

IN THE INCOME TAX APPELLATE TRIBUNAL
PUNE BENCH 'C' PUNE

BEFORE SHRI R.S. SYAL, VICE PRESIDENT AND
SHRI S.S.VISWANETHRA RAVI, JUDICIAL MEMBER

आयकर अपील सं. / ITA No.581/PUN/2021

निर्धारण वर्ष / Assessment Year : 2013-14

DCIT, Circle-8, Pune	Vs.	Fette Compacting Machinery India Pvt. Ltd. [formerly known as LMT (India) Pvt. Ltd.] Plot No.A-40/1, Phase-I, MIDC Chakan, Vill – Nighoje, Tal. Khed, Pune – 410501 PAN: AAACL8169N
Appellant		Respondent

CO No.27/PUN/2021

निर्धारण वर्ष / Assessment Year : 2013-14

Fette Compacting Machinery India Pvt. Ltd. [formerly known as LMT (India) Pvt. Ltd.] Plot No.A-40/1, Phase-I, MIDC Chakan, Vill – Nighoje, Tal. Khed, Pune – 410501 PAN: AAACL8169N	Vs.	DCIT, Circle-8, Pune
Cross Objector		Respondent

Assessee by
Revenue by

Shri Damodar Vaidya
Shri Piyush Kumar Singh Yadav

Date of hearing

28-04-2022

Date of pronouncement

28-04-2022

आदेश / ORDER

PER R.S. SYAL, VP :

This appeal by the Revenue and Cross Objection by the assessee arise out of the order passed by CIT(A) on 18.06.2021 in relation to A.Y. 2013-14.

2. Pithily put, the facts of the case are that the assessee is a wholly owned subsidiary of LMT Group, headquartered in Germany, which is a leading Metalworking technologies group. The products and services of the assessee include precision tools and cutting materials for the most diverse applications in cutting and non-cutting processing as well as tool reconditioning and tool management packages. The assessee filed return declaring total income at Nil with current year loss of Rs.1,54,13,216. The assessee had reported certain international transactions. The Assessing Officer (AO) made a reference to the Transfer Pricing Officer (TPO) for determining their Arm's length price (ALP).

I. Trading Segment

3.1. The first issue raised by the Revenue is against the direction of the Id. CIT(A) to adopt Internal Resale Price Method (RPM) as the most appropriate method for benchmarking the 'Trading segment' of the assessee. Under this segment, the assessee reported international transaction of 'Purchase of raw materials' at the transacted value of Rs.12.73 crore. The RPM was adopted as the most appropriate method for demonstrating that the international transaction was at ALP. The TPO observed that the assessee had

not proved that the goods used in transactions with AE and non-AE were comparable. Further, the assessee had booked huge Employees cost in the Trading segment *vis-a-vis* the Manufacturing segment. In this backdrop of the facts, the TPO held that the RPM was not the most appropriate method. Instead, he adopted the Transactional Net Marginal Method (TNMM) and accordingly, recommended transfer pricing adjustment of Rs.1,28,29,678. The assessee filed certain additional evidence before the Id. CIT(A), on which a remand report was called for. On the basis of such remand report, the Id. CIT(A) held that the assessee had correctly applied the Internal RPM. Aggrieved thereby, the Revenue has preferred the appeal before the Tribunal.

3.2. We have heard the rival contentions and gone through the relevant material on record. The Trading segment is under consideration, in which the goods purchased by the assessee were admittedly sold as such without any value addition. The Id. DR, on the basis of the remand report of AO, fairly conceded that no value addition was made by the assessee to the goods purchased under the Trading segment. He harped on other factors to support his contention that the RPM was not correctly applied by the assessee.

In view of the fact that the assessee purchased and sold the same goods without increasing or reducing their inherent value, clearly the most appropriate method for determining the ALP in such a situation is the RPM. The Hon'ble Delhi High Court in *Pr.CIT vs. Matrix Cellular International Services Pvt. Ltd. (2017) 100 CCH 0191 (DelHC)* has held that where the goods are re-sold without making any value addition, the RPM is the most appropriate method. The contention of the Id. DR that more employee cost was booked in the Trading segment or that there was something amiss in the computation of the ALP under the RPM are irrelevant considerations. The ground before the Bench is against the selection of the most appropriate method and not the manner of its application. As the assessee sold the goods as such without tinkering with its inherent value, we countenance the view taken by the Id. CIT(A) in approving the application of the Internal RPM as most appropriate method against the TNMM applied by the TPO. This ground fails.

