

THE INCOME TAX APPELLATE TRIBUNAL
“J” Bench, Mumbai
Before Shri Shamim Yahya (AM) & Shri Ramlal Negi (JM)

I.T.A. No. 605/Mum/2015 (Assessment Year 2010-11)

Mahindra Heavy Engines Pvt. Ltd. (Earlier Mahindra Navistar Engines Pvt. Ltd. and earlier to this MIM Engines India Pvt. Ltd.) Mahindra Towers P.K. Kurane Chowk Worli, Mumbai-400 018. PAN : AAFCM0476N (Appellant)	Vs.	DCIT Circle 6(3) Aayakar Bhavan M.K. Road Mumbai - 400 020. (Respondent)
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Assessee by	Shri R.D. Omkar & Shri Prasad Bapat
Department by	Shri Anand Mohan
Date of Hearing	15.4.2019
Date of Pronouncement	31.5.2019

ORDER

Per Shamim Yahya (AM) :

This appeal by the assessee is directed against the order of the Assessing Officer passed u/s. 143(3) read with section 144C(13) of the Act dated 8.12.2014 pursuant to direction of learned Dispute Resolution Panel (DRP) dated 27.10.2014.

2. Grounds of appeal read as under :-

The appellant objects to the order dated 8 December 2014 passed under section 143(3) r.w.s. 144C (13) of the Income-tax Act, 1961 (the Act) by the Dy. Commissioner of Income tax - 6(3), Mumbai (AO) in pursuance of the direction given by the Dispute Resolution Panel (DRP) for the aforesaid assessment year on the following among other grounds:

1. The learned AO erred in not demonstrating that how he considered it necessary and expedient to refer the computation of arm's length price (ALP) to the Transfer Pricing Officer (TPO). The transfer pricing proceedings initiated by the AO under section 92CA(1) of the Act are without any jurisdiction and ought to be quashed.

2. The learned AO/TPO erred in making transfer pricing adjustment without appreciating the fact that the appellant was a 51:49 joint venture (JV) between Mahindra & Mahindra Limited (M&M) and International Truck and Engine Mauritius Holding Limited (ITEMH) a step down subsidiary of Navistar International Corporation Inc., USA (NIC), respectively and in the case of JV, the transactions entered into between the JV and its JV partners are always at arm's length basis.

3. The learned AO/TPO erred in making transfer pricing adjustment amounting to INR 52,35,76,599 in respect of the international transaction of lump sum amount of USD 10 million paid as royalty to LuxIPCO, Luxembourg (associated enterprise) for the right to use the intellectual property and know-how in relation to Base Engine as per the direction of the DRP.

4. The learned DRP erred in not directing the TPO to accept the benchmarking analysis carried out by the appellant based on the Royalty Stat database.

5. The learned TPO erred in rejecting the CUP method applied by the appellant based on Discounted Cash Flow/Present Value Methodology of Valuation for determining the ALP for the above international transaction, which was also corroborated by a valuation report from the Registered Valuer during the course of assessment proceedings.

6. The learned TPO erred in not appreciating the submission made by the Assessee vide letter dated 28 January 2014 clarifying all the inconsistencies and irregularities that have been observed by the TPO in the valuation report.

7. The learned TPO erred in stating that the average rate of royalty rate 3%, which is in line with the industry norms, is not supported by the proper data. He erred in observing that the Assessee has not furnished the data based on scientific search or extraction of data from public domain.

8. The learned TPO erred in observing that the assumption of taking block of 8 years to suit the Assessee's convenience, makes the effort of DCF valuation fundamentally dented, and the results arrived at are distorted.

9. The learned TPO erred in observing that the Internal rate of return is negative. He erred in not appreciating that the projection considered by the appellant reflects the internal rate of return around 12% which itself show that the investment in technical know-how and intellection property is profitable.

10. The learned DRP erred in not directing the TPO to accept the a lump sum payment of royalty at ALP as the same has been paid after taking the approval from the Government of India (FIPB).Therefore, such approval can be considered as external CUP for determining the ALP for the above international transaction.

11. The learned DRP erred in not directing the AO to allow depreciation to the appellant as the fixed assets have already been put to use by the appellant during the previous year. The learned DRP erred in observing that the appellant has not filed actual proof of sales of prototype engines made during the previous year.

12. Each one of the above grounds of object is without prejudice to the other.

3. Grounds No. 1 to 10 are referring to arm's length price determination by the Assessing Officer with regard international transaction.

