as that of a distributor. Further, Id. AR also assailed the exclusion of two comparables which were selected by the assessee for benchmarking its international transactions and took us through his relevant "written submissions" in context of the issue under consideration. Apart therefrom, the Id. AR also submitted that the TPO had erred in declining to exclude certain extraordinary expenses which were claimed by the assessee while working out its operating margin for the year under consideration. Also, the dislodging of the claim of the assessee wherein it had sought exclusion of revenue of Rs.2.82 crores from its operational revenue for the reason that the same did not pertain to the sales of AE products was also challenged before us. Lastly, the declining on the part of the TPO to exclude the proportionate costs pertaining to revenue generated from customers of M/s Control Print Limited of Rs.1,63,57,121/- and the proportionate depreciation was also contested before us.

15. Per Contra, the Id. Departmental Representative (in short the "DR") submitted that the claim of the assessee counsel that the TPO had wrongly taken the purchase price of the machines at Rs.2,56,25,031/- as

against the actual value of Rs.12,56,25,031/- was not borne from the records and, thus could not be summarily accepted. It was further submitted by Id. DR that a FAR analysis of the assessee clearly revealed that the goods purchased by him from the AEs were not immediately sold by it. It was the contention of Id. DR that the lower authorities keeping in view the nature of the business of the assessee had rightly concluded that RPM was not the most appropriate method for bench marking the international transactions of the assessee, and had thus rightly applied TNMM. The Ld. DR relied on the orders of the lower authorities and submitted that as the appeal of the assessee was devoid of any force, thus, the same was liable to be dismissed.

16. We have heard the authorized representatives of both the parties, perused the orders of the lower authorities and the material available on record as well as the judicial pronouncements relied upon by them. Admittedly, the assessee in the course of the its business purchases finished goods i.e. coding and marking equipments viz. continuous Inkjet Printers, Labelling Equipments, Laser markers and related consumables & spares from its foreign affiliates for the purpose of sale in the domestic market. As such, the assessee does not carry out any value addition to the goods purchased from its AEs and, sells it in the same form in the domestic market. Before advertng to the fact as to whether the international transactions of the assessee with its AEs were rightly benchmarked by it in its TPSR by taking RPM as the most appropriate method, or not, we feel that it would be relevant to cull out Rule 10B(1)(b) of the Income-tax rules, 1962, which envisages the determination of ALP u/s.92C of the Act as per RPM, as under :-

"Determination of arm's length price under section 92C .

10B. (1) *For the purposes of sub-section (2) of section 92C, the arm's length price in relation to an international transaction [or a specified domestic transaction] shall be determined by any of the following methods, being the most appropriate method, in the following manner, namely :-*

(a) xxxxxxxx

(b) resale price method, by which-

- (i) *the price at which property purchased or services obtained by the enterprise from an associated enterprise is resold or are provided to an unrelated enterprise, is identified,'*
- (ii) *such resale price is reduced by the amount of a normal gross profit margin accruing to the enterprise or to an unrelated enterprise from the purchase and resale of the same or similar property or from obtaining and providing the same or similar services, in a comparable uncontrolled transaction, or a number of such transactions;*
- (iii) *the price so arrived at is further reduced by the expenses incurred by the enterprise in connection with the purchase of property or obtaining of services;*
- (iv) *the price so arrived at is adjusted to take into account the functional and other differences, including differences in accounting practices, if any, between the international transaction [or the specified domestic transaction] and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of gross profit margin in the open market;*
- (v) *the adjusted price arrived at under sub-clause (iv) is taken to be an arm's length price in respect of the purchase of the property or obtaining of the services by the enterprise from the associated enterprise,"*

