IN THE INCOME TAX APPELLATE TRIBUNAL
"J" BENCH, MUMBAI

BEFORE SHRI PRAMOD KUMAR (VICE PRESIDENT)

AND

SHRI SAKTIJIT DEY(JUDICIAL MEMBER)

I.T.A. No.2916/Mum/2015
(Assessment Year : 2008-09)

Merck Limited Shivsagar Estate Dr Annie Besant Road Worli, Mumbai-18 **PAN : AAACE2616F**	vs	ACIT, Circle-7(3)(2), Mumbai
(APPELLANT)		**(RESPONDENT)**

Appellant by	Smt. Aarti Vissanji(AR)
Respondent by	Shri N. Padmanabhan (DR)

Date of hearing	07-01-2021
Date of Pronouncement	04/02/2021

O R D E R

Per Saktijit Dey (JM),

This is an appeal by the assessee against order dated 10-02-2015of learned Commissioner of Income Tax (Appeals)-57, Mumbai for the assessment year 2008-09.

2. In ground no. 1, the assessee has challenged the addition of Rs.95,48,976/- made on account of transfer pricing adjustment.

3. Briefly the facts are, the assessee is a resident company and is engaged in manufacture and sale of pharmaceutical and chemical products including bulk drugs, pigments and licensed products. The assessee is a part of Merck group headed by Merck KGAA Incorporated under

the laws of Germany. During the year under consideration, the assessee had entered into various international transactions with its overseas Associate Enterprises (AEs) including purchase of raw materials known as Active Pharmaceutical Ingredients (API). In the transfer pricing study report, the assessee had benchmarked the international transactions by applying transactional net margin method (TNMM). The Transfer Pricing Officer (TPO), while examining the transfer pricing study report accepted the benchmarking of the assessee in respect of most of the transactions. However, only in respect of one of the raw-materials/API, viz. Bisoprolol Fumarate, the TPO proposed to apply comparable uncontrolled price (CUP) method on the reasoning that similar product has been exported by Unichem Laboratories Ltd at a price of Rs.32,624.56, whereas, the assessee has purchased the same product from AE @Rs.64,815/- per keg. Thus, applying the rate at which Unichem Laboratories Ltd has exported the product as CUP, the TPO proceeded to determine the arm's length purchase price of Bisoprolol Fumarate at Rs.96,77,749/-. Thus, he proposed an adjustment of Rs.95,48,976 which was added to the income of the assessee in the assessment order. Though, the assessee contested the aforesaid addition before the first appellate authority; however, was unsuccessful.

4. The learned Counsel appearing for the assessee submitted, the TPO, though, has accepted all other transactions of the assessee benchmarked under TNMM to be at arm's length, he has only picked up purchase of a single API and applied CUP for determining the ALP. She submitted, the CUP applied by the TPO is invalid as M/s Unichem Laboratories Ltd has exported the product outside India and to European markets. She submitted, while deciding identical issue involving purchase of very same API, the Tribunal in assessee's own case for assessment year 2009-10 an 2010-11, though, has accepted applicability of CUP as most appropriate method, however, the Tribunal has observed that while applying CUP, the price at which the product is available in the domestic market should be applied for determining the arm's length price. Though, of course, the Tribunal also observed that only those domestic transactions which are more than 20 kgs should be considered. The learned Counsel submitted, in view of the aforesaid observation of the Tribunal, the export sale price of Unichem Laboratories Ltd cannot be applied as CUP. However, she submitted, one more reason for inapplicability of the export sale price of Unichem Laboratories Ltd is because, out of

the four parties to whom exports were made, three are related parties. In this context, she drew our attention to the information received from Unichem Laboratories Ltd as reproduced in the show cause notice. The learned Counsel submitted, in absence of a valid CUP consisting of domestic price of the product for a transaction quantity of more than 20 kgs, the benchmarking done by the assessee under TNMM has to be accepted.

5. The learned Departmental Representative submitted, CUP has been accepted as the most appropriate method to benchmark the purchase of API even by the Tribunal. Therefore, the export sale price of Unichem Laboratories Ltd should be adopted with necessary adjustment.

