

IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH : I-2 : NEW DELHI
BEFORE SHRI R.K. PANDA, ACCOUNTANT MEMBER
AND
MS SUCHITRA KAMBLE, JUDICIAL MEMBER

ITA No.1928/Del/2017
Assessment Year: 2012-13

Ocap Chassis Parts Pvt. Ltd.,
62, Sreshtha Vihar,
Vikas Marg Extension,
New Delhi.

Vs ACIT,
Circle-19(1),
New Delhi.

PAN: AAACO4028M

(Appellants)

(Respondents)

Assessee By : Shri Vishal Kalra, Advocate
Deptt. By : Ms Nidhi Sharma, Sr. DR

Date of Hearing : 24.09.2019

Date of Pronouncement : 11.12.2019

ORDER

PER R.K. PANDA, AM:

This appeal filed by the assessee is directed against the order dated 20th January, 2017 passed by the Assessing Officer u/s 143(3) r.w. section 144C of the IT Act, 1961 relating to the assessment year 2012-13.

2. Facts of the case, in brief, are that the assessee is a company engaged in the business of manufacturing of automobile, steering and suspension parts for the auto manufacturers. It filed its return of income on 30.11.2012 declaring the total income of Rs.71,98,240/-. Since the assessee had entered into certain international

transactions, the Assessing Officer referred the matter to the Transfer Pricing Officer u/s 92CA of the Act for determination of the arm's length price of the international transactions. The TPO passed an order proposing an adjustment of Rs.2,69,92,075/-. The Assessing Officer, in the draft assessment order accordingly made the addition and determined the total income at Rs.3,41,90,315/-. The assessee approached the DRP who upheld the action of the A.O./TPO. Accordingly, the Assessing Officer passed the final order making the addition of Rs.2,53,72,551/-.

3. Aggrieved with such order of the A.O./TPO/DRP, the assessee is in appeal before the Tribunal raising the following grounds:-

1. That on facts and circumstances of the case and in law, the reference made by the Ld. Assessing Officer suffers from jurisdictional error as the Ld. AO did not record any reasons in the assessment order based on which he reached the conclusion that it was "expedient and necessary" to refer the matter to the Ld. Transfer Pricing Officer ("TPO") for computation of the arm's length price, as is required under section 92 CA (1) of the Act.

2. That on the facts and in the circumstances of the case and in law, the Ld. AO erred in assessing the total income of the Appellant at INR 32,570,791 as against income of INR 7,198,240 returned by the Appellant, after making transfer pricing adjustment of INR 25,372,551.

3. That on the facts and circumstances of the case and in law, the Ld. AO / Ld. TPO erred in making an addition, on transfer pricing matter, amounting to INR 25,372,551/-, to the Appellant's income by:

3.1 modifying the comparability analysis conducted in the transfer pricing documentation of the Appellant on inappropriate and inadequate grounds;

3.2 selecting companies which were not comparable to the Appellant on various grounds;

3.3 disallowing, without appreciating the facts, economic adjustment on account of a sales downturn made by the Appellant to factor for the different

geographic markets of operation vis-a-vis companies selected for arm's length price determination;

3.4 selecting current year (i.e. financial year 2011-12) data for comparability;

4 That on the facts and circumstances of the case and in law the Ld. AO/ Ld. TPO erred in not examining the validity of initiation of penalty proceedings u/s 271 (1) (c) of the Act.

5. That on the facts and circumstances of the case and in law, the Ld. AO erred in charging and computing interest under section 234B, 234C and 234D of the Act.

That the appellant craves leave to add, alter, amend or withdraw any ground of appeal either before or at the time of hearing of this appeal as they may be advised. That, the above grounds are independent and without prejudice to each other.ö

4. The assessee has also raised two additional grounds. However, at the time of hearing, the ld counsel did not press the additional ground No.1 for which the ld. DR has no objection. Therefore, we are not concerned with the same. So far as the additional ground No.2 is concerned, the same reads as under:-

ö2. That on the facts and circumstances of the case and in law, the DRP/ TPO have erred in making negative working capital adjustment for the differences in working capital between comparable companies vis-a-vis the Appellant.ö

5. Relying on various decisions, the ld. counsel for the assessee submitted that this additional ground being purely legal in nature do not require any fresh investigation into the facts and, therefore, the same should be admitted.

