

**IN THE INCOME TAX APPELLATE TRIBUNAL
'B' BENCH : BANGALORE**

**BEFORE SHRI. B.R. BASKARAN, ACCOUNTANT MEMBER
AND
SMT. BEENA PILLAI, JUDICIAL MEMBER**

IT(TP)A No. 73/Bang/2019
Assessment Year : 2014-15

M/s. A.O. Smith India Water Products Pvt. Ltd. (formerly known as A.O. Smith India Water Heating Pvt. Ltd.), No. 300, Phase-II, KIADB Industrial Area, Harohalli, Kanakapura Taluk, Ramanagara District. – 562 112. PAN: AAFCA8954R	Vs.	The Income Tax Officer, Ward-1(1)(2), Bangalore.
APPELLANT		RESPONDENT

Assessee by	:	Shri K.R. Vasudevan, Advocate
Revenue by	:	Shri Mathivanan M, CIT (DR)

Date of Hearing	:	16-12-2021
Date of Pronouncement	:	23-12-2021

ORDER

PER BEENA PILLAI, JUDICIAL MEMBER

Present appeal has been filed by assessee against final assessment order passed by Ld. ITO, Ward-1 (1)(2), Bangalore dated 30.10.2018 u/s. 143(3) r.w.s. 144C of the Act for Assessment Year 2014-15 on following grounds of appeal.

“The grounds mentioned hereinafter are without prejudice to one another.

1. *The learned Assessing Officer ("learned AO"), learned Transfer Pricing Officer ("learned TPO") and the Honourable Dispute Resolution Panel ("Hon'ble DRP") grossly erred in determining an adjustment of INR 44,29,64,584/- with respect to the international transactions of the Appellant under section 92CA of the Income-tax Act, 1961 ("the Act").*
2. *The learned AO/ learned TPO/ Hon'ble DRP erred in rejecting the Transfer Pricing ("TP") documentation maintained by the Appellant by invoking provisions of sub-section (3) of section 92C of the Act.*
3. *The learned AO/ learned TPO/ Hon'ble DRP erred in rejecting Cost Plus Method ("CPM") applied in the TP documentation as the Most Appropriate Method ("MAM") with respect to the manufacturing activity of the Appellant.*
4. *The learned AO/ learned TPO/ Hon'ble DRP erred in not accepting Resale Price Method ("RPM") as the Most Appropriate Method ("MAM") with respect to the trading activity of the Appellant.*
5. *The learned AO/ learned TPO/ Hon'ble DRP erred in law by selecting Transactional Net Margin Method ("TNMM") as the MAM for benchmarking the international transactions for both manufacturing and trading activities of the Appellant.*
6. *The learned AO / learned TPO / Hon'ble DRP erred in not giving cognizance to the commercial and business reasons for the losses in the manufacturing segment of the Appellant by attributing the losses to the international transactions entered into by the Appellant.*
7. *The learned AO / learned TPO / Hon'ble DRP ought to have appreciated the fact that the losses incurred by the Appellant in the manufacturing segment was mainly due to underutilization of its production capacity and thereby ought to have granted an adjustment towards the underutilized capacity.*
8. *The learned AO / learned TPO / Hon'ble DRP ought to have appreciated that the cost of goods imported by the Appellant has increased significantly due to the adverse exchange rate fluctuation and thereby warrants an adjustment for foreign exchange fluctuations.*

9. *The learned AO/learned TPO/Hon'ble DRP ought to have provided appropriate customs duty adjustment.*

10. *Without prejudice to the above, the learned AO / learned TPO / Hon'ble DRP erred in not analyzing the impact of the proposed transfer pricing adjustment on the gross margin of the Appellant.*

11. *The learned AO/ learned TPO/ Hon'ble DRP erred in not considering multiple years' financial data of the comparable companies while determining the ALP.*