17. We are of the considered view that from a perusal of Rule 10B(1)(b) of the Income-tax rules, 1962, it can safely be concluded that RPM is the best suited method for determining the ALP of an international transaction, in a case where the goods purchased by an assessee from its AE are thereafter resold without any value addition to unrelated parties. Our aforesaid view is fortified by the orders of the ITAT, Delhi Bench in the case of (i) Burberry India Pvt. Ltd. Vs. ACIT, Circle-5(1), New Delhi, ITA NO.758/Del/2017, dated 22.06.2018 and Nokia India Pvt. Ltd. Vs. DCIT, Circle-13(1), New Delhi [2014] taxmann.com 492 (Delhi-Trib). In the latter case, it was observed by the Tribunal that a close scrutiny of sub-clauses (i) and (v) along with the remaining sub-clauses of rule 10B(1)(b) of the Income-tax rules, 1962, makes it clear beyond doubt that RPM is best suited for determining the ALP of an international transaction in the nature of purchases made from an AE which are resold as such to

unrelated parties. It was further observed by the Tribunal that ordinarily the said method presupposes no or insignificant value addition to the goods purchased by an assessee from its foreign AE. Further, we find that the aforesaid issue had also been looked into by the Hon'ble High Court of Delhi in the case of PCIT Vs. Matrix Cellular International Services (P.) Ltd. [2018] 90 taxmann.com 54(Delhi). The Hon'ble High Court observing that in case of a pure trader where there was no value addition before reselling the products, RPM was the most appropriate method for benchmarking the transactions, had held as under :-

"8. This Court finds that once the ITAT, on considering the relevant facts as well as the order of the TPO, had concluded that the business of the assessee was merely that of a pure trader, and there was no value addition made before re-selling the particular products (i.e. the SIM cards), its consequent finding that RPM is the Most Appropriate Method, is irreproachable. In Nokia India (P) Ltd. v. Dy. CIT[2014] 52 taxmann.com 492/153 ITD 508 (Delhi), the Delhi bench of the ITAT held:

"A close scrutiny of the above two sub-clauses along with the remaining sub-clauses of r. 10B(1)(b) makes it clear beyond doubt that RPM is best suited for determining ALP of an international transaction in the nature of purchase of goods from an AE which are resold as such to unrelated parties. Ordinarily, this method presupposes no or insignificant value addition to the goods purchased from foreign AE. In a case the goods so purchased are used either as raw material for manufacturing finished products or are further subjected to processing before resale, then RPM cannot be characterized as a proper method for benchmarking the international transaction of purchase of goods by the Indian enterprise from the foreign AE."

9. Similarly, in *Swarovski India (P.) Ltd. v. Asstt. CIT[2017] 78 taxmann.com 325 (Delhi - Trib.)* the ITAT held:

"Adverting to the facts of the instant case, we find that the assessee purchased Crystal goods and Crystal components from its AE. No value addition was made to such imports. The goods were sold as such. In the given circumstances, the RPM is the most appropriate method for determining the ALP of the international transaction of Import of Crystal goods and Crystal components."

10. A similar view has been adopted by the Mumbai bench of the ITAT in *Mattel Toys India (P.) Ltd. v. Dy. CIT[2013] 34 taxmann.com 203/144 ITD 76:*

"Thus, the RPM method identifies the price at which the product purchased from the A.E. is resold to a unrelated party. Such price is reduced by normal gross profit margin i.e., the gross profit margin accruing in a comparable controlled transaction on resale of same or similar property or services. The RPM is mostly applied in a situation in which the reseller purchases tangible property or obtain services from an A.E. and reseller does not physically alter the tangible goods and services or use any intangible assets to add substantial value to the property or services i.e., resale is made without any value addition having been made."

11. *This view has also been affirmed by the Bombay High Court in its judgment dated 07.11.2014 in CIT v. L'Oreal India (P.) Ltd.[2015] 53 taxmann.com 432/228 Taxman 360 , where the Court found that there was no error in law committed by the ITAT when it held that RPM was the Most Appropriate Method in case of distribution or marketing activities especially when goods are purchased from associated entities and there are sales effected to unrelated parties without any further processing. In fact, a Division Bench of this Court in its decision in Bausch & Lomb Eyecare (India) (P.) Ltd. v. Addl. CIT[2016] 381 ITR 227/237 Taxman 24/65 taxmann.com 141 (Delhi), while considering the decision of this Court in Sony Ericsson Mobile Communications India (P.) Ltd. v. CIT[2015] 374 ITR 118/231 Taxman 113/55 taxmann.com 240 (Delhi), noted that:*

"The RP Method loses its accuracy and reliability where the reseller adds substantially to the value of the product or the goods are further processed or incorporated into a more sophisticated product or when the product/service is transformed."

