

IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCHES "A" BENCH: BANGALORE

BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER AND
SHRI GEORGE GEORGE K, JUDICIAL MEMBER

IT(TP)A. No. 182/Bang/2017
Assessment Year: 2012-13

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| M/s. AMC Cookware (India) Pvt. Ltd., #1180, 12 th B Main, 1 st Cross, HAL 2 nd Stage, Indira Nagar, Bangalore-560008. PAN: AACCA4970G | vs. | The Deputy Commissioner of Income Tax, Circle 1 (1) (2), Bangalore. |
| (Appellant) | | (Respondent) |

| | | |
|-------------|---|----------------------------------|
| Assessee by | : | Shri K.P. Srinivas, CA |
| Revenue by | : | Shri Deva Rathna Kumar, CIT (DR) |

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|-------------------------|------------|
| Date of Hearing : | 08.11.2021 |
| Date of Pronouncement : | 29.11.2021 |

ORDER

PER SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER

This appeal by assessee is directed against the order of DCIT, Circle-1(1)(2), Bangalore dated 28.11.2016.

2. The assessee raised the following grounds.

"1. The learned AO and TPO erred in determining and the Hon'ble DRP erred by not adjudicating on the submissions made that the adjustment to the arm's length price, if at all, has to be restricted to the transactions with associated enterprises, which constitutes less than 20% of the total operating cost of your appellant, and not with reference to the total cost incurred where the concerned parties are unrelated ones.

2. The learned AO and TPO erred in rejecting and the Hon'ble DRP erred in upholding the rejection of the 'Resale Price Method'

adopted by your appellant and instead adopted Transactional Net Margin Method as the most appropriate method to determine the arm's length price of the international transactions with its associated enterprises;

3. The learned AO and TPO erred by considering and the Hon'ble DRP erred in upholding that the foreign exchange loss of Rs. 64.08 lakhs is an operating expenditure to arrive at the operating margins of your appellant, although it was predominantly due to borrowing in foreign currency.

4. For these and other grounds that may be adduced at the time of hearing, the order of the learned Deputy Commissioner of Income Tax, Circle 1(1)(2), Bangalore, may be set aside to the extent appealed against and this appeal be allowed.”

3. The assessee has also raised the following additional grounds.

“5. Without prejudice to the other grounds, if the Hon'ble Tribunal upholds the adoption of the 'Transactional Net Margin Method' as the 'most appropriate method' to determine the arm's length price of the international transactions entered into by your appellant with its Associated Enterprises, then your appellant prays that the Hon'ble Tribunal directs the learned AO / TPO / DRP to exclude Kanchan International Ltd., Panasonic Home Appliances India Co. Ltd., Hawkins Cookers Limited, Bajaj Electricals Ltd. and TTK Prestige Ltd. as comparable companies to your appellant's business as all the above companies have a different business model of selling products through a chain of wholesalers and retailers as against the 'direct selling model' of your appellant, and retain Eureka Forbes Ltd. as the lone comparable.

6. Without prejudice to Ground 5, if the Hon'ble Tribunal upholds Kanchan International Ltd., Panasonic Home Appliances India Co. Ltd., Hawkins Cookers Limited, Bajaj Electricals Ltd. and TTK Prestige Ltd. as comparable companies, then your appellant prays that the Hon'ble Tribunal directs the learned AO/TPO/DRP to adjust the operating margin of your appellant by excluding the expenditure it incurred under the 'direct selling model' which the above companies do not incur under the model of selling products through a chain of wholesalers and retailers.”

4. The assessee has also filed petition for above additional grounds Sl.No. 5 & 6 and placed reliance on the judgment of Hon'ble Supreme Court in the case of NTPC Vs. CIT as reported in 229 ITR 383 and submitted that all the facts already brought on record and there is no question of any fresh

facts so as to decide the issue and additional grounds may be admitted. We have heard the parties on the admission of additional grounds. As rightly pointed out by the Ld.DR, there is no necessity for investigation of any fresh facts to decide the issue in ground nos. 5 & 6 and accordingly, these grounds are admitted for adjudication.