6. After hearing both the sides, the additional ground raised by the assessee is admitted for adjudication.

7. The ld. counsel for the assessee, at the time of hearing, did not press ground of appeal No.1, 2, 3.1 and 3.4 for which the ld. DR has no objection. Accordingly, these grounds are dismissed as not pressed. Ground No.4 being premature at this juncture is dismissed. Ground of appeal No.5 relating to levy of interest u/s 234B, 234C and 234D being mandatory and consequential in nature, therefore, the same is dismissed.

8. So far as transfer pricing adjustment of Rs.2,53,72,551/- is concerned, the facts of the case, in brief, are that the assessee, during the year has entered into the following international transactions:-

No.	Nature of transaction	Method	Value of transaction
1	Purchase of raw Material	TNMM	1,715,551
2	Purchase of Consumables		9,278
3	Sale of goods		428,344,863
4	Purchase of machinery		487,004
5	Payment of royalty		479,898
6	Availing of technical services		180,804
7	Reimbursement of expenses to AE's		7,311,328

9. It was seen that the assessee benchmarked the international transactions using Transactional Net Margin Method (TNMM) and Profit Level Indicator (PLI) of Operating Profit/Operating Cost. The assessee earned operating profit margin of 6.08% (after claiming idle capacity adjustment) vis-à-vis arithmetic mean of comparable companies being 5.91%.

10. The assessee had identified the following five comparable companies:-

S.No.	Name of the Company	Return on cost (basis 3 years weighted average as per TP documentation)	Return on cost (Single year updated margins) 6 refer pages 195-196 of paper book
1.	Bharat Gears Ltd.	7.62%	6.98%
2.	Hindustan Hardy Spicer Ltd.	1.01%	5.10%
3.	Raunaq Automotive Components Ltd.	8.66%	7.35%
4.	Talbros Engineering Ltd.	5.72%	8.67%
5.	Rane (Madras) Ltd.	6.54%	6.84%
Arithmetic Mean		5.91%	6.99%

11. The TPO accepted the claim of the assessee for capacity utilization adjustment and worked out the average margin of the comparable companies at 0.8%. He, however, selected the following two additional companies, namely, Rane TRW Steering Systems Ltd. and ZF Steering Gear (India) Ltd., as comparable companies. After granting working capital adjustment on the margin of the comparable companies, the TPO finally proposed the upward adjustment of Rs.2,69,92,075/- the details of which are as under:-

Company Name	OP/OC %	WCA OP/OC %
Bharat Gears Ltd.	2.57%	5.28%
Hindustan Hardy Spicer Ltd.	-0.04%	2.39%
Raunaq Automotive Components Ltd.	-0.78%	1.32%
Talbros Engineering Ltd.	-1.31%	1.27%
Rane (Madras) Ltd.	-2.24%	0.36%
Rane TRW Steering Systems Ltd.	1.84%	4.30%
Z F Steering Gear (India)Xtd,	5.58%	8.08%
Average	0.80%	3.28%

Particulars	Amount
Operating Cost	466,852,450
Arm's length margin (%)	3.28%
Arm's length margin (Rs.)	15,312,760
Arm's length Price	482,165,210
Price charged by the assessee	455,173,135
Difference between ALP and Price	26,992,075

12. Since there were certain errors while computing the ALP, the DRP directed the TPO to consider the same based on which the Assessing Officer finally made addition of Rs.2,53,72,551/- as against the upward adjustment of Rs.2,69,92,075/- proposed by the TPO.

13. The Id. counsel for the assessee, at the outset, challenged the inclusion of Rane TRW Steering Systems Ltd. and ZF Steering Gear (India) Ltd., as comparables. So far as Rane TRW Steering Systems Ltd., is concerned, he submitted that this company is not functionally comparables since it is engaged in two divisions, namely, Steering gear division and hydraulic pumps & seat belt division whereas the assessee is engaged in the manufacture of automobile steering and suspension parts. He submitted that the assessee is not engaged in the business hydraulic pumps and seat belt division as that of Rane TRW Steering Systems Ltd.

14. Referring to Rule 10TA of the IT Rules, 1962, the Id. counsel for the assessee drew the attention of the Bench to clause (b) of the said Rule and drew the attention of the Bench to the definition of 'Core auto components' which means ó

- (i) Engine and engine parts, including piston and piston rings, engine valves and parts cooling systems and parts and power train components
- (ii) Transmission and steering parts, including gears, wheels, steering systems, axles and clutches;
- (iii) Suspension and braking parts, including brake and brake assemblies, brake linings, shock absorbers and leaf springs.

15. He accordingly submitted that the business of the assessee comes within the ambit of manufacturing core auto components which has been given a separate treatment by the legislature as compared to manufacture of non-core components as in the auto industry the business of manufacture and sale of these two segments is very different.

