

आयकर अपीलीय अधिकरण, अहमदाबाद न्यायपीठ "डी" अहमदाबाद।
IN THE INCOME TAX APPELLATE TRIBUNAL
"D" BENCH, AHMEDABAD

BEFORE SHRI RAJPAL YADAV, JUDICIAL MEMBER
AND SHRI S. RIFAUR RAHMAN, ACCOUNTANT MEMBER

आयकर अपील सं./ ITA No. 2686/Ahd/2017

निर्धारण वर्ष/Assessment Year: 2011-12

The Dy. Commissioner of Income-tax, Circle 4(1)(1), Ahmedabad	Vs.	M/s. Schutz Dishman Biotech Ltd Bhadraraj Chambers, Nr. Swastik Cross Road, Navrangpura, Ahmedabad-380009 PAN : AACCS 0988 C
अपीलार्थी/ (Appellant)		प्रत्यर्थी/ (Respondent)
Revenue by :		Shri Vinod Tanwani, Sr DR
Assessee by :		Shri TP Hemani, AR

सुनवाई की तारीख/Date of Hearing : 20/06/2019

घोषणा की तारीख /Date of Pronouncement: 26/06/2019

आदेश/O R D E R

PER RAJPAL YADAV, JUDICIAL MEMBER:

The Revenue is in appeal before the Tribunal against the order of the learned CIT(A)-8, Ahmedabad dated 1st September 2017 passed for Assessment Year 2011-12.

2. The solitary grievance of the Revenue is that learned CIT(A) has erred in deleting the addition of Rs.3,89,36,781/- which was made by the Assessing Officer on the recommendation of Transfer Pricing Officer (TPO) in the value of International Transactions of the assessee with its Associated Enterprises (AE).

3. The brief facts of the case are that the assessee company has filed its return of income on 29.09.2012 declaring total income at Rs. Nil. At the relevant time, the assessee company was engaged in the business of manufacturing of pharmaceuticals and fine chemicals. In other words, assessee was bulk drug manufacturer. The learned Assessing Officer noticed international transactions of the assessee with its AEs and, therefore, he made a reference under Section

92CA(1) of the Income-tax Act, 1961 to the TPO for determining the Arms Length Price of International Transactions. The learned TPO has issued notice under Section 92CA(2) of the Act and a questionnaire to the assessee. On the scrutiny of the TP study report and other documents, he found that the assessee has two international transactions with its AEs namely:-

S No.	Description	Method used by the assessee	Amount in Rs.
1.	Purchase of Raw Material	TNMM	4,73,63,171
2.	Sale of various products	TNMM	10,22,42,056

4. The Assessing Officer thereafter observed that the assessee has adopted Transactional Net Margin Method (TNMM) for determining the ALP of its international transactions. It has adopted Profit Before Depreciation, Interest and Tax (PBDIT) as Profit Level Indicator (PLI). It has determined its PLI at 10.26%, which was compared with other comparable companies selected by the assessee. It was found out that the assessee's PLI at 10.26% was higher than the margin of comparable companies, i.e. 9.85%. Thus, according to the assessee, no adjustment is required in the value of the international transactions because it was at Arms Length. The TPO did not accept this contention of the assessee. He rejected the comparables selected by the assessee. He also rejected the method of determining PLI. In his opinion, the PLI ought to be adopted by dividing the operating profit by operating cost, i.e. operating profit/operating cost. The TPO thereafter selected the comparables whose PLI has been computed at 16.01%. He worked out the operating revenue by applying this PLI on the operating cost. The operating cost shown by the assessee was Rs.13,04,45,157/- by using the PLI of 16.01%. He worked out the operating revenue at Rs.15,13,29,427/-. The difference between the operating revenue shown by the assessee in the books vis-à-vis determined with the above formula has been worked out at Rs.3,89,36,781/- and this was recommended for making an adjustment in the value of the international transactions

undertaken by the assessee with its AEs. The working done by the TPO is reflected on page no. 57 of his order, which reads as under:-

“8. Thus after duly considering the contentions of the assessee submitted its reply to show cause notice the final average comparables PLI is calculated as follows:

S N	Company	Operating Revenues in Rs. Cr.	Operating Cost in Rs. Cr.	Operating Profit in Rs. Cr.	OP/Cost in%
1	Pure Pharma Ltd	16.93	15.98	0.95	5.94%
2	Tonira Pharma Ltd [Merged]0	31.2	31.32	-0.12	-0.38%
3	Harman Finochem Ltd	138.23	103	35.23	34.20%
4	Flamingo Pharmaceuticals Ltd	209.18	187.52	21.66	11.55%
5	Shilpa Medicare Ltd	263.37	204.57	58.8	28.74%
				Average Margin	16.01%

Now the computation of the adjustment in the case of the assessee is as follows:

Description	Amount in Rs.
Operating Cost as per books (computed in para 5.1 of show cause noticed)	13,04,45,157
Profit at Arms Length Price (ALP) @ 16.01% of operating cost	2,08,84,270
Operating Revenue (at ALP) (A)	15,13,29,427
Operating Revenue (Price) received as per books (computed in para 5.1 of show cause notice) (B)	11,23,92,646
Shortfall being adjustment u/s 92CA (C=A-B)	3,89,36,781
5% of the price shown in the books (i.e. international transaction in cost amounting to Rs.14,96,05,227/- (Sale and purchases)	74,80,261

9. Since the adjustment is more than $\pm 5\%$ limit, in view of the facts of the case, accordingly, as discussed above and calculated in above para an upward adjustment amounting to Rs. 3,89,36,781/- (rounded) is considered necessary to the total income of the company in order that the international transaction undertaken by the company are at arm's length. Consequence to this adjustment, the total income of the assessee is revised upwards by Rs.3,89,36,781/-.