12. *The learned AO/ learned TPO/ Hon'ble DRP erred in applying a manufacturing income filter-of 75% to sales, leading to a narrower set of comparables.*

13. *The learned AO/ learned TPO/ Hon'ble DRP have erred in considering provision for doubtful debts as non-operating in nature while computing the margin of the comparable companies.*

14. *The learned AO/ learned TPO/ Hon'ble DRP erred in rejecting Eon Electric Ltd, which is functionally comparable to the Appellant.*

15. *The learned AO/ learned TPO/ Hon'ble DRP erred in computing the Profit Level Indicator ("PLI") of the following companies adopted by the Ld. TPO, which ought to be corrected, which are:-*

- *Crompton Greaves Ltd.*
- *TD Power Systems*
- *Havells India Ltd.*
- *Kirloskar Electric Co. Ltd.*

16. *Without prejudice to the above grounds, the learned AO / learned TPO / Hon'ble DRP ought to have appreciated that the transfer pricing adjustment, if any, should be proportionate/ restricted to the extent of the international transactions of the Appellant.*

The appellant craves leave to add, alter, rescind and modify the grounds herein above or produce further documents, facts and evidence before or at the time of hearing of this appeal.

For the above and any other grounds which may be raised at the time of hearing, it is prayed that necessary relief may be provided."

2. Brief facts of the case are as under:

The assessee has e-filed its return of income for the A.Y. 2014-15 on 29.11.2014 declaring a total income of Rs. 28,99,73,905/-. The case was selected for scrutiny through CASS under the category 'Complete Scrutiny'. The statutory notice u/s. 143(2) was issued on 28.09.2015 and was duly served on the assessee. Also, statutory notice u/s. 142(1) dated 23.12.2015 was issued to the assessee calling for the details. In response to the notice(s) issued, representatives and authorised representatives of the assessee appeared and produced the details called from time to time.

2.1 The Ld.AO observed that assessee is doing the business activities by Manufacturing and sale of Water Heaters and Water Purifiers. The assessee also imports certain type of Water Heaters to meet differential needs of the Customers. It is noted that the assessee provides after sales service to their customers for repairs and maintenance of the products sold. The Ld.AO noted that following were the international transaction entered into by the assessee during the relevant year under consideration.

Particulars	As per TP		As per 3CEB
	Amount in Rs.		Amount in Rs.
	Received/ Receivable	Paid/Payable	
Purchase of Raw Materials	0	477,890,613	477,890,613
Purchase of Traded goods	0	35,53,34,836	35,53,34,836
Royalty Paid	0	1,65,05,362	1,65,05,362
Consulting engineer Project Expenses	0	2,93,42,702	2,93,42,702
External Commercial borrowing	0	94,32,115	94,32,115
Issue of Equity Shares	0	75,32,50,000	75,32,50,000

Trade Payables	0	31,70,28,112	31,70,28,112
Total		1,95,87,83,740	1,95,87,83,740

2.2 The assessee for year under consideration applied CPM (Cost Plus Method) as most appropriate method for manufacturing activity and RPM (Resale Price Method) as most appropriate method with respect to the trading activity. The Ld.TPO rejected the MAM adopted by assessee for the reason that availability of data is an important criteria in selection of most appropriate method and that in the present case, the assessee admitted that there is non-availability of required data to verify the CPM or RPM analysis.

2.3 The Ld. TPO adopted TNMM as the MAM to determine the ALP of the transaction by adopting fresh analysis. The Ld.TPO proceeded to determine ALP of international transaction in manufacturing segment by bench marking and aggregating international transactions that is purchase of raw materials and purchase of traded goods. The Ld.TPO used four set of uncontrolled comparables with the average PLI (OP/Sales) of 6.52%. The Ld.TPO computed shortfall of Rs. 49,79,12,164/- and proposed adjustment towards the international transaction.