16. Further, the segmental data are not available. He submitted that the assessee company primarily caters to the AEs based in Europe and has recorded export sales of 98.90% of the total sales where as Rane TRW Steering Systems Ltd. caters to the domestic market. It reported export sales of 78.09 crores which is 11.47% of the total sales during the F.Y. 2011-12. Further, Rane TRW Steering Systems Ltd., is engaged in the research and development activities in their product/process development and thereby incurred R&D expenses during the year whereas the assessee did not incur any such expenditure during the year. He submitted that Rane TRW Steering Systems Ltd., was rejected by the assessee in previous two

years while benchmarking the analysis which was accepted or not challenged by the TPO. Referring to the copy of the TP study report and the order u/s 92CA(3) for assessment year 2010-11 and 2011-12, he submitted that the TPO has accepted the rejection of Rane TRW Steering Systems Ltd., and has not considered the said company as a comparable company. Relying on the following decisions, he submitted that comparables have been excluded on account of owning intangible assets:-

- (i) Avaya India (P.) Ltd. vs ACIT [ITA No. 532 of 2019] Delhi HC
- (ii) Flour Daniel India Pvt. Ltd. vs ACIT [ITA No. 973/Del/2016], further upheld by Delhi HC in the case of Pr. CIT vs Flour Daniel India Pvt. Ltd. [ITA No. 665/2019]
- (iii) Alcatel-Lucent India Ltd. vs ACIT [ITA No. 1112/Del/2017]
- (iv) Transcend MT Services (P.) Ltd. vs ACIT [ITA Nos. 4048 & 4501 / Del/ 2013]
- (v) Qualcomm India Pvt. Ltd. vs DCIT [ITA No. 1810/Del/2014]
- (vi) Torus Business Solutions Pvt vs DCIT [ITA No. 1974/Del/2015], further upheld by Honøble Delhi Court in the case of Pr. CIT vs Torus Business Solutions Pvt. Ltd. [ITA No. 207/2019] (Delhi High Court)
- (vii) CGI Information Systems & Management Consultation (P.) Ltd. vs DCIT [ITA No. 502/Bang/2016]

17. Referring to the following decisions, he submitted that the comparables have been excluded on account of carrying out Research & Development activities:-

- (i) Terex India Private Ltd vs DCIT [ITA No. 4791/Del/2015];
- (ii) Calibrated Healthcare Systems India Pvt. Ltd. vs ACIT [ITA No. 5271/Del/2012];
- (iii) CIT Vs Agnity India Technologies Pvt. Ltd. [ITA No. 1204/Del/2011]

18. Relying on the following decisions, he submitted that low export sales have been considered appropriate criteria for exclusion of a comparable:-

- (i) Omniglobe Information Technologies (India) Pvt. Ltd vs Addl. CIT [ITA No. 6980/Del/2017];
- (ii) Cypress Semiconductor Technology India (P.) Ltd. vs DCIT [IT(TP) A No. 1002/Bang/2011; and
- (iii) 24/7 Customer.com (P.) Ltd. vs DCIT [ITA No. 227/Bang/2010]

19. He accordingly submitted that Rane TRW Steering Systems Ltd., should be excluded from the list of comparables since it owns substantial intangibles, has carried out R&D activities and has low export sales as compared to total sales.

20. The ld. DR, on the other hand, heavily relied on the order of the A.O./TPO/DRP.

21. We have considered the rival arguments made by both the sides and perused the record. We find the TPO, in the order passed u/s 92CA(3) added Rane TRW Steering Systems Ltd., as a comparable. From the orders passed u/s 92CA(3) for the assessment year 2010-11 and 2011-12, we find the TPO has accepted the TP analysis filed by the assessee and has not considered Rane TRW Steering Systems Ltd., as a comparable. Further, we find from the various details furnished by the ld. counsel that this company is not functionally comparable since Rane TRW Steering Systems Ltd., is engaged in two divisions, namely, steering gear division and hydraulic pumps & seat belt division whereas the assessee is engaged in the automobile steering and suspension parts. The assessee is not engaged in the business of hydraulic pumps and seat belt division as that of Rane TRW Steering Systems Ltd. We further find the segmental data in the case of Rane TRW Steering Systems Ltd., are not available. It has been held in various decisions that when segmental data is not available, a company cannot be considered as a comparable. Apart from the above, we also find the export sale of the assessee is 98.90% of the total sales whereas the export sale of Rane TRW Steering Systems Ltd., which primarily caters to the domestic market is 11.47% of the total sales. Apart from the above, Rane TRW Steering Systems Ltd., is engaged in the research and development activities in their product/process development and thereby has incurred huge Research & Development expenses during the year which is verifiable from the annual audit report placed at page 514 and 515 of the paper book. It also holds intangible assets which are verifiable from the notes on