5. Now the facts of the case are that the appellant is a private limited company incorporated under the provisions of The Companies Act, 1956, in the state of Karnataka. It is a pioneer in India in healthy & nutritious cooking and is engaged in the business of assembling and direct selling of multi-cooking systems to end consumers. The appellant filed its return of income for the assessment year ['AY'] 2012-13 on 29th November 2012 declaring 'Nil' income after claiming set off of brought forward losses of earlier years.
6. The case was selected for scrutiny and was subsequently referred to the learned Deputy Commissioner of Income Tax, Transfer Pricing, Circle 1(1)(1), Bangalore ['the TPO'] by the learned Assessing Officer ['the AO']. The learned TPO, vide his order under section 92CA of the Income Tax Act, 1961 ['the Act'], dated 29th January 2016, proposed an addition of Rs.3,81,06,010/- on account of transfer pricing adjustments. Aggrieved, the appellant filed its objections before the Hon'ble Dispute Resolution Panel, Bangalore ['the DRP']. Concurrently, the learned TPO initiated rectification proceedings and vide order u/s 92CA(5) r.w.s 154 of the Act, dated 29th August 2016, determined the transfer pricing adjustment at Rs. 4,17,29,931/- as against the original transfer pricing adjustment of Rs. 3,81,06,010/-.

7. The Hon'ble DRP sustained the additions made and granted no relief to the appellant. Accordingly, the present appeal is preferred against the final assessment order passed by the AO u/s 143(3) r.w.s 144C(13) of the Act, dated 28th November 2016, consequent to the directions of the Hon'ble DRP and determining the total income at Rs. 3,35,01,083/- after setting off losses of earlier years.

8. First ground for our consideration is as follows.

Ground No. 1

8.1 Without prejudice to Grounds 2 and 3, it is submitted that the learned AO and TPO erred in determining and the Hon'ble DRP erred in sustaining the adjustment to the Arm's Length Price ['ALP] without restricting the same to transactions with Associated Enterprises [AEs], which constitutes merely around 20% of the total operating cost of the appellant.

8.2 During AY 2012-13, the total expenses incurred towards transactions with AEs comprised of the following [refer Annexure 'A', page no. 30 of the Paper Book]:

- a. Cost of import of Raw Materials and finished goods Rs. 12,56,08,134/- [of which import of raw materials was Rs. 10,40,40,358/- and finished goods and accessories was Rs. 2,15,67,776/-]; and
- b. Interest of Rs. 1,44,161 on ECB loan.

8.3 Accordingly, the total expenditure incurred towards AE transactions during AY 2012-13 was Rs. 1,257.52 lakhs [i.e., 1,256.08 lakhs plus 1.44 lakhs]. The total expenditure incurred by the appellant during AY 2012-13 is Rs. 6,293.08 lakhs, which includes major expenses like employee cost of Rs. 996.73 lakhs, sales commission of Rs. 1,071.08 lakhs, rent of Rs. 436.02 lakhs, discounts and

incentives of Rs. 345.02 lakhs as well as various other administrative expenses incurred locally with unrelated parties. Since provision for doubtful debts of Rs. 110.06 lakhs is non-operating in nature, the total operating cost of the appellant would be Rs. 6,183.02 lakhs [i.e., Rs. 6,293.08 lakhs less Rs. 110.06 lakhs].

8.4 Thus, it can be seen that the transactions of Rs. 1,257.52 lakhs with AEs constitute merely 20.34% of the total operating cost of Rs. 6,183.02 lakhs incurred by the appellant. This is without adjusting for increase of Rs. 37.36 lakhs in closing stock. If the same is also adjusted, the rate would fall to 19.73%. Further the comparisons are made at the operating profit level which excludes interest of Rs. 1.44 lakhs. If adjustment is made for this, the net amount would be Rs. 1218.72 lakhs only [i.e., Rs. 1,257.52 lakhs less Rs. 37.36 lakhs less Rs. 1.44 lakhs], as against Rs.1257.52 lakhs adopted by the TPO. Accordingly, if the transfer pricing adjustment is restricted solely to transactions with AEs, the same would be Rs. 82.19 lakhs only [refer below working] as against the adjustment of Rs. 417.29 lakhs done by the AO / TPO in the final assessment order. This is without prejudice to ground 2 raised by the appellant that no transfer pricing adjustment is called for in the instant case.