4. The assessee in this case has paid to associated enterprise a lump-sum of USD 10 million after withholding taxes, the same had equivalent to Indian Rs. 52,35,76,599.49. The assessee had adopted CUP method to benchmark its international transaction. Learned Transfer Pricing Officer (TPO) during the course of proceedings before him had asked the assessee to undertake appropriate method to benchmark research based on royalty stat database. However, TPO noted that tax payer did not furnish their methodology benchmark based on royalty stat database. The Assessing Officer rejected the assessee's approach of discounted cash flow/present value methodology for the purpose of valuation of technical and intellectual property. After discussion, TPO held that the assessee has not followed proper procedure for benchmarking international transaction. Hence he determined value of international transaction of royalty paid in the current year at Rs. Nil. Hence, the Assessing Officer computed adjustment of Rs. 52,35,76,599.49 to the total income of the assessee.

5. The assessee filed objection before DRP. The assessee, inter alia, filed additional evidence with separate benchmarking international transaction and claimed it to be at arm's length price. For this purpose, assessee has used

royalty stat database. Learned DRP admitted additional evidence and asked for the remand report from the TPO. Learned TPO observed that during the course of proceedings before him repeated opportunities were given to the assessee to benchmark international transaction of royalty payment separately while using royalty stat database. Hence, TPO reported that additional evidence now furnished may be rejected.

6. Learned DRP, however, admitted additional evidence. However, DRP dismissed benchmarking analysis carried out by the assessee from royalty stat database pertaining to report of 34 pages on the ground that the same was without any authentication, seal or signature of any agency. Although DRP noted that on the first page, name of Altus International has been mentioned, there is no seal and signature of any person or agency of in the report of 34 pages. Therefore learned DRP held that in absence of authenticate documentation benchmarking analysis, (TPSR) submitted by the assessee cannot be relied upon and hence same was rejected. Thereafter the DRP proceeded to examine action of the TPO and confirmed the same.

7. Against the above order, assessee is in appeal before us.

8. We have heard both the counsel and perused the records. At the outset, learned Counsel of the assessee submitted that the assessee has submitted the benchmarking analysis done based upon royalty stat research, which was asked by TPO itself during the proceedings before him. However, the same could be obtained only when proceedings were going on before DRP. Hence, learned Counsel of the assessee prayed that TPO clearly erred in rejecting benchmarking analysis report submitted by the assessee on the ground that it was not submitted earlier. He further submitted that DRP also has erred in not considering the same report despite accepting the same on the ground that the said analysis report was not authenticated. Learned counsel submitted that the said report was duly submitted under the cover of letterhead of Altus International and it was duly signed by the partner of Altus International BV.

He further submitted that the said covering letter and certificate of the partner, inter alia, also gave address and contact person and phone number for any question regarding report. Learned counsel prayed that if authorities have any doubt about the authenticity of this document, the same may have inquired from the number given or address given or from their website mentioned therein. Hence, prayed that appropriate direction may be given to TPO to consider benchmarking analysis report submitted by the assessee.

9. Per contra, learned Departmental Representative relied upon the orders of the authorities below.

10. Upon careful consideration, we find that TPO in this case has asked the assessee to submit benchmark analysis report done on the basis of royalty research database. The assessee could not provide the same when proceedings were going on before the TPO. The same could be provided only before DRP. Learned DRP asked for the remand report from the TPO. Learned TPO refused to offer any comment on the documents submitted by the assessee on the ground that the same was not submitted earlier before him. Despite this learned DRP accepted the additional evidence and proceeded to observe that the report was unauthenticated in as much as it was unsigned and did not contain seal of the reporting party. We have gone through the copy of the said report submitted. We find that the said report is submitted by Altus International. It contains covering letter which contains full address and website address of the firm. Based on the report of Altus International, range of royalty rate is also mentioned in the covering letter. It has duly been signed by the partner of the firm. It also contains contact persons and phone number for any question regarding report. In these circumstances, in our considered opinion, rejection by DRP of the benchmarking report submitted by the assessee is not sustainable. In our considered opinion if authorities below have any doubt about the authenticity of the document, same could have very well inquired from the address and phone number mentioned therein. Hence in our considered opinion, interest of justice demands that this issue may be

remitted to the TPO. Learned TPO is directed to consider this issue afresh in accordance with our direction and observation as above. It is open to assessee to canvas other grounds also before TPO with this regard.