(Total Upward Adjustment : Rs.3,89,36,781/-)”

5. On the basis of the recommendation made by the TPO, the Assessing Officer has made adjustment in the value of international transactions, and accordingly made addition in the assessment order.

6. Dissatisfied with the addition, the assessee carried the matter in appeal before the learned CIT(A). The assessee contended that qua the comparables selected by the TPO it took an objection that if the turnover filter is being applied, then they will be excluded. In other words, case of the assessee is that turnover of 50% ought to be applied on the higher side as well as on the lower side. For example, if the total sales of the assessee is of Rs.14.80 crores, then the comparable companies whose sales are in the range of Rs.7 crores on the lower side and beyond Rs.22 crores on the higher side deserves to be excluded. Since in the case of the assessee, its turnover was Rs.11.23 crores, then 50% of this i.e. Rs.5.6 crores and Rs.16.5 crores sales shown by the companies engaged in the similar line of business deserves to be taken as comparables. If any company has lesser sales than Rs.5.6 crores, then it will not be considered as comparable on account of turnover filter. Similarly, if a company has sales more than Rs.16.5 crores, then again it will lose its comparable status with the assessee. In support of this contention, assessee relied upon the order of the ITAT in assessee's own case in earlier years. Learned First Appellate Authority has accepted this contention and deleted the addition. The relevant findings of the learned CIT(A) read as under:-

"7.1 The submissions are considered. I agree with the appellant that since the issue is already covered by the order of the Hon'ble ITAT for A.Y.2006-07, the issue being same, it has to be followed. Thus, the turnover filter of 50 percent is required to be applied. In view of this, the range of turnover for the comparable comes to Rs.5,61,96,323 -Rs.16,85,88,969/-. However, I do not agree with the appellant that all the comparables chosen by the Assessing Officer are required to be rejected. The appeal of 50 percent cannot be so sacrosanct that a minor variation in it will not be allowed. It is seen that one of the comparable company, (as selected by the TPO) having nearest turnover with the turnover of the Appellant Company is Pure Pharma Ltd. having turnover of Rs.16.93Crores. It is also seen that the CIT(A) in A.Y.2007-08 has held that even if there is only one good comparable case, the same can be taken as suitable comparable and ALP can be determined on that basis.

Excerpt from CIT(A) order for A.Y. 2007-08 (p.232 of P/B):

"It has also been held by Hon'ble ITAT Delhi Bench in the case of Haworth (India) (P.) Ltd. v. DCIT (OSD) in ITA No. 5341/Delhi/2010 reported in 11 Taxmann.com 76 (2011) that even if there is only one

good comparable case, the same can be taken as suitable comparable and Arms-Length Price can be determined on that basis."

7.2. Based on this revised comparable, the position can be tabulated as under:

Description	Amount in Rs
Operating Revenue as per books (computed in para 5.1 of show cause notice)	11,23,92,646
Profit at Arms length Price (ALP) @ 10.26 % of Operating Revenue (A)	1,15,31,485
Profit at Arms length Price (ALP)@ 5.94% of operating Revenue (B)	66,76,123
Excess Profit (C=A-B)	48,55,362

The above given table shows that as a matter of fact the appellant has shown better PLI than its peers and therefore no adjustment in the ALP is called for.

7.3. It is also noticed that even if the range is extended to 300% +/- of the Turnover of the appellant, only two companies would be left for comparison which can be tabulated as under:

S.No.	Company	Op/Cost in %
1.	Pure Pharma Ltd.	5.94%
2.	ToniraPharma Ltd. [Merged]	-0.38%
	Average Op/Cost in %	2.78%

The appellant has a better Op/Cost @ 10.26% compared to 2.78% as stated above. Hence, no adjustment in ALP on this ground could be made.

7.4. In view of the discussion above, as the issue is covered by the order of the Hon'ble ITAT for A.Y.2006-07 in own case of the Appellant, the impugned addition made by the TPO is deleted."