| Particulars | Rs. in Lakhs |
|--|-----------------|
| Operating Revenue as per TPO vide order Lils 92CA(5) r.w.s 154, dated 29th August 2016 | 6,142.24 |
| ALP Margin on Cost as per TPO's order dated 29 th August 2016 | 6.125% |
| ALP as a Percentage of Operating Revenue | 93.875 |
| Arm's Length Price [6,142.24 * 93.875%] [A] | 5,766.03 |
| Operating Cost of the Appellant [as per para 5 above and as considered by the TPO] [B] | 6,183.02 |
| Variation between Operating Cost and ALP [C = A - B] | 416.99 |
| 5% of Operating Cost [6,183.02 * 5%] | 309.15 |

| | |
|---|----------|
| Quantum of International Transactions included in operating cost | 1,218.72 |
| Percentage of International Transactions vis-à-vis Operating Cost | 19.71% |
| TP Adjustment [if Restricted to quantum of International Transactions] [C* D] | 82.19 |

8.5 Hence, it is prima facie erroneous to make a transfer pricing adjustment with reference to the total cost incurred by the appellant, which includes considerable expenses with non-AEs and also substantial amount of duties and taxes. By doing so, the learned TPO has grievously erred by making a transfer pricing adjustment for non-AE expenses also, which is against all principles of natural justice. If the TP adjustment of Rs. 417.29 lakhs is upheld, it would mean that the cost of goods imported, which was duly approved by the Customs Department, should have been Rs. 838.79 lakhs only as against Rs. 1,256.08 lakhs on which Customs Duty as well as Countervailing Duty was paid, implying a mark down of one-third of the value. This explicitly shows that the TP addition was made / sustained without considering the facts of the case.

(a) Attention is drawn to the judgement of the Hon'ble Mumbai High Court in the case of CIT vs. Thyssen Krupp Industries India Pvt. Ltd. 12016/ 70 taxmann.com 329 (Bombay), wherein the Hon'ble High Court observed as under:

“..... We find that in terms of Chapter X of the Act, re-determination of the consideration is to be done only with regard to income arising from International Transactions on determination of ALP. The adjustment which is mandated is only in respect of International Transaction and not transactions entered into by assessee with independent unrelated third parties. This is particularly so as there is no issue of avoidance of tax requiring adjustment in the valuation in respect of transactions entered into with independent third

parties. The adjustment as proposed by the Revenue if allowed would result in increasing the profit in respect of transactions entered into with non-AE. This adjustment is beyond the scope and ambit of Chapter X of the Act."

(b) Similar views have been expressed by the Hon'ble Bangalore Tribunal in the case of Kirloskar Toyoda Textile Machinery (P.) Ltd. vs. ACIT [20151 53 taxmann.com 389 (Bangalore - Trib.).

8.6 Likewise, the Hon'ble jurisdictional Tribunal, Bangalore Bench, in the case of Genisys Integrating Systems (India) Pvt. Ltd. vs. DCIT [2012] 20 taxmann.com 715 (Bang — Trib.) and several other judgements have also explicitly held that while determining the ALP, transfer pricing adjustments should be restricted to only international transactions between associated enterprises, and observed as under

".....Chapter-X of IT Act relates to special provisions relating to avoidance of tax and sec. 92 therein relates to computation of income from international transactions having regard to ALP. Thus, it can be seen that only international transactions between the associated enterprises either or both of whom are non-resident are to be computed having regard to ALP. This issue is also covered by the decisions relied upon by the learned counsel for the assessee. Accordingly, the AO is directed to make the transfer pricing adjustments by restricting the adjustments to the transactions of the AE only by adopting the operating revenue and operating costs of these transactions only."

8.7 Similar views have been expressed by:

a. The Hon'ble Mumbai High Court in the case of CIT vs. Hindustan Unilever Ltd. 120161 72 taxmann.com 325 (Bombay) [refer Annexure 'N', para 3, pages 187 and 188 of the Paper Book];

- b. The Hon'ble Tribunal, Hyderabad Bench, in the case of Alumeco India Extrusion Ltd. vs. ACIT [2013] 38 taxmann.com 371 (Hyderabad — Trib.) [refer Annexure '0', para 12, pages 194 and 195 of the Paper Book]; and
- c. The Hon'ble Tribunal, Delhi Bench, in the case of Cornell Overseas Pvt. Ltd. vs. DCIT [refer Annexure 'P', para 13, page 204 of the Paper Book].

