

IN THE INCOME TAX APPELLATE TRIBUNAL
PUNE BENCH "C", PUNE – VIRTUAL COURT

BEFORE SHRI R.S. SYAL, VICE PRESIDENT AND
SHRI PARTHA SARATHI CHAUDHURY, JUDICIAL MEMBER

आयकर अपील सं. / ITA No.1958/PUN/2019

निर्धारण वर्ष / Assessment Year : 2015-16

Knorr Bremse Systems for Commercial Vehicles India Private limited, S.No.276/1, Village Mann, Hinjewadi, Phase-II, Taluka Mulshi, Pune – 411 057, Maharashtra, India PAN : AACCK1395D	Vs.	DCIT, Circle-14, Pune
Appellant		Respondent

Assessee by

Shri Rajendra Agiwal

Revenue by

Shri Sardar Singh Meena

Date of hearing

21-01-2021

Date of pronouncement

22-01-2021

आदेश / ORDER

PER R.S.SYAL, VP :

This appeal by the assessee is directed against the final assessment order dated 04-10-2019 passed by the Assessing Officer (AO) u/s.143(3) r.w.s.144C(13) of the Income-tax Act, 1961 (hereinafter called 'the Act') in relation to the assessment year 2015-16.

2. Briefly stated, the facts of the case are that the assessee is a wholly owned subsidiary of Knorr Bremse, Asia Pacific Holding Limited, Hong Kong. It is engaged in manufacturing air braking

systems including compressors and electronic braking systems, components of air braking system, such as, valves, brake cylinders, air treatment, disc brakes etc. and wheel-end products for commercial vehicles. A return was filed declaring total income at Nil after adjustment of current year losses. The assessee reported certain international transactions in Form No.3CEB. The AO made a reference to the Transfer Pricing Officer (TPO) for determining the Arm's Length Price (ALP) of the international transactions. The TPO observed that out of twelve reported international transactions, the assessee applied the Comparable Uncontrolled Price Method (CUP) in respect of the last two and the Transactional Net Marginal Method (TNMM), on consolidated basis, in respect of the first ten. There is no dispute in respect of the last two transactions. The assessee computed its Profit Level Indicator (PLI) of Operating profit to Operating revenue (OP/OR) at (-) 9.10% in relation to the first ten transactions on an aggregate basis. Certain comparables were selected. In the process of the ALP determination, the assessee *suo motu* offered transfer pricing adjustment of Rs.2,88,11,571/-, which amount was added to the total income. The TPO computed the PLI of the assessee at (-)12.04%. Considering the average

OP/OR of comparables at 4.06%, the TPO computed the transfer pricing adjustment of Rs.19,66,02,197/-. The assessee assailed the ALP determination before the Dispute Resolution Panel (DRP), which restricted the amount of transfer pricing addition to Rs.16,77,90,626/- after allowing credit for the voluntary transfer pricing adjustment of Rs.2.88 crore offered by the assessee in the computation of total income. This has brought the assessee before the Tribunal.

3. We have heard the rival submissions through Virtual Court and scanned through the relevant material on record. The first issue in this appeal is against the computation of assessee's own PLI at (-) 12.04% in respect of the first ten international transactions on an aggregate basis, as against the assessee's computation at (-) 9.10%. The area of dispute is further narrowed down to the consideration of certain items credited to the Profit and loss account treated by the assessee as operating, which were reclassified by the TPO as non-operating. He treated Interest received; Rental income; Forex gain; Provision for write back; and Miscellaneous income, as non-operating. The assessee, in the extant appeal, has not disputed the treatment given by the

TPO to the first three items: Interest received; Rental income; and Forex gain.

4. We espouse the first disputed item, namely, Provision for write back at Rs.41,59,867/-. Its break-up has been given at page 563 of the paper book, consisting of two items of write back, viz., Provision for warranty expenses at Rs.32,59,867/- and Provision for IT Support charges at Rs.9.00 lakh. We have gone through the detail of the Provision for warranty that has been set out at Note 27 in the Notes to financial statements of the assessee. It shows opening balance of the provision at Rs.1.11 crore. Then there is a reduction of provision used during the year at Rs.33.29 lakh and an addition of Rs.32,59,867/-, being, the amount of provision reversed during the year. It is this amount of the provision reversed during the year which is subject matter of the extant dispute. The Id. AR was required to point out the amount of provision created during the year, if any, for ascertaining if that was also considered as part of operating cost. In reply, he submitted that no fresh provision was created during the year because the brought forward provision was sufficient enough to meet the warranty expenses during the year. On a further query, the Id. AR could not point out any break-up of the opening

provision of Rs.1.11 crore for ascertaining at our end if the same was taken as operating cost in determination of the ALP of the respective years. It goes without saying that reversal of a provision takes the same colour as its creation. If it is considered as operating cost at the time of its creation, then its reversal in the later years will also qualify to be considered as operating revenue and *vice-versa*. Here is a case in which the assessee is claiming reversal of the provision made during the year as operating revenue without demonstrating the nature of provision at the time of its creation as to operating or non-operating. The Id. AR submitted that necessary details can be culled out from the record, which were not readily available. Taking a holistic approach, we set aside the impugned order on this score and remit the matter to the file of AO/TPO for ascertaining the treatment given to the warranty provision at the time on its creation in the relevant year. If the amount of provision in the year of its creation was taken as part of operating cost, then its reversal during the year should also be given the same treatment of operating revenue and *vice-versa*.