2.4 On receipt of the transfer pricing order, the Ld.AO passed draft assessment order by making addition in the hands of the assessee towards the international transaction at Rs.49,79,12,164/-. The Ld.AO in the draft assessment order disallowed provision for bonus and leave encashment as the same was not made before the due date of filing of return for the year under consideration.

2.5 Against the draft assessment order, the assessee filed objections before the DRP. The DRP deleted the disallowance of provision for bonus and leave encashment, however upheld the addition made in respect of international transactions.

2.6 On receipt of the draft DRP order, the Ld.AO passed the final assessment order by making additions in the hands of the assessee.

Aggrieved by the final assessment order, the assessee is in appeal before us now.

3. The Ld.AR at the outset submitted that coordinate bench of this *Tribunal* in assessee's own case, in the preceding assessment years addressed the issue on application of appropriate MAM under both the segments for *Assessment Year 2011-12* reported in (2018) 98 *taxmann.com* 295, wherein the issue is remanded to the Ld.TPO.

3.1 The Ld.CIT.DR did not have any objection for the issue being remanded to the Ld.TPO to be dealt with in accordance with the directions of this *Tribunal* in assessee's own case for *Assessment Year 2011-12*.

4. We have perused the submissions advanced by both sides in the light of records placed before us.

4.1 We note that following were co-ordinate decisions by this *Tribunal* in assessee's own case in the preceding *Assessment Years*.

- i) A.O. Smith India Water Heating Pvt. Ltd. in IT(TP)A Nos. 176 & 332/Bang/2015 dated 08.02.2018 (AY : 2010-11)
- ii) AO Smith India Water Products Pvt. Ltd. in IT(TP)A No. 216/Bang/2016 dated 12.09.2018 (AY: 2011-12)

iii) A.O. Smith India Water Products Pvt. Ltd. in IT(TP)A No. 628/Bang/2017 dated 10.02.2021 (AY: 2012-13)

4.2 We note that *Tribunal for Assessment Year 2011-12 (supra)*, decided the issue on applicability of appropriate MAM under both the segments. The relevant observations are as under:

"16. It has been submitted that, Ground No.4-10 are in respect of transfer Pricing addition made by the Ld.AO. He submitted that, these issue have been addressed by coordinate bench of this Tribunal in the assessee's own case for assessment year 2011-12, reported in [2018] 98 taxmann.com 295, wherein the issue has been remanded to the Ld.TPO.

17. The Ld.CIT.DR did not have any objection for the issue being remanded to the Ld.TPO, to be dealt with in accordance with directions by this Tribunal in assessee's own case for assessment year 2011-12.

18. We note that, this Tribunal for assessment year 2011-12 (supra) decided the issue as under:

"16. Aggrieved by the order of the DRP as aforesaid, the revenue has preferred the present appeal before the Tribunal.

17. We have heard the rival submissions. The ld. DR submitted that the basis on which the DRP deleted the TP adjustment made by the AO was not correct. In this regard, the ld. DR submitted that the requirement of [section 92\(1\)](#) of the Act for determination of ALP in respect of an international transaction has to be followed and merely for the reason that on such determination, the profit margin of the assessee will be exorbitant cannot be the basis to delete the addition made on account of determination of ALP. His submission that if the DRP finds that the MAM is CPM for international transaction for purchase of raw materials and RPM for international transaction for trading in water heaters is appropriate, then the DRP ought to have embarked upon an enquiry as to whether the ALP computed by the assessee in accordance with those methods was correct. It was submitted by him that by default price paid in international transaction cannot be considered as at arm's length. It was therefore submitted by him that determination of MAM

and determination of ALP based on the MAM should be directed to be carried out.

