

आयकर अपीलिय अधिकरण "सी" न्यायपीठ पुणे में ।  
**IN THE INCOME TAX APPELLATE TRIBUNAL "C" BENCH, PUNE**

**BEFORE SHRI R. S. SYAL, VP  
 AND  
 SHRI PARTHA SARATHI CHAUDHURY, JM**

आयकर अपील सं. / ITA No.565/PUN/2015  
निर्धारण वर्ष / Assessment Year : 2010-11

ACIT, Circle-9,  
 Pune.

.....अपीलार्थी / Appellant

**बनाम / V/s.**

Hyundai Construction Equipment (I) Pvt. Ltd.,  
 Plot No.A/2, Chakan MIDC, Phase-II,  
 Khalumbre, Chakan – Talegaon Road,  
 Chakan, Khed, Pune-410501.

PAN : AABCH8756Q

.....प्रत्यर्थी / Respondent

आयकर अपील सं. / ITA No.644/PUN/2015  
निर्धारण वर्ष / Assessment Year : 2010-11

Hyundai Construction Equipment (I) Pvt. Ltd.,  
 Plot No.A/2, Chakan MIDC, Phase-II,  
 Khalumbre, Chakan – Talegaon Road,  
 Chakan, Khed, Pune-410501.

PAN : AABCH8756Q

.....अपीलार्थी / Appellant

**बनाम / V/s.**

ACIT, Circle-9,  
 Pune.

.....प्रत्यर्थी / Respondent

Assessee by : Shri M. P. Lohia &  
 Shri Rajendra Agiwal  
 Revenue by : Shri Shivraj B. Morey, CIT

सुनवाई की तारीख / Date of Hearing : 07-06-2019

घोषणा की तारीख / Date of Pronouncement : 11-06-2019

**आदेश / ORDER**

**PER PARTHA SARATHI CHAUDHURY, JM :**

These cross appeals preferred by the assessee as well as by the Revenue emanates from the orders of the DRP/Assessing Officer dated

23.12.2014 and 27.02.2015 for the assessment year 2010-11 respectively. These cases were heard together and since facts similar & issues common, therefore, these cross appeals are being disposed of by this consolidated order.

2. First, we would take up the assessee's appeal in ITA No.644/PUN/2015 and the grounds of appeal are as under :-

*“Based on the facts and circumstances of the case, Hyundai Construction Equipment India Private Limited (‘the Appellant’) respectfully craves leave to prefer an appeal against the order passed under section 143(3) read with section 144C(13) of the Income-tax Act, 1961 (the ‘Act’) by the Assistant Commissioner of Income-tax, Circle 9, Pune (the ‘learned Assessing officer’ or the ‘learned AO’ or the ‘AO’) dated 27 February 2015 (received on 16 March 2015) on the following grounds, which are independent of and without prejudice to each other :*

*On the facts and in circumstances of the case and in law, the learned AO has erred as under:*

- 1 *Inappropriate transfer pricing adjustment amounting to Rs 20,24,62,986 made even though all international transactions of the Appellant are at arm's length  
Erred on the facts and in circumstances of the case and in law to propose an upward adjustment amounting to Rs 20,24,62,986 to the international transactions of the Appellant pertaining to manufacturing operations for financial year (‘FY’) 2009-10 thereby ignoring the fact that all the international transactions of the Appellant are at arm's length.*
- 2 *Inappropriate non-consideration of economic and commercial reasons for losses in the manufacturing operations of the Appellant  
Erred on the facts and in circumstances of the case by making transfer pricing adjustment to the international transactions of the Appellant pertaining to manufacturing operations without considering the fact that the losses in manufacturing operations are on account of economic and commercial reasons and not on account of transfer pricing.*
3. *Inappropriately selecting an additional company, BEML Limited as comparable to the Appellant for FY 2009-10 on an adhoc basis.  
Erred on the facts and in circumstances of the case and in law by inappropriately considering an additional company, BEML Limited as comparable to the Appellant for FY 2009-10 on an adhoc basis.*
- 4 *Inappropriately rejecting the methodology adopted by the Appellant for carrying out capacity utilization adjustment  
Erred on the facts and in circumstances of the case by inappropriately rejecting the methodology adopted by the Appellant for carrying out capacity utilization adjustment to the operating profit margins of comparable companies.  
Without prejudice to the above, erred on the facts and in circumstances of the case by inappropriately not considering capacity utilization adjustment using alternative method.*
- 5 *Inappropriate initiation of penalty proceedings under section 271(l)(c) of the Act*

