

**IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH 'I-1', NEW DELHI**

Before Ms. Suchitra Kamble, Judicial Member

Dr. B. R. R. Kumar, Accountant Member

ITA No. 8119/Del/2018 : Asstt. Year: 2014-15

Humboldt Wedag India Pvt. Ltd., A-36, Mehtab House, Mohan Co- op Estate, Mathura Road, New Delhi-110044	Vs	ACIT, Circle-11(2), New Delhi-110002
(APPELLANTT)		(RESPONDENT)
PAN No. AAACH7474G		

ITA No. 475/Del/2021 : Asstt. Year: 2016-17

Humboldt Wedag India Pvt. Ltd., A-36, Mehtab House, Mohan Co- op Estate, Mathura Road, New Delhi-110044	Vs	DCIT, Circle-10(1), New Delhi-110002
(APPELLANTT)		(RESPONDENT)
PAN No. AAACH7474G		

**Assessee by : Sh. Ajit Kumar Jain, CA
Revenue by : Sh. Surenderpal, CIT DR**

Date of Hearing: 13.08.2021	Date of Pronouncement: 18.08.2021
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ORDER

Per Dr. B. R. R. Kumar, Accountant Member:

The present appeals have been filed by the assessee against the final assessment orders dated 31.10.2018 and 31.03.2021 for the AYs. 2014-15 and 2016-17 passed by the AO u/s 143(3) r.w.s. 144C of the Income Tax Act, 1961.

Markup on Services availed: (A.Y. 2014-15 & 2016-17)

2. Humboldt Wedag India Private Limited ('Appellant' or 'the Company' or 'HW India'), incorporated in 1976, is a wholly owned subsidiary of KHD Humboldt Wedag International AG Cologne ('KHD AG'). KHD AG, through its subsidiaries is engaged in the business of process technology design, engineering, project management, the supply of technology and equipment, as well as supervising the erection and commissioning of cement plants and related equipment. It also provides customer services such as, supplying spare parts, optimization of cement plants, and training plant personnel round out KHD's service portfolio. HW India is engaged in providing services such as designing and engineering, project management, supply of technology and equipment, and supervision of erection and commissioning of cement plants and related equipment.

3. During AY 2014-15, the Appellant has undertaken various international transactions with its associated enterprises ('AEs'). For the purpose of benchmarking the prices of the international transactions, the Appellant in its transfer pricing documentation, has followed the transaction-by-transaction approach.

4. The assessee paid Rs.8.28 lacs for supervising charges, and Rs.14.25 Crores for central services. On supervision services, the AE charged a net profit markup of 4% on the internal cost incurred on the basis of number of hours spent by its personal in providing such services. On the central services,

the AE charged 5% profit markup on internal cost while third party costs are charged on cost to cost basis.

5. The markup of 4% and 5% has been disallowed by the TPO and accordingly enhanced the income of the assessee based on the Id. DRP observations for the year 2010-11. For the sake of ready reference, the same is reproduced as under:

"3.3.2. In the assessee's case, the intra- group services relate to general administration, finance and accounting, coordination, general management, corporate and project financing, recruitment and education. It is noted that the assessee is an entrepreneur in its own right and is engaged in engineering, procurement and commissioning projects for the third party clients. It procured orders on independent basis and also carried out the project on its own. It is hardly operating as an extension of AE or catering exclusively to the AE. It virtually undertakes all the risks associated with rendering services, marketing and performs various complex roles. Therefore, the ratio of Supreme Court decision in the case of Morgan and Stanley & Co. hardly applies on the facts of the assessee's case. The assessee has also provided substantial evidence in form of e-mails and correspondence with the AE in respect of the services rendered by the AE. On going through the same, it clearly comes out that the AE was rendering services which were beneficial for the assessee in conducting its business. No doubt, some benefit of the services may have accrued to overall group also. But the primary beneficiary was definitely the assessee. Under these circumstances, it would not be proper to term the services rendered by the AE as stewardship activity.

