

**IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH 'I-2', NEW DELHI**

**BEFORE SH. N. K. BILLAIYA, ACCOUNTANT MEMBER
AND
SH. SUDHANSHU SRIVASTAVA, JUDICIAL MEMBER**

ITA No.6435/DEL/2012
Assessment Years: 2008-09

M/s. Capsugel Healthcare (Formerly Bharti Healthcare Limited), 21, Joniawas, Dharuhera (Distt.), Rewari, Haryana- 122100	Vs	ACIT Circle Rewari Haryana
(APPELLANT)		(RESPONDENT)

Appellant by	Sh. Nageshwar Rao, Advocate
Respondent by	Sh. H. K. Choudhary, CIT DR

Date of hearing:	08/08/2019
Date of Pronouncement:	26/08/2019

ORDER

PER N. K. BILLAIYA, AM:

This appeal by the assessee is preferred against the order dated 25.10.2012 framed u/s. 143 (3) r.w.s 144 C of the Act.

2. The assessee is aggrieved by the following transfer pricing adjustments:-

1. Adjustment to ALP of transaction related to sale of furnished goods to Associated Enterprises (AE's)
2. Adjustment related to arms length price of transaction of purchase of fixed assets from Associated Enterprises.

3. Briefly stated the facts of the case are that the assessee is a Pfizer Group company. Pfizer procured Bharti Health Care Limited from Bharti Enterprises. Bharti Healthcare Limited was in the business of manufacturing and marketing of empty head gelatin capsules. Bharti Health Care acquired by Pfizer through Pfizer Pharmaceuticals India Private Limited holds 94.68% of equity shares of the company. Assessee has a plant located at Dharuhera, Haryana. The international transactions under taken during the year are summarized as under :-

S. No.	Description of transaction	Method	Value (in Rs.)
1	Sale of Consumables	Not benchmarked	111,318
2	Sale of Finished Goods (Hard Gelatine Capsule Shells)	CUP	44,800,172
3	Purchase of Fixed assets	Not benchmarked	79,111,841

4	Expenses reimbursed	Not benchmarked (cost to cost recharge)	53,21,991
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4. The dispute under consideration before us relate to transaction mentioned at Sr. No.2 and 3 above.

5. **Sale of finished goods – Hard gelatin capsules Shells :** In its transfer pricing study report the assessee has stated that in regard to international transaction of sale of consumables it had purchased certain consumables from domestic market for its internal use. But after purchasing the consumables the company realized that these consumables are not of any use of the company. So it sold these consumables to its AE's who were in need of these consumables. Since this transaction was not the principle business activities and since the value of this transaction was not significant no bench marking was required and the transaction is considered at arms length.

6. So far as the international transaction of sale of finished goods is concerned the assessee selected the comparable uncontrolled price [CUP] method as the most appropriate method. It was submitted that empty hard gelatin capsules were sold to AE's as well as non AE's and since average rate charged from non AE's during the year under consideration for the same product is

less than the rate charged from AE's, the transaction was taken at arms length price.

7. During the transfer pricing assessment proceedings the TPO observed that this is not a fair comparison. The TPO was of the firm belief that for fair comparability not only contractual terms should be same but the date of the transaction should also be same and if not possible at least nearby dates should be attempted.

8. A show cause notice was issued to the assessee to explain why the CUP method used by it should not be discarded and replaced by TNMM as the most appropriate method. The assessee filed a detailed reply justifying its claim that CUP is the most appropriate method (MAM). The assessee emphasized that since internal CUP is available the same should be accepted as the MAM for bench marking the international transaction relating to sale of finished goods and since the transaction is at arms length price no adjustment need to be made.

9. The submissions of the assessee did not find any favour with the TPO who was of the opinion that there was no direct correlation in the dates of sale to related and unrelated parties and the nature of invoicing was different. The TPO further observed that the quantum of variety of gelatin capsules shells sold varied between related and unrelated parties.