8.8 Various other judicial precedents exist to substantiate the claim of the appellant that the transfer pricing adjustment, if any, ought to be restricted to transactions with AEs alone.

8.9 Without prejudice to the above submissions, it is submitted that all the imports made by the appellant have already been subjected to audit by the Special Valuation Bench of the Customs Department, which is another arm of the Ministry of Finance. The Special Valuation Bench vide its orders dated 9th May 2008 and 17th January 2013 have accepted that the import prices are at arm's length [refer Annexure J, page no's 136 to 154 of the Paper Book]. Thus, it does not hold good to make any further adjustment to the ALP in the case of imports of the appellant which is not in line with the order of the Commissioner / Additional Commissioner of Customs. Any such adjustment would tantamount to contradicting the valuation done by the Customs Department, which in itself is an arm of the Ministry of Finance. The adjustment of Rs. 417.29 lakhs made by the TPO works out to 33.22% of the total import value of Rs. 1,256.08 lakhs from AEs. There cannot be such wide variation between the ALP as approved by the Customs Department and that determined by the Income Tax Department. For this reason alone it can be seen that the approach adopted by the learned TPO is fundamentally erroneous.

9. This ground was raised first time before the Tribunal and DRP had no occasion to examine this issue and hence this issue remitted to the file of DRP to decide in accordance with law.

10. Ground no. 2 is with regard to applying the TNMM method instead of Resale Price Method. The Ld.AR submitted that

10.1 The appellant imports finished and semi-finished products of high quality stainless steel cookware and accessories from AMC International and re-sells the imported goods in the Indian market to end consumers under the direct selling model, after minimal value additions like assembling, polishing and fixing of handles. The said products are the products of the AMC Group and are not procured from any unrelated parties directly. The OECD guidelines explicitly state that an appropriate resale price margin is easiest to determine where the re-seller does not add substantially to the value of the product. Therefore, RPM ought to be considered as the most appropriate method for determining the ALP with respect to import of finished goods and sold using direct marketing channels of the appellant. It is pertinent to note that the predominant value addition in India is through marketing expenses and not through manufacturing expenses. In fact, the purchases from related parties form a minimal portion of its total costs, as explained in above paras. In respect of goods sold (net of adjustment for inventory) out of the goods assembled in India, the production cost including the cost of materials imported from AEs constitute only 21% of the selling price of manufactured goods and about 25% for all goods and services [refer Annexure 'E', page 86 of the Paper Book]. Rest of the expenditure is marketing and administrative costs. Selling expenses are substantial under the direct selling model as the sale is directly to the ultimate consumer and revenue is at MRP. All the expenses normally incurred separately by the manufacturer, wholesaler and retailer are incurred by one entity under the

direct marketing model, thereby increasing the marketing expenses. As marketing is the main activity, bulk of the administrative cost is also attributable to it as all senior executives focus on marketing.

10.2 Typical transactions where RPM could be adopted are distribution of goods involving little or no value addition, i.e., when the re-seller does not add substantial value to the products or services received from the related party to get it ready for sale. RPM is used to test transactions involving the distribution function, i.e., when the tested party purchases products or acquires services from a related party and re-sells the same to independent parties. In the instant case, finished goods imported amounted to Rs. 215.68 lakhs where there was no value addition. and raw materials imported amounted to Rs. 1,040.40 lakhs where there was minimal value addition, as against an aggregate operating revenue of Rs. 6,103.63 lakhs. Out of the imports, Rs. 37.36 lakhs worth of goods remained in stock.

10.3 RPM evaluates the arm's length nature of a controlled transaction by reference to the gross profit margin realised in a comparable uncontrolled transaction. RPM measures the value of functions performed and is ordinarily considered most appropriate in cases involving purchase and resale of tangible goods or services in which the buyer and the reseller does not add substantial value to the goods by physically altering them or by using marketing intangibles.