3.3.3. Corning to the quantum of payment for the services, it is seen that from the total cost of services, cost of stewardship activity services/duplicate services is first removed. The remaining cost is allocated to different organizations of the group. The assessee pays the cost of services allocated to it plus ore-agreed mark up. In the course of hearing, the assessee was asked to justify the mark up. However, no detailed justification was provided in this regard. It was only stated that since the AE was providing the services, it was entitled to earn some margin on the same. However, as discussed earlier, while the primary beneficiary of the services is the assessed, there are also some incidental benefits accruing to the group. The parent company gets benefited by better synergies, scale of economy, better coordination and reporting. Considering this, the AE, in our opinion, was not justified in charging any mark up on the cost of services. The arm's length price of the services is therefore decided at the actual cost. The adjustment is therefore sustained to the extent of mark up only. The TPO is directed to reduce the adjustment accordingly."

6. The main argument of the Id. AR was that these transactions are benchmarked by using TNMM and furnished that TP documentation whereas the TPO did not follow any prescribed method and the entire markup is disallowed without giving any reasons. The observation of the revenue that the parent company gets benefited by better synergies, scale of economy, better coordination and reporting cannot be accepted.

7. While the assessee avails supervision services from its AEs and pays markup charges, it also provides such services to the AEs for their third party contracts and receives markup charges. The pricing basis and the results arising from the same have been accepted by the TPO. Disallowing the mark-up on receipt of services while in-principle accepting the provision of similar services rendered having similar intent and basis of pricing cannot be valid ground to disallow the markup. It is not out of contest to note that no such disallowance has been made on the markup in the case of the assessee AY 2007-08 to 2012-13 and AY 2015-16.

8. Hence, keeping in view, the entire facts and circumstances, the contention of the revenue that the AE invariably derives some benefit and hence no markup should be charged, cannot be accepted.

Provision for warranty:(A.Y. 2014-15 & 2016-17)

9. The assessee contended that the issue of warranty is a recurring provision made in the past several years and that in all the year from 2009-10 onwards by the various judicial authorities.

10. The Id. DRP for both the years in question directed the AO to modify the disallowance after verifying the provisions made in the earlier years, its actual utilization and writing back of unutilized provision for taxation. The AO was further directed to examine and verify complete details of the data of the provisions created, and actual expenses on the warranty incurred in the subsequent years.

11. Heard the arguments of both the parties and perused the material available on record.

12. The details submitted by the assessee are perused.

13. The agreements pertaining to the warranty clause on completion of the projects have been examined. The Article 9 pertaining to the warranties specify that the equipment carry a warranty for a period of 12 months from completion of performance test or 18 months from the date of commissioning or 24 months from the date of last major delivery, whichever is earlier, against any material defect, design defect, manufacturing defect and/or failure of equipment to perform as stipulated. The spares shall carry a warranty period of 12 months from the date of their being put to use or maximum 24 months from the date of delivery whichever is earlier. The Performance Bank Guarantee submitted by the supplier will remain valid till the aforesaid warrantee period. Further, specific items as Gear Box for kith, girth gear, thrust rollers, will have latest defect liability period of 60 months from the date of delivery.

14. The provision for warranty has been made on a scientific and reasonable basis that the assessee makes a provision for warranty @3% of the contract value upon the completion of the deliveries based upon the historical trend. The following table provides a reconciliation of provisions for warranty for various years i.e. provision created in preceding years, actual expenditure during the year, earlier provision utilized, the balance provision carried forward.