fixed assets, copy of which is placed at pages 553 and 554 of the paper book. In view of all these i.e., diversified business, low export sale, non-availability of segmental data, incurring of expenditure on R&D activities and presence of intangibles, we are of the considered opinion that Rane TRW Steering Systems Ltd., cannot be considered as a comparable company. We, therefore, direct the A.O./TPO to exclude Rane TRW Steering Systems Ltd., from the list of comparables.

22. So far as ZF Steering Gear (India) Ltd., is concerned, the ld. counsel submitted that this company also is not functionally comparable since it is engaged in diversified business. Referring to the copy of the annual report of ZF Steering Gear (India) Ltd., he submitted that it clearly demonstrates that it is in the business of generating renewable energy through solar and windmill. The energy from its windmills has been utilized in-house and accounts for 96% of the energy utilized by it for its manufacturing business, thus, resulting in a different business module. Referring to page 662, 663 and 665 of the paper book, he submitted that ZF Steering Gear (India) Ltd., has also recorded income from sale of long-term investments, cost of which is unknown and cannot be determined. Further, the export sale of ZF Steering Gear (India) Ltd., is 0.5% of the total sales as against export sale of 98.90% to the total sales in the case of the assessee. He submitted that ZF Steering Gear (India) Ltd., is engaged in research and development activities in their product/process development during the year whereas the

assessee has not incurred any such expenditure during the year. Relying on the decisions cited while arguing exclusion of Rane TRW Steering Systems Ltd., he submitted that all these decisions are also applicable to the present comparable. He accordingly submitted that ZF Steering Gear (India) Ltd., should be excluded from the list of comparables.

23. The ld. DR, on the other hand, heavily relied on the order of the A.O./TPO/DRP.

24. We have heard the rival arguments made by both the sides, perused the orders of the A.O./TPO/DRP and the paper book filed on behalf of the assessee. We have also considered the various decisions cited before us. We find the TPO added ZF Steering Gear (India) Ltd., as a comparable while determining the ALP of the international transaction although the assessee has not considered the same. From the details furnished by the assessee in the paper book, we find from the annual report of ZF Steering Gear (India) Ltd., that it is also in the business of generating renewable energy through solar and windmill. The energy from its windmills has been utilized in-house and accounts for 96% of the energy utilized by it for its manufacturing business. Therefore, we find force in the argument of the ld. counsel that it results in a different business module. The submission of the ld. counsel that ZF Steering Gear (India) Ltd., has recorded income from sale of long-term investments, cost of which is unknown and cannot be determined, could not be controverted by the ld. DR. Apart from the above, from the details

furnished by the assessee, we find the export sales of the assessee is 98.90% of the total sales whereas the export sale of ZF Steering Gear (India) Ltd. is only 0.5% of the total sales. Therefore, we find merit in the argument of the ld. counsel that ZF Steering Gear (India) Ltd., cannot be compared to the assessee which is catering primarily to the European market. We further find from page 665 of the paper book that ZF Steering Gear (India) Ltd., has carried out research and development activities in their product/process development during the year and has incurred huge R & D expenses. However, the assessee company has not incurred any such R & D expenses. In view of the above and relying on various decisions to the proposition that the comparables have to be excluded on account of carrying out research and development activities and considering the fact that the comparable company has very low export sales as compared to that of the assessee, we hold that ZF Steering Gear (India) Ltd., cannot be considered as a comparable. We, therefore, direct the A.O./TPO to exclude ZF Steering Gear (India) Ltd., from the list of comparables.

25. So far as the additional ground raised by the assessee is concerned, the same relates to making negative working capital adjustment for the differences between the working capital of comparable companies vis-à-vis the assessee.

26. After hearing both the sides, we find the TPO, during the TP proceedings, granted working capital adjustment on the margin of the comparable companies even though the same was not asked for and calculated the average margin of the

comparable companies at 3.28% (after working capital adjustment of cost of the assessee). He accordingly computed the TP adjustment. The Id. DRP dismissed the ground raised by the assessee objecting the working capital adjustment in the light of the assertion of the Assessing Officer that the said claim was already allowed to the assessee at the time of TP proceedings.