10. Not convinced with the CUP method as the MAM. The TPO proceeded to apply TNMM and used three comparables namely Medicaps, Sunil Health Care and Associated Capsules and computed the transfer pricing adjustment as under :-

	Capsugle	Medicaps	Sunil Healthcare	Associated Capsules
Income	(in thousands)			
Net Sales	115033	18,06,64,971/-	25750023	2,804887410
Stock	632	-38006671	6546952	-9804400
Other op income	2981	179442	0	0
Total	117382	177037742/-	264047184/-	2795083010
Expenses				
Cost of materials	57077	53247093	85333234	1486341343
Mfg Expenses	81901	36935938	80433626	1486341343
Personnel Exp	51995	27349098	26066301	462322842
Admn. Exp	40391	21670118	0	342910519
Sales & Mktg	6828	0	13762584	0
Depreciation	24667	8273212	20453273	66592853
Total Cost (TC)	262859	147475459	226049018	2351867557
Operating Profit (OP)	-145477	29562283	37998166	436915453
OP/TC (%)	-55.345	20.05%	16.81%	18.53%
Mean OP/TC of comparables			18.46%	

Thus it is seen that the assessee has booked an OP/TC margin of (55.34%) as compared to 18.46% of the comparables.

Calculation of ALP of sales of hard gelatin capsules

The assessee has sold the hard gelatin capsules to its AE's at a price of Rs.44,800,172. In the proportion of Revenue and Expenses at entity level the cost of the transaction translates to Rs.100,323,119. On this cost the assessee should have charged to markup of 18.46% and the corresponding arm's length price of sales should have been Rs.11,88,42,767/-. Since the price charged is Rs.44,800,172 the difference on this account is Rs.7,40,42,595/-. The Assessing Officer shall, accordingly increase the taxable income by Rs.7,40,42,595/-.

11. Objections were raised before the DRP but the DRP confirmed the transfer pricing adjustment made by the TPO.

12. Before us the counsel for the assessee vehemently reiterated that CUP is the MAM and, therefore, the TNMM method adopted by the TPO is uncalled for and the transfer pricing adjustment should be deleted. It is the say of the counsel that the TPO has used three comparables out of which only the financials of Medicap is available in the public domain and the financials of Sunil Healthcare and associated Capsules were obtained by the TPO after issuing notice u/s. 133 (6) of the Act. The counsel stated that the assessee could not be expected to comply with these two comparables as the financials data are not available in the public domain but are available with the TPO. The counsel stated that no opportunity of cross examination was made available which is against the decision of the Hon'ble High Court of Delhi in the case of Cash Edge India Private Limited in WP

3628/2016 counsel continued by stating that the TPO has not granted the adjustment over difference in excluding the working capital of the assessee viz-a-viz the comparable companies nor he has granted the adjustment for difference in the capacity utilization of the assessee viz-a-viz the comparable companies. The Counsel urged on accepting the internal TNMM proposed by him stating that the internal TNMM is also good comparable. The counsel further stated that the TPO should be directed to examine internal TNMM as proposed by the assessee.

13. Per contra the DR strongly supported the findings of the TPO.

14. We have carefully considered the orders of the authorities below. The quarrel is in respect of the most appropriate method. The assessee claims that CUP is the MAM in the given circumstances and the revenue states that TNMM is the MAM method as the CUP method adopted by the assessee is full of flaws.

15. We find that the assessee has adopted average rate of sale to unrelated parties for the whole year and compared with the rate of sale booked to related parties. We, further find that from FOB value of invoice of related parties, amount of commission allowed has been deducted. In case of sales to AE freight paid has been added.

16. In our considered view this is not a fair comparison. In our understanding, not only contractual terms should be same but date of the transaction should also be same. We are of the considered view that the application of average rates leads to highly skewed results. In direct methods of comparison 1 to 1 comparability should be made, transaction by transaction invoices need to be analyzed on same or closest available dates. We find that the assessee has drastically increased the price in a few uncontrolled transactions in comparison to sale of products to associate enterprises at lower prices than uncontrolled rates, therefore, we are of the opinion that the CUP method used by the assessee cannot be accepted as the MAM.