AY	Opening balance	Additions	Reversal	Utilization	Closing balance	Contract revenue
2009-10	35,58,78,785	10,22,90,817	5,13,94,994	25,54,00,584	15,13,74,024	3,92,60,86,075
2010-11	15,13,74,024	28,81,12,854	4,50,43,319	9,11,22,433	30,33,21,126	3,55,32,53,339
2011-12	30,33,21,126	18,76,87,197	3,24,89,702	9,49,25,941	36,35,92,680	4,60,22,79,741
2012-13	36,35,92,680	23,89,75,515	6,28,00,944	24,32,96,504	29,64,70,747	3,39,46,41,837
2013-14	29,64,70,747	41,88,64,157	2,02,09,842	20,55,67,885	48,95,57,177	2,57,40,20,904
2014-15	48,95,57,177	5,02,88,810	2,68,65,259	5,68,84,319	45,60,96,407	3,99,17,38,396
2015-16	45,60,96,407	13,99,70,672	15,15,91,912	18,70,47,392	25,74,27,775	2,37,98,26,136

15. Further, we also find that the Co-ordinate Bench of ITAT vide order dated October 31, 2017 for AY 2008-09, has dismissed the Revenue's appeal filed against the order of Id. CIT(A) allowing the deduction for provision for warranty. The relevant extract from the order is as follows:

"14. So far as the issue relating to disallowance of 'provision for warranty', it is an admitted fact that under the terms of agreement, assessee has provided warranty for the period ranging from 12 to 36 months to which assessee is contractually obliged to pay warranty on its own case in case of any breach in supply and services, in case if there is any demand from the purchaser. The terms of agreement clearly provides that assessee has to take effective steps; for rejection or modify or replace or remove the defect or deficiency or in case of damage of equipment; assessee shall do the needful and for this purpose it has been making provision for making such guarantee. The Id. CIT(A) has also taken note of the actual expenses incurred on warranty by the assessee in earlier years and also calculated the percentage of such expenditure (as noted by us herein above). If based on such actual expenditure incurred on warranty, assessee has made the provision for warranty, then ostensibly it can be held that, not only assessee

has made the provision as per past experience but there was a certain degree of certainty while making such estimate.

The ratio laid down by the Hon 'ble Apex Court in the case of Rotork Controls India (P) Ltd Vs. CIT (supra) is squarely applicable...

15. The observations and finding of the Id. CIT(A) is not only in accordance with the facts and material on record, but also in conformity with the principle laid down by the Hon'ble Supreme Court, hence there is no reason to deviate from such a finding and accordingly same is confirmed."

16. The Co-ordinate Bench of ITAT vide combined order dated June 11, 2018 for AY 2010-11 & AY 2011-12, has dismissed the Revenue's appeal filed against the directions of Id. DRP allowing the deduction of provision for warranty, following their order for AY 2008-09. The relevant extract from the order is as follows:

For AY 2010-11

"12.2 Ground No. 3 challenges the direction of the Ld. DRP in allowing the provision for warranty amounting to Rs. 288,112,854/-. We find that the Ld. DRP had held the issue in a similar issue had arisen in AY 2008-09 wherein the Ld. CIT (A) had deleted the disallowance. The Ld. DRP has noted that the facts were identical in AY 2008-09 and the year under consideration and, therefore, the disallowance was to be deleted. ... The Department has not been able to bring out any distinguishing factor with respect to the facts in the proceedings

before us. In the circumstances, we find no reason to interfere and dismiss ground no. 3."

For AY 2011-12

"13.3 Ground No. 4 challenges the direction of the Ld. DRP in deleting the disallowance pertaining to provision of warranty amounting to Rs. 187,687,197/-. We find that a similar issue had come up in Assessment Years 2008-09 and 2010-11 and the department's ground challenging the deletion had been dismissed by the ITAT in ITA Nos. 2295/Del/2013 and 567/Kol/2015 respectively. The Department has not been able to bring out any distinguishing factor with respect to the facts in the proceedings before us. In the circumstances, we find no reason to interfere and dismiss ground no. 4."