5. The second component of the provision reversed is a sum of Rs.9.00 lakh representing Provision of IT Support service charges. In response to the same query, which was raised for the

provision of warranty expenses, the Id. AR gave a similar reply that necessary details were not available off-hand. Following the view taken hereinabove in respect of reversal of Provision for warranty expenses, we set-aside the impugned order in respect of reversal of Provision for IT Support service charges as well and remit the matter to the file of AO/TPO for ascertaining the nature of Provision of IT Support service charges at the time of its creation. If it was taken as a part of operating cost in the relevant year, then its reversal in the year under consideration should also assume the same shade and *vice-versa*.

6. The next contested item is Miscellaneous income of Rs.6,58,711/- that was taken by the TPO as non-operating as against the assessee's claim of operating revenue. Details of Miscellaneous income are available at page 576 of the paper book. Here it is apposite to mention that total Miscellaneous income credited to the Profit and loss account at Rs.38.90 lakh was considered by the assessee as operating revenue. The TPO accepted the assessee's contention in respect of Service charges of Rs.21.69 lakh and Insurance of Rs.10.63 lakh. He only refuted the assessee's claim in respect of VAT refund of Rs.3,63,363/- and Other miscellaneous income of Rs.2,95,348/-.

7. In respect of VAT refund of Rs.3.63 lakh, the Id. AR again could not demonstrate as to how the payment of VAT was considered. We, therefore, set-aside the impugned order in respect of VAT refund having been treated as non-operating by the TPO and send the matter back to the file of AO/TPO for ascertaining whether the payment of VAT was taken as operating or non-operating cost. In case the payment of refund was taken as non-operating expense, then naturally, the VAT refund will also be taken as non-operating and *vice-versa*.

8. The last item is 'Other miscellaneous income' of Rs.2.95 lakh. The Id. AR candidly accepted that no details of such amount were available. In that view of the matter, it is manifest that the same cannot be considered as operating income as the assessee has failed to make out any case. The view taken by the authorities below in respect of this item is countenanced.

9. The next issue raised by the assessee in this appeal is against not allowing the proportionate transfer pricing adjustment. The TPO determined the arithmetic mean of the PLI of the comparables at 4.06%. He started the ALP determination of the assessee with a figure of Operating revenue of Rs.122.00 crore. This was deduced by considering total revenue of the assessee at

Rs.125.78 crore as reduced by Interest received, Rental income, Forex gain, Provision for write back and Miscellaneous income, giving the amount of Operating income at Rs.122.01 crore. The TPO took up this figure and computed the transfer pricing adjustment. The assessee specifically raised the issue before the TPO that the transfer pricing adjustment should be restricted to the AE transactions only, which did not find favour with the TPO as well as the DRP.

10. Having heard the rival submissions and perused the relevant material on record, we find that this issue is no more *res integra* in view of the judgment of Hon'ble Bombay High Court in *CIT Vs. Phoenix Mecano (India) Pvt. Ltd. (2019) 414 ITR 704 (Bom.)* holding that the transfer pricing adjustment can be made only in respect of AE transactions and not the entity level transactions. It is further observed that the Department's SLP against this judgment has since been dismissed by the Hon'ble Supreme Court in *CIT Vs. Phoenix Mecano (India) Pvt. Ltd. (2018) 402 ITR 32 (St)*. In view of this legal position, we hold that the transfer pricing adjustment cannot extend to non-AE transactions. The impugned order to this extent is set-aside and the matter is remitted to the file of AO/TPO for restricting the transfer pricing

adjustment only in respect of the AE transactions. Needless to say, the assessee will be allowed reasonable opportunity of hearing in such fresh proceedings.

11. In the result, the appeal is partly allowed for statistical purposes.

Order pronounced in the Open Court on 22nd January, 2021.

Sd/-
(PARTHA SARATHI CHAUDHURY)
JUDICIAL MEMBER

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

पुणे Pune; दिनांक Dated : 22nd January, 2021
सतीश

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

1. अपीलार्थी / The Appellant;
2. प्रत्यर्थी / The Respondent;
3. The CIT(A)-13, Pune
4. The Pr.CIT-V, Pune
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, पुणे "सी" /
DR 'C', ITAT, Pune;
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

// True Copy //

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

		Date	
1.	Draft dictated on	21-01-2021	Sr.PS
2.	Draft placed before author	21-01-2021	Sr.PS
3.	Draft proposed & placed before the second member		JM
4.	Draft discussed/approved by Second Member.		JM
5.	Approved Draft comes to the Sr.PS/PS		Sr.PS
6.	Kept for pronouncement on		Sr.PS
7.	Date of uploading order		Sr.PS
8.	File sent to the Bench Clerk		Sr.PS
9.	Date on which file goes to the Head Clerk		
10.	Date on which file goes to the A.R.		
11.	Date of dispatch of Order.		

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