17. However, at the same time we find that the TNMM method used by the TPO though is the MAM but the working capital adjustment and the capacity utilization has to be considered in the light of the fact that the financials of two of the comparables are not available in the public domain and the TPO has used the same by calling the financial data u/s. 133 (6) of the Act without giving any opportunity to the assessee.

18. Considering the facts of the case in totality we hold that TNMM is the MAM on the given facts and direct the TPO to allow working capital adjustment and capacity utilization adjustment in respect of the comparables used by him after affording reasonable opportunity of being heard to the assessee. Ground No.2 to 6 are allowed for statistical purposes with the above directions which

will also adjudicate ground No.10 raised, through, the application for raising the additional ground of appeal.

19. Coming to the second transfer pricing adjustment relating to purchase of fixed asset from associated enterprises, the facts on record show that in order to improve product facility the assessee had purchased fixed assets from its AE. Since the fixed assets were proprietary items of the AE no practical method is available to establish that the prices paid for asset acquisition is at arms length. As the assets acquired have been capitalized and not expensed of the depreciation on these assets only affect the taxable profits.

20. There is no dispute that assets acquisition is being made for up-gradation of technology that will improve the overall financial aspect of assessee's business and reduce the cost of goods procured.

21. The TPO has treated the ALP at nil as against book value of Rs.79,11,841/- which again was confirmed by the DRP.

22. Before us the Counsel for the assessee vehemently stated that no third party invoice can be produced since the value addition was made at the end of the AE. The counsel further stated that the transaction value determined by custom authorities in custom valuation report should not have be

discarded by the TPO and prayed for accepting the custom authorities valuation.

23. Per contra DR strongly supported the findings of the TPO. It is the say of the DR that the purpose and process of determination of value by the custom authorities are different and there is no link between custom valuation and valuation of goods for purpose of transfer pricing in income tax.

24. We have carefully considered the orders of the authorities below and have given a thoughtful consideration to the rival contentions. There is no dispute that the asset purchased by the assessee from its AE are proprietary design items of the AE, therefore, invoices from unrelated parties cannot be available to this extent. We agree with the counsel that the ALP cannot be taken as nil. This would amount to hold that the fixed assets purchased by the assessee from its AE have no cost or are purchased at nil cost. This would give absurd results. In our considered opinion the quarrel can be settled if the AE is treated as the tested parity. We find that through application for the admission of additional evidences, the assessee has provided certain additional information relating to the transaction of fixed assets by treating the AE as the tested party.

25. We restore this issue to the file of the TPO and direct the TPO to treat the AE as the tested party and direct the assessee to furnish necessary details/ documents for the determination of the

ALP by treating the AE as the tested party. Ground No.7 and 9 are treated as allowed for statistical purposes.

26. This will also cover the additional grounds raised in relation to this transfer pricing adjustment.

27. In the result, the appeal filed by the assessee is allowed for statistical purpose.

Order pronounced in the open court on 26.08.2019.

Sd/-
(SUDHANSHU SRIVASTAVA)
JUDICIAL MEMBER

NEHA

Date:-26.08.2019

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

Sd/-
(N. K. BILLAIYA)
ACCOUNTANT MEMBER

ASSISTANT REGISTRAR
ITAT NEW DELHI

Date of dictation	16.08.2019
Date on which the typed draft is placed before the dictating Member	19.08.2019
Date on which the typed draft is placed before the Other member	26.08.2019
Date on which the approved draft comes to the Sr.PS/PS	26.08.2019
Date on which the fair order is placed before the Dictating Member for Pronouncement	26.08.2019
Date on which the fair order comes back to the Sr. PS/ PS	26.08.2019
Date on which the final order is uploaded on the website of ITAT	26.08.2019
Date on which the file goes to the Bench Clerk	26.08.2019
Date on which file goes to the Head Clerk.	
The date on which file goes to the Assistant Registrar for signature on the order	
Date of dispatch of the Order	