11. Another issue raised is non-allowance of depreciation on fixed asset.

12. On this issue upon Assessing Officer's query that why claim of depreciation should not be allowed as business was not set up. The assessee responded as under :-

- A. "The assessee was in the process of setting up of a project to manufacture Mechanical engines for trucks. The said project was under execution as on 31st March 2010.
- B. The prototypes engines assembled during the year were sent to customer for testing and validation. The production was trail run production.
- C. Accordingly expenses incurred was reduced by the sale proceed of prototypes and the net amount was taken to capital work in progress.
- C. Since the expenses on test runs had been grouped under capital work in progress, the amount recouped by the assessee towards prototype engine was adjusted with the cost of construction of the project".

13. Considering the above Assessing Officer observed that the assessee has not submitted any explanation as to why depreciation should be allowed. He observed that the assessee itself has admitted that business not started till 31.3.2010 and disallowed all expenses. Hence, he held that when the assessee itself admitted that business did not start, question of allowing depreciation does not arise. Hence, the Assessing Officer rejected the claim of depreciation of Rs. 14,63,03,230/-. Upon assessee's objection, DRP observed that since TPO computed arm's length price royalty at 'nil', he also recommended to the Assessing Officer to withdraw corresponding claim of depreciation, on account of royalty having been capitalized by the assessee (in its books). Thereafter, learned DRP upheld the action of the Assessing Officer.

14. Against the above order, the assessee is in appeal before us.

15. Learned Counsel of the assessee submitted that the authorities below denied depreciation on asset acquired and put to use by the assessee during the relevant previous year. He submitted that the assessee has put to use said asset in the relevant previous year and had conducted trial run. That prototype engines were manufactured by taking trial run and then sold for validation testing. He submitted that said sale of prototype engines Rs. 52,47,878/- has been duly reflected in the audited annual accounts. Further submission of the assessee on this issue is as under :-

The learned DRP has observed that the said sale was not reflected in the accounts. It is submitted that the said sale income has been taken to the Balance Sheet in the books of account as per accounting standard and reduced from the expenditure on project to be capitalized in the accounts. It is submitted that such an accounting treatment had no bearing on the computation of taxable income. The assets were put to use by the appellant and therefore the appellant was eminently eligible to claim depreciation under Income Tax Act. The disclosures in the ROI regarding consumption of material (PB Page 165), production of finished goods viz. engines (PB Page 166) and depreciation on plant and machinery (PB Pages 175 to 179) were duly furnished by the appellant for the relevant previous year. The issue is squarely covered in favour of the appellant by the decision of Honourable Bombay High Court in the case of Larsen & Toubro Limited reported in 89 taxmann.com 186 wherein on the backdrop of similar set of facts Honourable Bombay High Court has allowed depreciation claim by holding that once the plant commenced operations and small quantity was produced on trial run basis the business of the assessee is set up even if product is in small quantity and sub standard and depreciation was to be allowed even if machinery was used for trial production. It is pertinent to submit that SLP against the said decision of Bombay High Court has been dismissed by Honourable Supreme Court (98 taxmann.com 368). It is prayed that depreciation claimed be allowed.

16. Per contra, learned Departmental Representative relied upon the orders of the authorities below.

17. Upon careful consideration, we are of the considered opinion that the authorities below have erred in appreciating the facts of the case as being

claimed by the assessee. Assessee's claim is that machines were duly put to use during the year in a trial run. In the trial run prototype engines were duly manufactured and they were then sold for validation and testing. Sale of said prototype engine for Rs. 52,47,878/- has been duly reflected in audited annual accounts as per details submitted above. In these circumstances, in our considered opinion, this issue needs to be remitted to the file of the Assessing Officer to consider the issue afresh in the light of the assessee's submission as above. Accordingly, issue stands remitted to the file of the Assessing Officer.

18. In the result, appeal of the assessee stands allowed for statistical purposes.

Order has been pronounced in the Court on 31.5.2019.

Sd/-
(RAMLAL NEGI)
JUDICIAL MEMBER

Sd/-
(SHAMIM YAHYA)
ACCOUNTANT MEMBER

Mumbai; Dated : 31/5/2019

Copy of the Order forwarded to :

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

//True Copy//

BY ORDER,

(Assistant Registrar)
ITAT, Mumbai

PS