10.4 The OECD in its Transfer Pricing Guidelines on RPM has observed as under:

"An appropriate resale price margin is easiest to determine where the reseller does not add substantially to the value of the product. In contrast, it may be more difficult to use the resale price method to arrive at an arm's length price where, before resale, the goods are further processed or incorporated into a more complicated product so that their identity is lost or transformed (e.g.

where components are joined together in finished or semi-finished goods). Another example where the resale price margin requires particular care is where the reseller contributes substantially to the creation or maintenance of intangible property associated with the product (e.g. trademarks or trade names) which are owned by an associated enterprise. In such cases, the contribution of the goods originally transferred to the value of the final product cannot be easily evaluated.

10.5 A resale price margin is more accurate where it is realised within a short time of the reseller's purchase of the goods. The more time that elapses between the original purchase and resale the more likely it is that other factors — changes in the market, in rates of exchange, in costs, etc. -will need to be taken into account in any comparison."

10.6 RPM begins with the price at which a product that has been purchased from an associated enterprise is re-sold to an independent enterprise. This resale price is then reduced by an appropriate gross margin ['the resale price margin'] representing the amount out of which the reseller would seek to cover its selling and other operating expenses and, in the light of the functions performed, taking into account the assets used and the risks assumed, to make an appropriate profit.

10.7 TNMM, on the other hand, assesses the arm's length character of transfer prices in a controlled transaction by testing the profit results of one participant in the transaction. TNMM examines the net profit margin relative to an appropriate base [e.g. costs, sales, and assets] that a taxpayer realises from a controlled transaction, or transactions that are appropriate to aggregate.

10.8 Under TNMM, comparable transactions need to be only broadly similar. Significant product diversity and some functional diversity between the controlled and uncontrolled parties are acceptable. As per ICA1 guidelines, typical transactions where TNMM may be used are:

- a) Provision of services;
- b) Distribution of finished products where re-sale price methods cannot be adequately applied; and
- c) Transfer of semi-finished goods.

10.9 From the above, it is evident that TNMM can be applied to distribution of finished products only if resale price cannot be adequately applied.

In the case of the appellant, the resale of imported finished goods can easily be covered by RPM. Since RPM can be easily applied, the appellant did not consider TNMM as the most appropriate method to evaluate international transactions arising from import of materials and components for use in the manufacturing process for re-sale. TNMM is a modified cost plus method and ought not to be used wherever RPM can be applied. As it is possible to apply RPM in the instant case, it is the right method and ought not to have been rejected. There is no reason to adopt any method other than RPM.

10.10 Attention is drawn to the judgement of the Hon'ble Tribunal, Mumbai Bench, in the case of Mattel Toys (1) Pvt. Ltd. vs. DCIT ff20141 30 ITR (Trib.) 283 (ITAT Mum) wherein the Hon'ble Tribunal observed as under

“..... RPM is mostly applied in a situation in which the reseller purchases tangible property or obtains services from an AE and the reseller does not physically alter the tangible goods and services or use any intangible assets to add substantial value to the property or services, i.e. resale is made without any value addition having been made. Since the gross profit margin is the main criteria while evaluating the transactions in the RPM wherein price is identified at which property or services are resold and normal gross profit margin is derived at by the enterprise which is deducted from the resale price of such property or service in comparable uncontrolled transactions. The gross profit margin earned by the independent enterprise in comparable uncontrolled transactions is served as a guidance factor. This is also what happens in the case

of a distributor wherein the property and service are purchased from the A.E. and are resold to other independent entities, without any value additions. The gross profit margin earned in such transactions becomes the determination factor to see the gross compensation after the cost of sales. In the instant case, the assessee is a distributor of Mattel toys and gets the finished goods from its A.E. and resells the same to independent parties without any value addition. In such a situation, RPM can be the best method to evaluate the transactions whether they are at arm's length price."

10.11 Further, in respect of the applicability of TNMM, the Hon'ble ITAT also observed as under

"... If the arm's length price of any transaction can be determined by applying any of the direct methods like comparable uncontrolled price, resale price method, cost plus method then they should be given the preference and once these traditional methods have been rendered inapplicable then only transactional net margin method should be resorted to. On the facts of the assessee's case, in our opinion, the assessee being a distributor who is purchasing the goods from its A.E. and reselling them to independent parties/unrelated parties, resale price method would be the most appropriate method for determining the ALP of the transactions between the assessee and the A.E.