6. We have considered rival submissions in the light of decisions relied upon and perused materials on record. It is a fact on record that the assessee had benchmarked all its international transactions including purchase of raw materials (API) under TNMM. It is also evident, except the transaction relating to purchase of one API, viz. Bisoprolol Fumarate, the TPO has accepted all other transactions to be at arm's length. Only in respect of the aforesaid product, the TPO has applied CUP as the most appropriate method and for comparability purpose, has considered the purchase price charged for export sales made by Unichem Laboratories Ltd. It is worth mentioning, under identical facts and circumstances and for the very same API, the TPO had applied CUP method for determining the ALP in assessee's own case for Assessment Years 2009-10 and 2010-11. When the matter ultimately travelled to Tribunal, the co-ordinate bench, though, upheld applicability of CUP, however, accepting assessee's plea held that considering strict quality control and stringent regulatory method followed in Germany compared to India, 10% quality adjustment has to be provided while determining ALP under CUP. Further, accepting assessee's plea, the Tribunal in no uncertain terms has held that only the price at which the product is sold in domestic market, that too, sale transaction exceeding quantity of 20 kgs has to be considered for applying CUP. Admittedly, in the facts of the present case the TPO while applying CUP has considered the price charged for export sales made by Unichem Laboratories Ltd. Therefore, in our considered view, such price adopted for applying CUP is invalid. That being the case, when no comparable

price for sale of the product in the domestic market is available in terms of the directions of the Tribuanl in assessee's own case for Assessment Years 2009-10 and 2010-11 vide ITA No.1946/Mum/2014 and others, dated 31-03-2016, there is no other course left open, but to accept the benchmarking of the assessee under TNMM. In view of the above, we delete the addition of Rs.95,48,976/-. This ground is allowed.

7. Ground No.2.1 being general, we dismiss the same.

8. In ground 2.2., the assessee has challenged the disallowance of 70% out of the expenditure incurred towards distribution of samples.

9. Briefly the facts are, in course of assessment proceedings, the Assessing Officer noticed that the assessee has debited an amount of Rs.4,84,43,325 towards distribution of free samples and stock. Noticing this, he called upon the assessee to furnish various details including confirmations of the persons to whom such free samples were distributed. As alleged by the Assessing Officer, the assessee was unable to provide the requisite details. Alleging that the assessee failed to substantiate the expenses and taking note of the fact that in the previous year similar expenditure claimed by the assessee was disallowed to the extent of 70%, the Assessing Officer followed the same and allowed 30% of the expenditure claimed. Though, the assessee contested the aforesaid disallowance before the first appellate authority; however, the disallowance was sustained.

10. Reiterating the stand taken before the departmental authorities the learned Counsel for the assessee submitted, distribution of free samples being made purely for the purpose of business, has to be allowed as expenditure. She submitted, though, while deciding identical issue in assessee's own case for Assessment Year 2013-14, learned DRP has restricted the disallowance to 20% of the amount claimed, however, in case of another assessee, viz. Johnson & Johnson Ltd Vs. CIT (2014) 150 ITD 377 (Mum), the Tribunal has restricted the disallowance to 2% of the amount claimed. Thus, she submitted, the disallowance may be restricted to 2%.

11. The learned Departmental Representative relied upon the observations of the Assessing Officer and learned Commissioner (Appeals).

12. We have considered rival submissions and perused materials on record. As could be seen from the observations of the departmental authorities, various details called for by the Assessing Officer could not be furnished by the assessee. It is also relevant to observe, while deciding identical issue in assessee's own case for Assessment Year 2003-04 in ITA No.925/Mum/2007 dated 19-07-2013, the Tribunal has restored the issue to the Assessing Officer for fresh examination after verifying the details of names and addresses of doctors. Keeping in view the aforesaid directions of the Tribunal in assessee's own case, we restore the issue to the Assessing Officer for fresh examination after due opportunity of being heard to the assessee. While doing so, the Assessing Officer may also examine the decision of the co-ordinate bench in case of Johnson & Johnson Ltd vs CIT (supra). This ground is allowed for statistical purpose.

13. In ground no. 2.3, assessee has challenged disallowance of Rs.1,09,16,789/- under section 14A of the Act. The only submission made before us by the learned Counsel for the assessee is, while working out the disallowance, the Assessing Officer has also included investment ofRs.65.50 crores in REC Bond and investment of Rs.73.50 crores in NSB, NABARD and REC Bonds held as on 3-03-2008 and 31-07-2007 respectively, which would yield taxable income. Therefore, such investment should be excluded for computing disallowance under rule 8D(2)(iii). We find substantial force in the aforesaid submission of the assessee. Accordingly, we direct the Assessing Officer to verify the claim of the assessee and exclude the investments capable of yielding taxable income from the average value of investment for computing the disallowance under rule 8D(iii). Needless to mention, the Assessing Officer must afford reasonable opportunity of being heard to the assessee before deciding the issue.