27. The Id. counsel for the assessee submitted that the TPO, in his order, has wrongly stated that the assessee asked for such working capital adjustment. He submitted that working capital adjustment was never sought by the assessee and was also not required in the case of the assessee. He submitted that the relevant market factors such as difference in inventories, debtors and creditors play a major role while setting up price mechanism for transactions in independent scenario. The said factors have already been considered by the assessee during the price setting process for transactions between the assessee and its AEs. He submitted that the TPO, after arriving at the arithmetic mean of all comparables at 0.80%, worked out the negative working capital adjustment thereby making ALP at 3.28%. He submitted that the working capital adjustment is made for the time value of money lost when credit time is provided to the customers. However, in the instant case, majority of sales are made to the related parties. Therefore, the assessee is running its business with no working capital risk while the comparable companies primarily caters to the domestic markets having working capital risk.

Relying on the following decisions, he submitted that the negative working capital adjustment is not warranted:-

- (i) Inductis India Pvt. Ltd. vs ACIT: ITA No. 1203/Del/2017 (Del - Trib.)
- (ii) TNS India Pvt Ltd vs ACIT: ITA No. 1927/Hyd/2011 (Hyderabad - Trib.)
- (iii) Lam Research India (Private) Limited vs DCIT: IT(TP) A No.1437/Bang/2014.
- (iv) DCIT vs Software AG Bangalore Technologies Pvt. Ltd. [IT(TP)A No 1628/Bang/2014]
- (v) Adaptec (India) Private Limited vs ACIT [ITA No. 206 /Hyd./ 2014]
- (vi) CAPCO IT Services India (Pvt) Limited vs ITO [ITA No. 1340/Bang/2011]

28. He accordingly submitted that when the assessee has not claimed any working capital adjustment, the TPO cannot make a negative adjustment in the working capital. He accordingly submitted that such negative working capital adjustment should be cancelled.

29. The ld. DR, on the other hand, heavily relied on the order of the A.O/TPO/DRP.

30. We have considered the rival arguments made by both the sides, perused the orders of the A.O./TPO/DRP and the paper book filed on behalf of the assessee. We have also considered the various decisions cited (supra). We find the TPO,

after arriving at the arithmetic mean of all comparables at 0.80%, worked out the negative working capital adjustment thereby making arm's length price at 3.28%. It is the submission of the ld. counsel that neither the assessee has sought any working capital adjustment nor the same is required in the case of the assessee. It is also his submission that working capital adjustment is made for the time value of money lost when credit time is provided to the customers. However, in the instant case, the sales are made to the related parties and, therefore, there is no working capital risk whereas the comparable companies primarily cater to the domestic market having working capital risk. Therefore, according to the ld. counsel, negative adjustment on account of working capital is not required.

31. We find merit in the above arguments of the ld. counsel. It is an admitted fact that more than 94% of the sales made by the assessee are to the related parties and, therefore, the assessee is running its business with no working capital risk whereas the comparables companies who primarily cater to the domestic market are having working capital risk. Under such circumstances, if at all any working capital adjustment has to be made, then, it has to be a positive adjustment and there cannot be any negative working capital adjustment. We find the Delhi Bench of the Tribunal in the case of Inductis India Pvt. Ltd. (supra) has held that in case the assessee renders ITES Services to the AE, there was no need for making any negative working capital adjustment when the assessee did not carry any working capital risk. The Bangalore Bench of the Tribunal in the case of Lam Research

India (Private) Limited (supra) has held that negative working capital adjustment cannot be carried out where the assessee was a captive service provider. The Hyderabad Bench of the Tribunal in the case of Adaptec (India) Private Limited (supra) has held that there is no need for making any negative working capital adjustment when the assessee does not bear any working capital risk. The Bangalore Bench of the Tribunal in the case of CAPCO IT Services India (Pvt) Limited (supra) has held that where the assessee did not carry any working capital risk, there was no need for making any negative working capital adjustment. Since, in the instant case, majority of sales i.e., 94% of the total sales made by the assessee is to its related parties, therefore, the assessee, in our opinion, is running its business with no working capital risk. Therefore, in view of the decisions cited (supra), we are of the considered opinion that the TPO/DRP were not justified in making negative working capital adjustment. Therefore, the additional ground raised by the assessee is allowed.

32. In the result, the appeal filed by the assessee is partly allowed.

The decision was pronounced in the open court on 11.12.2019.

Sd/-

(SUCHITRA KAMBLE)
JUDICIAL MEMBER

Sd/-

(R.K. PANDA)
ACCOUNTANT MEMBER

Dated: 11th December, 2019

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Copy forwarded to :

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR

Asstt. Registrar, ITAT, New Delhi