10.12 The facts in the instant case of the appellant are squarely applicable to the rationale as laid down by the Hon'ble Tribunal, Mumbai Bench in the case of Mattel Toys (supra). The appellant imports goods from its AEs and re-sells the same in the Indian market under the direct selling model after minimal value additions like assembling, polishing and fixing of handles. Accordingly, RPM ought to be considered as the most appropriate method to determine the ALP in the appellant's case at least for finished goods, if not for all the goods.

10.13 At this stage, it is also pertinent to note the findings of the Hon'ble jurisdictional Tribunal, Bangalore Bench, in the case of Aztec Software and Technology Services Ltd. vs. ACIT 120071 294 ITR (A. T) 32 ((ITATIBand), which made the following observations on RPM [refer Annexure `S', para 175 and 176, page no. 295 of the Paper Book]:

"..... The RPM is to be applied when a property purchased or services obtained from an associated enterprise is resold to an unrelated enterprise.

The RPM is based on the price at which a product that has been purchased from an associated enterprise is resold to an independent enterprise. The resale price is reduced by resale price margin for arriving at the ALP. The resale price of goods is reduced by the direct expenditure and the normal gross profit margin that would have been earned by an unrelated enterprise in a similar transaction. The price is further adjusted on account of accounting practices and other differences between the transactions. There may be an internal RPM or external RPM as in the case of a CUP. Benchmarking of the margins is critical in this process. RPM could be reasonable method to apply to transactions involving resale of tangible property or in cases where the services are resold without value addition. This method is particularly suitable in cases where goods are sold within a short period of purchases and influence of other factors is found to be minimal."

10.14 Similar observations with regard to the applicability of TNMM were made by the Hon'ble Tribunal, Pune Bench, in the case of ACIT vs. MSS India Pvt. Ltd 2009/ 32 SOT 132 (Pune - Trib.) which held as under

"..... In our considered view, the transaction profit methods should be applied only when standard or traditional methods are incapable of being properly applied on the facts of a case. While traditional methods seek to compute the

prices at which international transactions would normally be entered into by the associated enterprise, but for their interdependence and relationship, transactional profit methods seek to compute the profits that the tested party would normally earn on such transactions with unrelated parties. It is only axiomatic that the profits earned by an enterprise is dependent on several factors, and not only on the prices at which transactions have been entered into with the associated enterprises. The profit based results thus admit possibility of vitiation of results by a number of factors which are not relevant to the determination of prices at which international transactions are entered into by the associated enterprises. These methods, which are a step removed from the methods of computing the prices at which independent transactions would normally take place in respect of the product or service, must therefore be put to service when the traditional methods, which seek to compute prices in independent situations, fail or are incapable of being implemented, as there are large number of situations in which, for a variety of reasons, traditional methods are simply unworkable. The inputs necessary for applying the traditional methods are not always available and that is the reason that despite better results produced by these methods, these methods are not as much put to use. However, whenever necessary inputs for applying one of these methods are available and there is no dispute about comparability of those inputs, there is no good reason to resort to transactional profit methods. It would thus follow that in a situation in which the assessee has followed one of the standard methods of determining ALP, such a method cannot be discarded in preference over transactional profit methods unless the revenue authorities are able to demonstrate the fallacies in application of standard methods. In any event, any preference of one method over the other method must be justified by the Transfer Pricing Officer on the basis of cogent material and sound reasoning.

10.15 Since in the instant case of the appellant, as RPM could easily be adopted to determine the ALP, there was no reason to adopt TNMM as the most appropriate method. The Hon'ble ITAT, in para 28 of its order, also held that the test in selecting the most appropriate method of ALP determination does not have 'complexity of the method' as one of the factors.

10.16 Since the appellant is re-selling the goods to unrelated customers on a direct selling model, it has a substantial mark up of 74.42% on selling price over the direct cost of goods sold. It is to be noted that the amount paid to AEs is much lower as the landed cost of imported goods include Customs Duty, freight, handling charges etc. The substantial mark-up makes it amply clear that the import prices charged by the AEs are extremely fair and reasonable and ought to be held at arm's length. The computation of mark-up of 74.42% is as under:

| Particulars | Amount (Rs. in Lakhs) |
|---|-----------------------|
| Operating Revenue as considered by the TPO | 6,142.24 |
| Less: operating revenue towards recovery of expenses not considered below | (112.68) |
| Net Operating Revenues [A] | 6,029.56 |
| Less: Expenditure | |
| Purchase Costs | 291.78 |
| Cost of Goods Sold | 1,154.83 |
| Changes in Inventory | (37.36) |
| Wages | 49.51 |
| Consumption of Stores & Spare Parts | 48.58 |
| Power & Fuel | 35.01 |
| Total Direct Expenses [B] | 1,542.35 |
| Gross Profit [C = A-B] | 4,487.21 |
| Gross Profit Margin [C / A] | 74.42% |