*Without prejudice to the above grounds of appeal, erred on the facts and in law by proposing to initiate penalty proceedings under section 274 of the Act read with section 271(1)(c) of the Act, without considering the fact that, adjustment to transfer price is on account of difference of opinion which has consequently resulted in adjustment to the income of the Appellant.*

*Additional grounds of appeal*

6 *JCB India Limited, not a comparable company*

*Based on the facts and circumstances of the case, JCB India Limited is functionally different and accordingly, should not be considered as comparable to the manufacturing operations of the Appellant for FY 2009-10.*

7 *Action Construction Equipment Limited, a comparable company*

*Based on the facts and circumstances of the case, Action Construction Equipment Limited is functionally similar to the manufacturing operations of the Appellant and satisfies all qualitative and quantitative filters applied by the Appellant in its TP study for FY 2009-10, accordingly, Action Construction Equipment Limited should be considered as comparable company.*

*The Appellant craves leave to add, alter, vary, omit, substitute or amend the above grounds of appeal, at any time before or at the time of hearing of the appeal, so as to enable your Honours to decide this appeal according to law.”*

3. At the time of hearing, ld. AR of the assessee appraised the Bench that ground no.1 is general, ground no.5 is premature in nature needs no adjudication and ground nos.2, 6 & 7 are not pressed. In view of these submissions made by the ld. AR, **ground nos.2, 6 & 7 are dismissed as not pressed.** Ground no.1 is general in nature and ground no.5 as submitted by the ld. AR is premature, hence, on these grounds no adjudication is required. The only effective grounds are no.3 and 4 before us for adjudication.

4. With regard to ground no.3, ld. AR submitted by referring to the Annual Report of the company i.e. BEML Limited is a Government Company wherein 54% of the holding is by the Government and as per the Companies Act, if more than 50% holding of a company is by the Government then it is a Government Company. Ld. AR further submitted that a Government Company cannot be made a comparable to that of the

assessee. He placed reliance on the decision of the preceding year in assessee's own case in ITA No.1472/PUN/2015 for the assessment year 2009-10 wherein the same issue came up before the Co-ordinate Pune Bench of the Tribunal whether BEML Limited could be selected as a comparable to that of the assessee. On this issue, the Tribunal has held as follows :-

*“13. On hearing both the sides on this issue of exclusion of BEML on the ground of government company, we find it is an adjudicated issue already by the order of the Tribunal in the case of M/s. Behr India Ltd. (supra). The contents of paras 34 and 35 of the said order (supra) are relevant in this regard. For the sake of completeness, paras 34 and 35 are extracted hereunder :-*

*“34. We have heard the rival contentions and perused the record. In the IT Enabled Services Division, the assessee was providing services to its parent company in Germany and was a limited scope service provider. The assessee adopted TNMM method as the most appropriate method to benchmark its international transactions and had applied PLI of OP/OC. For benchmarking the said transactions, the TPO had selected certain concerns as comparable. Out of five external comparables selected, the TPO finally taken M/s. Kitco Ltd., M/s. Water & Power Consultancy Services (India) Ltd. and M/s. Engineers India Ltd. The assessee is aggrieved by the inclusion of said three concerns in the final set of comparables, wherein the said three concerns were Public Sector Enterprises providing consultancy and end to end solutions to government and other companies. The said concerns i.e. WAPCOS is a Mini Ratna - I Public Sector Enterprise; Engineers India Ltd. was a Government of India Enterprise and became Public Listed Company in 1996 and KITCO was established in 1972 by IDBI, Government of Kerala, seven Public Sector Banks and other National and State level financial institutions, to provide technical assistance and consultancy. We find merit in the plea of the assessee that where the concerns were working on governmental policies and social obligations, the risk profile and functions of the said Public / Government Enterprises were completely distinct and dissimilar from a concern which was a captive service provider to its associated enterprises. The assessee was operating on Cost Plus Method which was distinct from the operations of the Public Sector / Government Enterprises. Further, even from the risk perspective, the assessee ITA Nos. 566 & 645/PUN/2013 and ITA No. 2637/PUN/2016 does not bear material risk including credit risk product liability, etc., whereas the said concerns bear the market and credit risk and other risks.*

*35. The Hon'ble Bombay High Court in CIT Vs. M/s. Thyssen Krupp Industries India Pvt. Ltd. reported in 239 Taxman 46 (Bom) had excluded Engineers India Ltd. being **government company** and where **substantial part of its revenue came from executing projects of Public Sector Undertakings**. Following the same parity of reasoning, **we hold that Engineers India Ltd. and the other***