14. In ground no. 2.4, the assessee has challenged disallowance ofRs.1,36,67,817 by invoking section 145A of the Act.

15. In course of assessment proceedings, the Assessing Officer, while examining the details of loans and advances furnished by the assessee, noticed that the assessee had receivables on account of CENVAT credit and other taxes. Taking note of the fact that in preceding assessment year similar disallowance was made under section 145A of the Act, followed the same and added back an amount of Rs.1,36,67,817/- to the income of the assessee.

16. The learned Counsel for the assessee submitted, while deciding identical issue in assessee's own case for Assessment Year 2003-04, the Tribunal has directed the Assessing Officer to examine the issue keeping in mind that adjustment must be made to opening stock, purchases, sales and closing

stock. She submitted, while carrying out the directions of the Tribunal, the Assessing Officer has deleted such addition in Assessment Year 2003-04 and in subsequent assessment years up to Assessment Year 2009-10. She also drew our attention to the relevant assessment orders. Further, in support of her contention, she relied upon the decision of Hon'ble Bombay High Court in case of CIT vs Diamond Dyechem Ltd 396 ITR 536 (Bom).

17. The learned Departmental Representative relied upon the observations of the departmental authorities. However, he submitted that the issue may be restored back to the Assessing Officer.

18. We have considered rival submissions and perused the materials on record. It is a fact that while deciding identical issue in assessee's own case for Assessment Year 2003-04, the Tribunal in the order referred to above, has restored the issue to the Assessing Officer for fresh examination keeping in view that the adjustment, if any, has to be made to opening stock, purchases, sales and closing stock. We have also noted that while giving effect to the order of the Tribunal, the Assessing Officer has deleted the adjustment made under section 145A of the Act. In view of the above, we restore the issue back to the Assessing Officer for fresh examination keeping in view the directions of the Tribunal in Assessment Year 2003-04 that adjustment, if any, must be made to opening stock, purchases, sales and closing stock. This ground is allowed for statistical purpose.

19. In ground no. 2.5, the assessee has challenged disallowance of club expenditure amounting to R.4,4,383/- by holding it to be of capital nature.

20. We have considered rival submissions and perused materials on record. We have noticed that while deciding identical issue in assessee's own case for Assessment Year 2007-08 vide ITA No.8201/Mum/2011 dated 02-08-2013, the Tribunal has allowed the claim of the assessee. Facts being identical, respectfully following the aforesaid decision of the Tribunal, we delete the disallowance made by the Assessing Officer. This ground is allowed.

21. In ground no. 2.6 the assessee has challenged the disallowance of Rs.13,50,000/- u/s 43B(f). Briefly stated, in course of assessment proceedings, the Assessing Officer noticed that the assessee has claimed deduction of Rs.13,50,000/- towards amount provided for leave salary payable to employees on retirement. Since the aforesaid expenditure was claimed on accrual basis and was not actually paid during the year, the Assessing Officer disallowed the same under section 43B(f) of the Act. Learned Commissioner (Appeals) also upheld the disallowance.

22. At the time of hearing before us, the learned Counsel for the assessee fairly accepted that the issue has to be decided against the assessee in view of the recent judgment of the Hon'ble Supreme Court.

23. Having considered rival submissions, we find that in case of UOI Vs. Excide Industries Ltd, the Hon'ble Supreme Court in judgment dated 24-04-2020 delivered in Civil Appeal No.3545 of 2009, while reversing the judgment of the Hon'ble Calcutta High Court, has held hat this type of expenditure has to be disallowed under section 43B(f) of the Act if they were not actually paid during the year. Following the decision of the Hon'ble Supreme Court noted above, we dismiss the ground of the assessee.

24. Grounds 2.7 to 2.9 are consequential in nature, hence, dismissed.

25. Grounds 3 & 4 are general in nature; hence dismissed.

26. In the result, appeal is partly allowed.

Order pronounced in the Open Court on this 04/02/2021.

Sd/-	sd/-
(PRAMOD KUMAR)	**(SAKTIJIT DEY)**
VICE PRESIDENT	**JUDICIAL MEMBER**

Mumbai, Dated : 04/ 02/2021.
Pavanan, Sr.P.S (on contract)

Copy of the order forwarded to :

1. The Appellant.
2. The Responent.
3. The CIT(A)
4. 4. The CIT
5. D.R., ITAT, Mumbai.
6. Guard File.

//True Copy//

By order

I.T.A.T., Mumbai.