10.17 It is reiterated that the appellant imports finished and semi-finished products from its AEs and re-sells the imported goods in India after doing

minimal value addition like assembling and polishing, fixing the handle etc to the semi-finished goods and re-selling the finished goods. Hence, RPM ought to be considered as the most appropriate method for determining the ALP. Thus, gross margins are to be analysed for determining the Profit Level Indicator rPLI1 and not net margins as done by the learned TPO using TNMM.

10.18 The net margins earned by the appellant is low due to heavy marketing expenses incurred in India for the direct selling model adopted by it without having adequate volumes to cover such costs. Lower volumes are primarily due to higher retail price of these products which caters to the higher end of the market where the market size in India is still relatively very small. As bulk of the costs are incurred in India and the counter parties are third parties, the arm's length margin is well established. As explained in para 5 and 6 of this submission, expenditure towards transactions with AE is merely 19.73% of the total operating cost of the appellant. Thus, it is erroneous to adopt a 'net margin analysis' which includes substantial expenses incurred with non-AEs, i.e. 80.27% of the total expenditure.

10.19 It is obvious that the locally contracted and incurred expenses with third parties and the weak market sector development in India resulting in inadequate volumes are the only reasons for the low net margins of the appellant. The transfer prices are very fair and are calculated at arm's length. Hence there is a compelling necessity to reject the TNMM as it does not have any relevance to the facts of the appellant who ought to have been compared with other direct selling parties and not to parties who market through distributors and retailers.

Without prejudice to the above submissions, we further submit as under:

(a) It is pertinent to note that all the imports made by the appellant have already been subjected to audit by the Special Valuation Bench of the Customs Department, which is another arm of the Ministry of Finance. The Special Valuation Bench vide its orders dated 911' May 2008 and 17111 January 2013

have accepted that the import prices are at arm's length [refer Annexure J, page no's 136 to 154 of the Paper Book]. Thus, it does not hold good to make any further adjustment to the ALP in the case of imports of the appellant which is not in line with the order of The Commissioner / Additional Commissioner of Customs. Any such adjustment would tantamount to contradicting the valuation done by the Customs Department, which in itself is an arm of the Ministry of Finance. The adjustment of Rs. 417.29 lakhs made by the TPO works out to 33.22% of the total import value of Rs. 1,256.08 lakhs from AEs. There cannot be such wide variation between the ALP as approved by the Customs Department and that determined by the Income Tax Department. For this reason alone it can be seen that the approach adopted by the learned TPO is fundamentally erroneous and requires to be quashed.

(b) At least in the case of finished goods imported and resold, RPM ought to have been applied, although it has to be applied to the entire import transactions with AEs as value addition is minimal and predominant expenses are towards marketing activities incurred with third parties.

11. The Ld.DR submitted that RPM can be applied only wherein there is minimal or Nil value addition to the Resale goods. In the case of assessee, there is significant value addition and hence RPM cannot be applied. Further it was submitted that TNMM method is more appropriate method since the data net margins is available in the public domain and also related as, OP on sale is considered at the profit level indicator. Therefore TNMM method is most appropriate method. We have heard both the parties.

12. The argument of the Ld.AR is that the assessee imports finished and semi-finished products of high quality stainless steel cookware and accessories

from AMC International and re-sells the imported goods in the Indian market to end consumers under the direct selling model, after minimal value additions like assembling, polishing and fixing of handles etc to the semi-finished goods and re-selling the finished goods. In case of goods, there is no value additions for that RSM method is most appropriate method and on the other hand in case of semi-finished goods, TNMM method could be applied. In our opinion, these facts has to be verified for which fresh TP study should be carried out at the end of the TPO. Accordingly, this issue is remitted to the file of TPO to conduct fresh TP study and if there is no value addition in respect of finished goods, RSM method should be applied. On the other hand, in case of semi-finished goods, TNMM should be applied if the assessee furnished the finance of these segments so as to apply. With these observation, the issue is remitted to the AO/TPO for fresh consideration.