12. *Therefore, a contrario, when the reseller does not add any value to the product of the goods, the RP method would be appropriate for determining the arms' length price."*

18. We also find that the Hon'ble High Court of Bombay in the case of CIT Vs. L'oreal India Pvt. Ltd., ITA No.1046/2012 had upheld the order of the Tribunal, wherein it was observed that RPM was the most appropriate method in the case of distribution or marketing activities, specifically when goods which are purchased from AEs are thereafter sold to unrelated parties without any further processing. Also, a similar view had been taken by the coordinate benches of the Tribunal viz. (i) Horiba India (P) Ltd. Vs. DCIT, 81 taxamnn.com 209(Delhi); (ii) Fresenius Kabi India Pvt. Ltd. Vs. DCIT (ITA No.235/PUN/2013); and (iii) ACIT Vs. Kobelco Construction Equipment India Pvt. Ltd., ITA NO.6401/De1/2012 (Delhi).

Accordingly, in terms of our aforesaid observations, we are of the considered view that in the case of a pure trader RPM is the most appropriate method for bench marking the international transactions. On the other hand, under the TNMM, the ALP is determined by comparing the operating profit related to an appropriate base i.e. cost or sale or assets of the "tested party" with the operating profit of an uncontrolled party engaged in comparable transactions. As such, under the TNMM, the net margin or operating profit achieved in related party transactions is compared against with those entered into between the independent entities. Accordingly, under the TNMM the major thrust is to derive the operating profit at the transactional level and to identify the operating expenses of both the tested party as well as the independent parties, which, thus, requires a lot of adjustments to arrive at the actual operating profit. Thus, if the ALP of a transaction can be determined by applying any of the direct methods like CUP, RPM, CPM then they should be given a preference, and it is only where the said traditional methods have been rendered inapplicable that under such circumstances TNMM should be resorted to. We, thus, in the backdrop of the facts of the case before us, are of the considered view that RPM can safely be taken as the most appropriate method for benchmarking its international transactions, as against TNMM.

19. We shall now deliberate on the observations of the lower authorities on the basis of which application of RPM for benchmarking the international transactions of the assessee had been rejected by them. We find that a primary reason given by the TPO for rejectingg RPM as the most appropriate method, and the gross profit margin as the PLI, was that as per him the assessee had not demonstrated that uniform accounting norms were followed in the accounting of "cost of goods sold" by the assessee and the comparables selected by the assessee. As observed hereinabove, we find that though it has been the claim of the assessee that both the assessee and the comparables have used Indian GAAP and

accordingly followed the uniform accounting norms, however, the said claim of the assessee was rejected by the TPO/DRP without placing on record any material which could disprove the same. Be that as it may, we are of the considered view that as per the rule 10B(1)(b)(iv) of the Income-tax Rules, 1962, while determining the ALP in relation to an international transaction as per RPM, the price so arrived at is to be adjusted to take into account the functional and other differences including difference in accounting practices, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of gross profit margin in the open market. As such, we are of the considered view that in case the AO held a conviction that the comparables selected by the assessee were not found to be appropriate, then the remedy available with him was either to make necessary adjustments as envisaged in Rule 10B(1)(b)(iv) of the Income-tax rules, 1962 or to search for fresh comparables. However, merely for the reason that the comparables selected by the assessee were not found to be appropriate could have by no means justified the rejection of the aforesaid method adopted by the assessee for benchmarking the ALP of its international transactions. Our aforesaid view is fortified by the order of the ITAT Bangalore Bench of the Tribunal in the case of CIT Vs. Sanyo India Pvt. Ltd. [2015] 45 CCH 98 (Bang) and the order of ITAT, Delhi Bench in the case of Burberry India Pvt. Ltd. (supra). Further, we find that another reason given by the TPO/DRP for rejecting the RPM is that the assessee as per them was a full-fledged/full risk distributor and was performing a host of functions which would involve huge costs and, hence, the said method may not represent correct gross profit margin. We are unable to persuade us to accept the said observations of the lower authorities, because, in our considered view, in a comparable uncontrolled transaction scenario also a normal distributor will undertake all such functions which are related to sales of a product viz. market research, sales and marketing, warehousing, inventory control, quality