**concerns M/s. KITCO and M/s. WAPCOS are to be excluded from the final list of comparables.”**

14. Thus, the Government Companies operate entirely different controlled environment. Their customers are different. Their raw material suppliers are different. Their profit margins are different. They would not operate in a free competitive environment. Therefore, in our opinion, the orders of the lower authorities need to be reversed. The Co-ordinate Bench of the Tribunal has already taken a view in the matter. Considering the above reasoning as well as the Coordinate Bench decision (supra), we are of the opinion the Government company like BEML cannot be held as a good comparable to the one like the present assessee – a private company under consideration. Regarding the ld. DR’s argument about the existence of profit making company in the client list of BEML, we find it is not a sustainable argument.

14.1 Further, we find Hon’ble Bombay High Court has given a categorical finding about the requirement of excluding Government companies like M/s. Engineers India Limited held in the case of M/s. Thyssen Krupp Industries India Pvt. Ltd. (239 Taxman 46 (Bom.), is relevant and binding on us. For the sake of completeness, conclusion part of the judgment is extracted as under :-

“Where a substantial part of revenue of a comparable Co. in execution of turnkey projects arose out of executing projects of public sector undertakings, it could not be considered to be comparable to assessee-company providing turnkey services to its AE as contracts between Public Sector undertakings were not driven by profit motive alone but other consideration also weigh in such as discharge of social obligations etc.”

15. Therefore, the decisions of the CIT(A), Assessing Officer and the TPO are required to be reversed. Considering the relief granted to the assessee, we find it relevant to not go into the other arguments relating to the functional test of BEML and other arguments raised by the assessee’s AR. Accordingly, ground no.2 is allowed without going into the merits of the function test. Thus, ground no.2 is allowed.”

5. Ld. DR, *per contra*, placed strong reliance on the orders of the subordinate authorities though principally agreeing that the issue is covered in assessee’s own case as stated by the ld. AR.

6. We have perused the case records and heard the rival contentions. We observe that the issue is squarely covered in favour of the assessee by assessee’s own case for assessment year 2009-10 in ITA No.1472/PUN/2015 (supra) wherein it has been categorically held by the Co-ordinate Pune Bench that BEML Limited being a Government Company even without going into the merits of the functional test of BEML Limited,

it cannot be considered as a comparable to that with the assessee since Government Companies operate entirely in different controlled environment, customers are different, raw material suppliers are different, profit margins are different and would not operate in a free competitive environment. Respectfully following the decision of the Co-ordinate Bench, **we allow ground no.3 raised in appeal by the assessee.**

7. Coming to ground no.4, it was contended by the ld. AR that this issue has been restored back to the file of the Assessing Officer in the preceding year by the decision of the Co-ordinate Bench and the same view may be taken for this relevant year as well.

8. Ld. DR fairly conceded to the prayer of the ld. AR.

9. We have perused the case records and heard the rival contentions. We find that in ITA No.1670/PUN/2015, the Revenue has raised this ground in appeal before the Co-ordinate Bench for assessment year 2009-10 which is as follows :-

*“1. Whether on the facts and circumstances of the case, the Ld. CIT(A) erred in directing the AO to **make capacity adjustment** by recommending a method without justifying the reliability of the method?”*

10. With regard to this ground, the assessee had made the following relevant submissions which are as follows :-

*“32. Referring to Ground nos.1 and 2 (i.e. “capacity adjustment”), ld. Counsel for the assessee brought our attention to (i) the judgement of the Hon’ble Bombay High Court in the case of CIT vs. Petro Araldite (P.) Ltd. (256 Taxman 16) (copy of which is placed at page 436 of the Paper Book) as well as (ii) the contents of para 23 of the said decision of the Mumbai Bench of the Tribunal in the case of DCIT vs. Petro Araldite (P.) Ltd. in ITA No.3782/MUM/2012, order dated 24.07.2013 (copy of which is placed at page 440 to 454 of the Paper Book) and submitted that the formula provided in the said judgement is relevant. The detailed discussion mentioned by the CIT(A) in para 2.3.1 to 2.3.7 of his order are relevant. Further, the gist of the*

submissions extracted by the CIT(A) in para 2.3.1 is also relevant and hence, the said para (relevant portion) is extracted hereunder :-

*“2.3.1 The learned TPO computed the amount of the adjustment on account of the low capacity utilization as under :-*