17. The Co-ordinate Bench of ITAT vide combined order dated April 7, 2021 for AY2012-13 and AY 2013-14, has dismissed the Revenue's appeal filed against the order of Id. CIT(A) allowing the deduction of provision for warranty, following their order for AY 2008-09. The relevant extract from the order is as follows:

"13. Since, the matter stands adjudicated and allowed for several years prior, in the absence of any material change, we hereby hold that the addition made by the AO cannot be sustained."

18. Since, the provision for warranties has been made @ 3% and the unutilized portion has been reversed at a regular intervals from year to year, the appellant has been consistently following the policy of making provision for warranty as per the

terms of the contract, the ITAT for AY 2008-09, AY 2010-11, AY 2011-12, AY 2012-13 & AY 2013-14 has allowed provision for warranty, the provision made during AY 2014-15 is on same basis as in earlier years is hereby allowed.

Provision for anticipated losses: :(A.Y. 2016-17)

19. The anticipated loss claimed by the assessee with regard to Shri Cements Ltd. has been disallowed by the AO. The Id. DRP held that the details furnished by the assessee in this regard do not contradict the view taken by the AO.

Liquidated Damages :(A.Y. 2014-15)

20. The assessee is engaged in the business of industrial plant engineering and supply of equipment for cement and mineral plants, entered into various contracts with customers for supplies and engineering services ranging from 2 to 4 years. The contracts contain clause for payment of liquidated damages for default of delivery as per the agreed terms entered in the contract agreements. The Id. DRP directed the AO to verify the provisions made in the earlier years, actual utilization and writing back of unutilized provision to taxation.

21. The table below provides a reconciliation of provision for Liquidated Damages made/ reversal of Provision and utilization for Liquidated Damages for various years:

AY	Opening balance	Additions	Reversal	Utilization	Closing balance
2009-10	20,06,94,749	16,80,30,693	10,25,75,683	10,55,822	26,50,93,937
2010-11	26,50,93,937	3,18,02,972	2,45,24,252	12,63,45,462	14,60,27,195
2011-12	14,60,27,195	10,97,86,518	4,85,62,347	2,31,36,169	18,41,15,197
2012-13	18,41,15,197	17,76,31,240	3,31,22,000	10,31,162	32,75,93,275
2013-14	32,75,93,275	8,83,02,186	29,54,62,259	26,47,557	11,77,86,274
2014-15	11,77,86,274	11,78,25,376	3,04,70,046	-	20,51,41,604
2015-16	20,51,41,604	3,95,29,500	8,51,40,846	2,18,11,696	13,77,18,562

22. We also find that the issue has been adjudicated in the case of the assessee in the appeals filed by the revenue for the assessment years 2008-09, 2010-11, 2011-12, 2012-13, 2013-14.

23. For the sake of ready reference, the operative part of the earlier order is reproduced below:

"13 ... The Id. CIT(A) has categorically noted that assessee has provided for liquidated damages based on the period of delay which occurred during the end of the year and on the basis of percentage of the contract the value payable as damages in terms of the agreement. Apart from that, assessee has also reversed the provision for liquidated damages in the year in which clients waived the said liquidated damages and the write back amount has been offered to tax by the assessee. Whence a provision is arising out of a contractual obligation and the basis of providing the provision is based on past experience and such a reasonable basis of estimation has been regularly followed by the assessee in the past, then ostensibly it cannot be held that the basis of estimation or working of the provision is not correct. Further, once it is brought on record that assessee on

the year of reversal has paid taxes on excess provision and similar feature appeared in the earlier years and assessee had payments for liquidated damages on delay in delay of deliverables, then no adverse view can be taken, because it is not the charge of the Assessing Officer that assessee has made some kind of excessive provision in this year in relation to past. The finding and observations of the Id. CIT(A), are based on correct appreciation of facts and law, hence we confirm the order of CIT(A) on this score and accordingly, ground No. 1 by the Revenue is dismissed.”