7. Before us, learned Counsel for the assessee placed on record the copies of the Tribunal orders in earlier assessment years which has been followed by the CIT(A). He also placed on record that even in other assessment years, i.e. AYs 2007-08, 2008-09, 2009-10 and 2010-11, similar issue has been considered and consistent approach has been adopted. He made reference to the order of the ITAT passed in ITA Nos. 954 & 1229/Ahd/2012 for Assessment Year 2007-08. These appeals have been decided by the Tribunal after the order of the CIT(A) on 05.06.2018. The Tribunal has followed the orders in earlier years

and upheld the application of turnover filter. Consequently, the Tribunal has rejected the appeal of the Revenue on this issue. Learned Departmental Representative, on the other hand, was unable to controvert this contention of the learned Counsel for the assessee.

8. We have duly considered rival submissions and gone through the records carefully. Identical issue was considered by the Tribunal in assessee's own case for Assessment Year 2007-08 vide order dated 05.06.2018. The findings of the Tribunal on this issue read as under:-

"8. We have duly considered rival contentions and gone through the record. As observed earlier, the Revenue and the assessee have not disputed selection of appropriate method i.e. TNMM; selection of tested party i.e. assessee; selection of profit level indicator i.e. operative profit/operative cost. They are only disputing on selection of comparables. The assessee has selected four comparables viz. Advik Laboratories Ltd., Gujarat Terce Laboratories Ltd., Zyden Gentc Ltd., and Welcure Drug & Pharmaceuticals Ltd. All these comparables were not accepted by the TPO because according to him, they were not engaged in manufacturing bulk drug, rather they are manufacturing formulations i.e. tablets, capsules, syrups etc. Thus, the ld.TPO selected comparables which were engaged in manufacturing of bulk drugs. The comparables selected by the TPO and working of their PLI reads as under:

Name of Company	Economic Activity	Sales Cr.	Export Cr.	Export % of the total sales
Advik Laboratories Ltd	Drug Formulations	9.74	0.0	0%
Gujarat Terce Laboratories Ltd	Drug Formulations	11.22	0.04	0.36%
Zyden Gentec Ltd	Drug Formulations	7.12	1.2	16.85%
Welcure drug & Pharmaceuticals Ltd	Drug Formulations	18.79	0.07	0.37%

9. On the basis of above PLI, the ld.TPO has worked out adjustment required to be made in the value of international transactions entered by the assessee with its AE. The first question for our determination is whether turnover filter is to be applied or not. According to the ld.DR, this filter ought not to be applied. She made reference to the decision of ITAT, Mumbai. However, we are of the view that in large number of decisions, it has been held that turnover filter is one of the essential filter in order to select comparables when acted in same atmosphere. It is pertinent to observe that while conducting transfer price analysis an effort is being made to compare related party transactions undertaken by the assessee with the uncontrolled transactions undertaken by the comparable, and thus arrive at a conclusion as to whether transaction bench

mark is at arm's length or not. For example, a chosen company, though functionally comparable has entered international transactions beyond a percentage with related parties, it is quite possible that its overall profit may have distorted due to such transaction rendering it as un-comparable. There are so many other circumstances which are required to be examined under FAR analysis, and due to this, adjudicator is required to apply appropriate filter in order to work out comparables which have not under any influence of the related party transactions. Hon'ble Bombay High Court in the case of CIT Vs. Pentair Water India (P.) Ltd., 381 ITR 216 concluded that turnover is obviously a relevant factor to be considered for comparability. Hon'ble High Court has relied upon the decision of Hon'ble Delhi High Court in the case of CIT Vs. Agnity India Technologies (P.) Ltd., (2013) 36 taxmann.com 289. Thus, there are conflicting decisions in favour or against the application of turnover filter. However, the ld.Revenue authorities have not brought to our notice of any judgment of the Hon'ble jurisdictional High Court which prohibits application of turnover filter. Therefore, we are of the view that the ld.CIT(A) has rightly made an analysis that smaller companies having turnover of Rs.3 crores could not be considered as comparable with the assessee who has turnover of Rs.15.84 crores. Similarly, the company who has turnover of more than Rs.30 crores could not be compared with the assessee. Thus, we do not find any error in the order of the ld.CIT(A) on this aspect, and if we uphold the turnover filter then the ground of appeal raised by the Revenue is required to be rejected. Accordingly, we reject the grounds of appeal raised by the Revenue."

9. Since there is no disparity on the facts and on the principle of applicability of turnover filter, learned CIT(A) has followed the orders of ITAT in earlier years and its view is in consensus with the view of the ITAT in Assessment Year 2007-08 also. If turnover filter is being applied on the comparables, then they will be excluded and no adjustment will be made. Learned CIT(A) has rightly deleted the addition. We, therefore, do not find any merit in this appeal of the Revenue, which is rejected.

10. In the result, appeal is dismissed.

Order pronounced in the Court on 26th June, 2019 at Ahmedabad.

Sd/-

**(S. RIFAUR RAHMAN)
ACCOUNTANT MEMBER**

Ahmedabad; Dated 26/06/2019

Sd/-

**(RAJPAL YADAV)
JUDICIAL MEMBER**

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

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. संबंधित आयकर आयुक्त / Concerned CIT
4. आयकर आयुक्त(अपील) / The CIT(A)
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, अहमदाबाद / DR, ITAT, Ahmedabad
6. गार्ड फाईल / Guard file.

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