12.1 Ground no. 3 not pressed and dismissed accordingly.

13. Ground no. 4 is general which does not require adjudication.

14. Ground no. 5 is additional ground.

“5. Without prejudice to the other grounds, if the Hon'ble Tribunal upholds the adoption of the 'Transactional Net Margin Method' as the 'most appropriate method' to determine the arm's length price of the international transactions entered into by your appellant with its Associated Enterprises, then your appellant prays that the Hon'ble Tribunal directs the learned AO / TPO / DRP to exclude Kanchan International Ltd., Panasonic Home Appliances India Co. Ltd., Hawkins Cookers Limited, Bajaj Electricals Ltd. and TTK Prestige Ltd. as comparable companies to your appellant's business as all the above companies have a different business model of selling products through a chain of wholesalers and retailers as against the 'direct selling model' of your appellant, and retain Eureka Forbes Ltd. as the lone comparable.”

15. The Ld.AR submitted that

Without prejudice to the above grounds, if the Hon'ble Tribunal upholds the adoption of the 'Transactional Net Margin Method' as the 'most appropriate method' to determine the arm's length price of the international transactions entered into by the appellant with its Associated Enterprises, then the appellant prays that the Hon'ble Tribunal directs the learned AO / TPO / DRP to exclude Kanchan International Ltd., Panasonic Home Appliances India Co. Ltd., Hawkins Cookers Limited, Bajaj Electricals Ltd. and TTK Prestige Ltd. as comparable companies to your appellant's business as all the above companies have a different business model of selling products through a chain of wholesalers and retailers as against the 'direct selling model' of the appellant, and retain Eureka Forbes Ltd. as the lone comparable.

The appellant submits that it selected Kanchan International Ltd., Panasonic Home Appliances India Co. Ltd., Hawkins Cookers Limited, Bajaj Electricals Ltd. and TTK Prestige Ltd. as comparable companies solely on the basis that 'Resale Price Method' is the 'most appropriate method' to determine the arms' length price of its international transactions. Since the learned TPO and the Hon'ble DRP has rejected RPM and instead adopted TNMM, the appellant is well within its right to consider the above companies as functionally different to the appellant's business on the basis of TNMM, as the appellant incurs substantial expenses on direct marketing and selling to the customer, while in the case of its comparable companies the same is incurred by their dealers and distributors.

16. We have heard both the parties and perused the record. Since the issue relating to the applicability of MAM to determine ALP of the international transactions is remitted to the AO/TPO, at this stage we refrain from adjudicating the issue related to selection of comparables and kept it open

at this stage and the assessee had liberty to raise this issue at the appropriate stage.

17. Ground no. 6

33. Without prejudice to Ground 5, if the Hon'ble Tribunal upholds Kanchan International Ltd., Panasonic Home Appliances India Co. Ltd., Hawkins Cookers Limited, Bajaj Electricals Ltd. and TTK Prestige Ltd. also as comparable companies, then the appellant prays that the Hon'ble Tribunal directs the learned AO / TPO / DRP to adjust the operating margin of the appellant by excluding the expenditure it incurred under the 'direct selling model' which the above companies do not incur under the model of selling products through a chain of wholesalers and retailers. Further, their turnover is already reduced by considering only the dealer prices at which they have sold their products to the dealers.

18. The Ld.DR relied on the lower authorities. We have heard both the parties and perused the record. As discussed in earlier para regarding selection of comparables in ground no. 5, this ground is also kept it open with a liberty to the assessee in appropriate stage.

19. In the result, the appeal filed by the assessee is partly allowed for statistical purposes.

Order pronounced in the open court on 29th November, 2021.

Sd/-
(GEORGE GEORGE K)
JUDICIAL MEMBER

Sd/-
(CHANDRA POOJARI)
ACCOUNTANT MEMBER

Dated: 29th November, 2021.
/MS/

Copy to

1. The Appellant
2. The Respondent
3. CIT(A)
4. Pr. CIT
5. DR, ITAT, Bangalore.
6. Guard File

By order

Assistant Registrar
Income-tax Appellate Tribunal
Bangalore