24. Since, the provision for liquidated damages has been made regularly and allowed in P&L account and since the unutilized portion has been reversed at a regular intervals from year to year, since, the ITAT for AY 2008-09, AY 2010-11, AY 2011-12, AY 2012-13 & AY 2013-14 has allowed provision for liquidated damages, the provision made during AY 2014-15 is on same basis as in earlier years is hereby allowed.

Provision for Anticipated Losses: (AY 2016-17)

25. The assessee has claiming provision for anticipated losses on the grounds that Accounting Standard 7 on construction contracts allows such provision. He relied on the judgments in the case of Mazagaon Dock Ltd. Vs. JCIT 29 SOT 356, Dredging International Vs ACIT 48 SOT 430 wherein the loss on estimated basis determined on technical estimation has been allowed.

26. The Id. DRP held that this liability has not been crystallized during the relevant period and disallowed the loss owing to the

absence of cogent evidences to prove that the liability has been taken shape.

27. Before us, the assessee reiterated the arguments taken up before the authorities below while the Id. AR relied on the order of the Id. DRP.

28. Heard and perused the material available on record.

29. What is the profit of a trade or business is a question of fact and it must be ascertained, as all facts must be ascertained, with reference to the relevant evidence, and not on doctrine or theories. At first sight, it might be thought that the calculation of variables such as revenue, expenditure and profits should be the same for the purposes of both commercial accounting and taxation but not so. The fundamental point, of course, is that accounting and taxation exist for different reasons. The purposes and requirements of commercial accounting principles and taxation are not always the same.

30. Accounting involves the preparation of information for the purposes of control and decision-making and may require interpretation, forecasting or simply recording factual information.

31. The main purpose of taxation is usually to raise revenue but it is also used as an instrument of government economic and social policy. For a tax system to operate successfully within the law it requires a degree of certainty that may not always be appropriate for commercial accounting. Furthermore there alternative methods of preparing accounts that are

equally acceptable in terms of accounting standards but the choice of which is not accepted for the taxation purpose. There are several reasons why financial reporting rules and practices might not always be appropriate for determining final tax liability. The primary goal of financial accounting is to provide useful information to management, shareholders, creditors, and others properly interested; the major responsibility of the accountant is to protect these parties from being misled. The primary goal of the income tax system, in contrast, is the equitable collection of revenue, the major responsibility of the state is to protect the public finance. Hence, any presumptive equivalency between tax and financial accounting would be unacceptable.

32. Furthermore, there are other reasons why taxation might deviate from accounting concepts of income. While the most obvious purpose of taxation is to finance public expenditure, the extent and magnitude of taxation in modern economies also makes it a powerful instrument of government economic and social policy in its own right. While it is true that some taxation measures might be introduced to improve economic decision making, others are implemented for very different reasons. The concept of tax expenditures ably describes the situation that those provisions of the income tax containing special exemptions, deductions and other tax benefits were really methods of providing benefits by deviating from the system of profits derived following accounting standards. Thus, we find that wherever exemption or deductions are called for, the same has been provided explicitly in the provision of the Income Tax Act. Even, the provision for warranty, liquidated damages have

been allowed taking into consideration the matching principle of revenue accounting. In the instant case, we further find that no cogent evidences have been furnished by the assessee as to how this loss has been arrived at.

33. Hence, we decline to interfere with the decision of the Id. DRP on this issue.

Charging of interest u/s 234A: (AY 2014-15)

34. We hereby direct the AO to verify the date of filing of return by the assessee with regard to the timeline extended for the instant year and charge interest accordingly.

35. In the result, the appeal of the assessee in ITA No.8119/Del/2018 is allowed and the appeal in ITA No.475/Del/2021 is partly allowed.

Order Pronounced in the Open Court on 18/08/2021.

Sd/-

(Suchitra Kamble)
Judicial Member

Dated: 18/08/2021

Subodh Kumar, Sr. PS

Copy forwarded to:

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

Sd/-

(Dr. B. R. R. Kumar)
Accountant Member

ASSISTANT REGISTRAR