control etc., and would also bear risks viz. market risk, inventory risk, credit risk etc. As a matter of fact, the TPO/DRP had not placed on record instances of any such comparable which is engaged in the business of a distributor and is not performing the aforementioned functions. We are of the considered view that for the purpose of application of RPM what is relevant is that as to whether there is any value addition or not to the goods purchased for resale or not. In case, there is no value addition and the finished goods which are purchased from the AE are resold in the market in the same form, then the gross profit margin earned on such transactions becomes the determinative factor for benchmarking the international transaction of the assessee with its AE by taking RPM as the most appropriate method. Our aforesaid view is supported by the order of ITAT Pune Bench in the case of Fresenius Kabi India (P) Ltd. Vs. DCIT (ITA No. 235/Pun/2013), wherein it was held that in case of a distribution activity, the selling and marketing expenses which are borne by the assessee would not lead to any value addition to the product in question. We, thus, in terms of our aforesaid observations vacate the view taken by the TPO/DRP, who had concluded that the freight, transaction cost, insurance discounts, rebates, packaging, duties, etc. would affect the reliability of gross profit margin as PLI for the purpose of comparison. In terms of our aforesaid observations, we are of the considered view that the TPO/DRP while dislodging the RPM followed by the assessee for benchmarking its international transactions, had lost sight of the fact that only the transaction of import of goods by the assessee from its AEs were to be benchmarked and all the other functions carried out by the assessee having no nexus with the said import transactions were, thus, not relevant for the said benchmarking analysis.

20. We shall now deliberate on the aspect as to whether the TPO/DRP were justified in excluding two of the comparables viz. (i) M/s K. Dhandapani & Co. and (ii) M/s Kusam Electricals Industries Pvt. Ltd. from the final list of comparables. As is discernible from the order of the TPO,

the aforesaid parties were rejected as comparables primarily for the reason that while for the assessee's line of business was "trading in high-ended technology related products", on the other hand, the said comparables were dealing in routine electrical equipments. We may herein observe that under the RPM method, the focus is more on the functions rather than the similarity of products because product differentiation does not materially affect the gross profit margin, as it represents gross composition after the cost of sales for specific functions performed. Our aforesaid view is supported by the orders of the ITAT, Mumbai in the case of Mattel Toys (I)(P.) Ltd. Vs. DCIT, Circle-6(3), Mumbai, [2013] 34 taxamnn.com 203 (Mumbai-Trib) and ITAT, Delhi Bench in the case of Horiba India (P) Ltd. Vs.DCIT, 81 taxamnn.com 209(Delhi). As we have upheld the RPM as the most appropriate method in the case of the assessee as against TNMM applied by the TPO, therefore, we find no justifiable reason for exclusion of the aforementioned comparables from the final list of comparables. Accordingly, we direct the AO/TPO to include the aforementioned two comparables viz. (i) M/s K. Dhandapani & Co. and (ii) M/s Kusam Electricals Industries Pvt. Ltd. in the final list of comparables for the purpose of benchmarking the ALP of the international transactions of the assessee as per the RPM adopted by it in its TPSR.

21. As we have set aside the order of the AO/TPO insofar the assessee's claim for benchmarking its international transaction as per RPM was rejected by the TPO/DRP and was substituted by TNMM, therefore, we refrain from adverting to the other issues raised by the assessee before us on merits viz. declining on the part of the TPO for exclusion of the revenue of Rs.2.82 crores and purchase expenses of Rs.1.74 crores while working out its ALP which, thus, are left open.

22. We, thus, in terms of our aforesaid observations, direct the AO/TPO to benchmark the ALP of the assessee as per RPM after including the

above-mentioned two comparables in the final list of comparables. Accordingly, we allow the appeal of the assessee in terms of our above-mentioned observations.

23. In the result, appeal of the assessee is allowed.

Order pronounced in the open court on 28/05/2019.

Sd/-
(G.S.PANNU)
VICE PRESIDENT

Sd/-
(RAVISH SOOD)
JUDICIAL MEMBER

Mumbai; Dated 28/05/2019
Prakash Kumar Mishra, Sr.PS

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent.
3. The CIT(A), Mumbai.
4. CIT
5. DR, ITAT, Mumbai
6. Guard file.

BY ORDER,

सत्यापित प्रति //True Copy//

(Asstt. Registrar)
ITAT, Mumbai