*It is submitted that the capacity utilization in case of assessee this year in respect of manufacturing activity is only 4.50%, it has accordingly made adjustments to the PLI of the comparables whose capacity utilization is higher. In the show cause notice the assessee was informed that any adjustment can be made as per IT Rules only if there are material differences that affect prices of transactions and reasonably accurate adjustments can be made to eliminate these differences. In the reply, the assessee has side stepped the question as to how low capacity utilization affects the price of the transactions. Assessee has merely stated that capacity utilization is different. Second, as regard the reported capacity utilization which is more than 100% in the case of comparable, leading to doubts on the reliability of installed capacity figure and the corresponding capacity utilization, the assessee in its reply has merely reiterated that the figures should be accepted as reliable and that this is the only information in public domain.*

*The assessee in its TP report has claimed capacity utilization adjustments. The methodology adopted by the assessee comprises of fitting ‘a straight line through 3 data points on a two dimensional axis graph plotting Sales vs Total Costs for two comparables. The 3 data points is of sales and total costs for AY 2009-10 and two preceding years i.e. AY 2008-09 and 2007-08. This has been used by attempting to fit an equation  $y = a + bx$ . This mathematical model has been used to determine the average fixed costs across 3 years:*

*The method adopted is not found acceptable for the following reasons. Firstly, this involves data for 3 years which is not sanctioned by the IT Rules which require contemporaneous data to be used. No case has been set up justifying the use of data of prior 2 years. Secondly, this assumes a mathematical model that relationship between sales and total costs is linear. There is no evidence or basis to support this hypothesis. In fact it is generally not the case that fixed costs will remain the same across years. In theory of finance and accounting too, no such theory is found. Thirdly, the statistical indicator of goodness of fit to validate the accuracy of model is not submitted despite specifically calling for the same. Fourthly, a visual inspection of the scatter diagram shows that there are three data points through which a straight line is drawn which does not fit well. In the case of JCB, the two data points almost overlap and thus a straight line is drawn virtually through two points only. Thus, the assumption is neither accurate nor based in any financial theory. In fact, there is no analysis of the nature of actual expenditure. Hence, the methodology adopted is rejected.*

*9.8 Without prejudice to the view that adjustment can be made to PLI of comparables only in respect of transactional difference of functions, assets and risks and not to specific items of expenditure which may be higher in the case of the tested entity, the approach adopted in this order is to determine the adjusted PLI for each comparable treating depreciation as fixed costs, and assuming that the comparable operated at the same level of capacity utilization as the assessee ie at*

4.50%. The data of capacity utilization in the case of JCB India Ltd is not found to be reliable as mentioned in SCN. The data of capacity utilization is not available in, case of BEML. Hence, only, Telco Construction Equipment Co Ltd. is considered.

*Without prejudice to the argument as a full-fledged manufacturer carrying risk relating to capacity utilization, and hence adjustment is not demonstrated as warranted, the effect of difference in capacity utilization is eliminated by treating the depreciation expenses in case of each comparable as fixed costs, and computing the contribution at different level of capacity utilization. Accordingly, the adjusted PLI is determined adjusting for difference in capacity utilization in each case by comparing it with the assessee.”*

33. *Questioning the method adopted by the TPO in the present case, ld. AR for the assessee made various submissions in this regard and the same are extracted in para 2.3.2 of the order of the CIT(A). In the said submission, the assessee sought a direction from the CIT(A) to the Assessing Officer to accept the method used by the assessee to carry out ‘capacity utilization adjustment’ to the operating margins of the comparable companies identified by the assessee. The CIT(A) considering the same and directed the Assessing Officer to grant the “capacity utilization adjustment” by computing the formula specified in page 113 in the Book published by the Chamber of Tax Consultant, Mumbai in ‘**Practical Guide to Indian Transfer Pricing**’.”*

11. On this issue, the Co-ordinate Bench has observed and held as follows :-

*“35. Therefore, rejecting the assessee’s method for quantifying the “capacity utilization adjustment” to the tested party, we direct the Assessing Officer to follow the judgement of the Jurisdictional High Court in the case of Petro Araldite (P.) Ltd. (supra). The said judgement is relevant for following proposition :-*

*“(v) In the above view, taking into account the capacity utilization of the comparable, in the present facts, as it materially affects the profit margin, the invocation of Rule 10-B(1)(e)(iii) of the Rules, cannot be found fault with This is self evident position from the reading of the aforesaid provision that all aspects/difference between the international transactions and the comparable uncontrolled transactions which materially affects the net profit margin had to be taken into account so as to have the fair comparison while determining the ALP of the tested party’s transaction.”*