18. The ld. counsel for the assessee, on the other hand, pointed out that as far as international transaction of trading in heaters is concerned, in assessee's own case, this Tribunal has held that RPM is the MAM for determining the ALP. The decision of ITAT in [Dy. CIT v. A.O. Smith India Water Heating \(P.\) Ltd.](#)[2018] 97 taxmann.com 218 (Bang. - Trib.) was sought to be relied upon by the ld. counsel for the assessee. With regard to the international transaction of purchase of raw materials, the ld. counsel for the assessee brought to our notice that the only reason given by the TPO for rejecting the CPM as MAM is the absence of details regarding computation of gross profit of the assessee. In this regard, our attention was drawn to the TP study where the gross margins earned by the assessee have been clearly given. These details have already been extracted while dealing with the contentions of the assessee before the DRP in the earlier part of this order. It was therefore submitted by the ld. counsel for the assessee that the conclusions of the TPO that CPM is not the MAM in respect of international transaction for purchase of raw materials is not correct. The ld. counsel for the assessee therefore prayed that the order of the DRP should be upheld.

19. We have given a careful consideration to the rival submissions. As far as international transactions for purchase of raw materials is concerned, the only reason given by the TPO in rejecting CPM as MAM is the absence of gross margins of the assessee and the manner in which it was computed. In this regard, we find that in a letter dated 14.10.2014 filed by the assessee before the TPO in Annexure-2, the assessee has given cost of sales and other indirect cost. The same is at page 525 of assessee's PB. In these circumstances, we are of the view that the reasons given by the TPO for rejecting CPM as MAM cannot be sustained.

20. As far as international transaction of trading in water heaters is concerned, this Tribunal has already taken a view in assessee's own case for AY 2010-11 that RPM is the MAM. Following the aforesaid order, we hold that the TPO is not correct in rejecting the RPM as MAM.

21. As far as determination of ALP for both international transactions are concerned, we are of the view that the provisions of [section 92](#) mandate determination of ALP.

The fact that after carrying out such exercise, the profit margins of the assessee would be abnormal cannot be the basis to accept the price paid in the international transactions as at arm's length. In other words, it is mandatory to determine the ALP in the manner contemplated by the Act and the Rules. In our view, the DRP fell into an error in accepting the price received by the assessee in international transactions as at arm's length without carrying out such an exercise. We therefore feel it proper to set aside the order of DRP and remand to the AO/TPO for fresh consideration the determination of ALP on the basis of MAM as adopted by the assessee in its TP study.

22. The ld. counsel for the assessee submitted before us that the comparables chosen by the assessee in its TP study were also chosen by the TPO, when he adopted TNMM. His prayer was that pursuant to the remand by the Tribunal, the TPO should be directed to restrict himself from choosing any fresh comparables. In our view, the TPO has to carry out the exercise in accordance with the law and no restriction can be placed on his powers to bring any relevant and appropriate data on record in the matter of determination of ALP.

23. In the result, the appeal by the revenue is allowed for statistical purposes."

4.3 Admittedly, no difference of facts have been brought out for the year under consideration vis-a-viz the Assessment Years relied by the Ld.AR in the paper book being *Tribunal* orders passed in the assessment years.

4.4 Respectfully following the directions of this *Tribunal* for Assessment Year 2011-12, in assessee's own case, we direct the Ld.TPO to determine the ALP of the transactions under trading segment as well as manufacturing segments by adopting RPM and CPM respectively as most appropriate method as adopted by assessee in the TP study. We direct the Ld.TPO to determine the ALP in accordance with law. Needless to say that appropriate

opportunity of being heard shall be granted to assessee in accordance with law.

Accordingly, this ground raised by assessee stands allowed for statistical purposes as the ALP has to be computed afresh.

5. Ground nos. 7-16 becomes academic at this point and hence not adjudicated.

In the result, the appeal filed by assessee stands allowed for statistical purposes.

Order pronounced in open court on 23rd December, 2021.

Sd/-
(B.R. BASKARAN)
Accountant Member

Sd/-
(BEENA PILLAI)
Judicial Member

Bangalore,
Dated, the 23rd December, 2021.
/MS /

Copy to:

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

By order

Assistant Registrar,
ITAT, Bangalore