36. *Considering the above, we find this issue should be remanded to the file of the Assessing Officer to follow the precedent in existence on this issue and make the adjustment in any after granting a reasonable opportunity of being heard to the assessee. Accordingly, ground nos.1 and 2 stands allowed for statistical purposes.”*

12. Therefore, the Co-ordinate Bench had restored the matter to the file of the Assessing Officer following the judgment of the Jurisdictional High

Court in the case of CIT vs. Petro Araldite (P.) Ltd. (256 taxmann.com 16). Respectfully following this observation of the Co-ordinate Bench, we remand this issue to the file of the Assessing Officer. **This ground no.4 is allowed for statistical purposes.**

13. In the result, **the appeal of the assessee is partly allowed for statistical purposes.**

14. Now, we take up the Revenue's appeal in ITA No.565/PUN/2015.

The effective ground is as under :-

*"1. Whether on the facts and circumstances of the case, the Hon'ble DRP was justified in giving relief of Rs.15,59,09,042/- out of total adjustment made by the TPO, without appreciating the non-availability of authentic bifurcation of the transactions between the AE and Non-AE?"*

15. The issue herein is with regard to the inappropriate computation of transfer pricing adjustment on the total turnover of the assessee from manufacturing operations instead of adjustments, if any only on the value of international transactions pertaining to manufacturing operations. The assessee filed the grievance before the DRP that the TPO while making the adjustments to the international transactions pertaining to manufacturing operations had computed the adjustments on the total operating income of Hyundai India from manufacturing operations instead of only the value of international transactions pertaining to manufacturing operations. Thus, the TPO has made an adjustment even on the international transactions accepted at arm's length price and the transactions other than international transactions beyond his jurisdiction. Aggrieved, the assessee preferred appeal before the DRP. The assessee requested that the transfer pricing adjustment should be restricted to the value of international

transactions for which assessee relied on various judicial decisions such as :-

- (i) Demag Cranes & Components (India) Pvt. Ltd. – ITA No.120/PN/2011.
- (ii) DCIT, Mumbai vs. M/s. Starlite (2010-TII-28-ITAT-MUM-TP).
- (iii) Abhishek Auto Industries Ltd. vs. DCIT, New Delhi (2010-TII-54-ITAT-DEL-TP).
- (iv) Tara Ultima Pvt. Ltd. vs. ACIT (2010-TIOL-166-ITAT-Mum).

16. After considering the submission of the assessee, the DRP has given direction to compute and restrict the transfer pricing adjustment only on the value of international transaction pertaining to manufacturing operations. The facts on record further suggest that the TPO vide letter No.Pn/Addl.CIT(TP)-1/Appeal/HCEIPL/2014-15/453 dated 26.02.2015 has given the revised working of TP adjustment re-computed by him. Consequently, the reduction in the adjustment due to the effect given as per the direction of the DRP comes to Rs.15,59,09,042/-.

17. We have perused the case records and heard the rival contentions. We find the observation of the DRP on the issue is as follows :-

*“2.5.2 The assessee has relied upon certain decisions to claim that the transfer pricing adjustments should be restricted to the value of the international transactions. Since this is a case of import transactions, we agree with the assessee and direct that the transfer pricing adjustments should be restricted to the value of the international transactions. Hence, this objection of the assessee is accepted.”*

18. We are inclined to agree with the decision of the DRP since it is settled and accepted position of law and, therefore, we do not find any

infirmity with the findings of the DRP and the relief provided to the assessee is sustained. **Revenue's appeal is dismissed.**

19. Resultantly, **the appeal of the assessee is partly allowed for statistical purposes and the appeal of the Revenue is dismissed.**

Order pronounced on 11<sup>th</sup> day of June, 2019.

**Sd/-**  
**(R. S. SYAL)**  
**VICE PRESIDENT**

**Sd/-**  
**(PARTHA SARATHI CHAUDHURY)**  
**JUDICIAL MEMBER**

पुणे / Pune; दिनांक / Dated : 11<sup>th</sup> June, 2019

*Sujeet*

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

1. अपीलार्थी / The Appellant.
2. प्रत्यर्थी / The Respondent.
3. The DRP, Pune;
4. The CIT (Central), Pune;
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, "सी" बेंच, पुणे / DR, ITAT, "C" Bench, Pune.
6. गार्ड फ़ाइल / Guard File.

आदेशानुसार / BY ORDER,

//True Copy//

Senior Private Secretary  
आयकर अपीलीय अधिकरण, पुणे / ITAT, Pune