II. Manufacturing Segment

4.1. The first issue raised by the Revenue is against the direction of the Id. CIT(A) to include Electronica Machine Tools Ltd. in the list

of comparables. The Manufacturing segment comprised of the international transactions of 'Purchase of raw materials' at Rs.2.87 crore and 'Sale of materials' at Rs.2.43 crore. The assessee adopted the TNMM for showing the Manufacturing segment at ALP. The assessee treated Electronica Machine Tools Ltd. as one of the comparables. The TPO excluded it on the ground that it incurred extraordinary losses for the year under consideration. The assessee placed on record relevant material before the Id. CIT(A) in support of its contention. The Id. CIT(A), on appreciation of remand report from the AO, reversed the assessment order on this count and approved inclusion of this company.

4.2. Having heard the rival submissions and perused the relevant material on record, it is observed from the remand report of the AO, as reproduced at pages 24 and 29 of the impugned order, that: "As per the details available, it is not a persistent loss making company, as it has earned profits in earlier two years and next two years compared to the relevant year". The TPO, however, accentuated on the fact that there was a huge dip in the revenue for this year. Thus, it is evident that the only reason for the exclusion of this company by the TPO is the losses incurred by it in the year under

consideration. The Hon'ble Bombay High Court in *CIT vs. Welspun Zucchi Textiles Ltd. (2017) 92 CTR 1 (Bom)* has held that loss made in one year would not *ipso facto* result in exclusion of a company from comparability analysis. The Hon'ble Bombay High Court in an earlier decision in *CIT Vs. Goldman Sachs (India) Securities (P) Ltd. (2016) 290 CTR 236 (Bom)* has held that only persistent loss making companies can be excluded from the list of comparability. Since Electronica Machine Tools Ltd. admittedly incurred loss only in the year under consideration and was into profits in the earlier years, it ceased to be persistent loss making company. We are thus satisfied that the Id. CIT(A) was justified in including this company in the list of comparables. This ground fails.

5.1. Another issue raised by the Department is against direction of the Id. CIT(A) to allow adjustment on account of higher Customs duty paid by the assessee.

5.2. The facts apropos this issue are that the assessee submitted before the TPO that it had made 100% import of raw materials and components in comparison with comparables importing at 25.20%. It was urged that the increased cost of raw materials having the effect of Customs duty element, should be proportionately scaled

down so as to bring the assessee at par with the comparables. The TPO rejected such a contention which however, met with concurrence in the first appeal.

5.3. After considering the rival submissions and perusing the relevant material on record, it is observed that the claim of assessee for exclusion of Customs duty is based on the premise that it made more imports with the resultant increased cost of production because of higher incidence of Customs duty as against the comparables paying less amount of Customs duty. In our considered opinion, this argument is devoid of merits. It is not a case of payment of Customs duty by the assessee at a higher rate *vis-a-vis* comparables. It is just fundamental that if a person uses better quality raw materials, obviously, the corresponding sale price also goes up and *vice-versa*. Given the fact that the assessee imported more raw materials for manufacturing, it is but natural that the corresponding sale price would also have been on higher side, thereby nullifying the effect of higher payment of Customs duty, forming a part of the Operating cost base on the overall basis. The situation would have been different if the assessee had paid Customs duty at a rate higher than that paid by its comparables,

which would have called for adjustment to have a level playing. Instantly, we are confronted with a case in which the assessee is claiming exclusion of extra custom duty on the strength of its higher quantum and not the higher rate of Customs duty. In that view of the matter, we are satisfied that the Id. CIT(A) was not justified in reducing the operating cost base of the assessee in the Manufacturing segment by higher Customs duty paid by the assessee. This ground is allowed.

6.1. The first ground of assessee's Cross Objection pertains to the Manufacturing segment. The assessee is aggrieved by the treatment of Project expenses amounting to Rs.1.12 crores as operating, which were claimed as deductible in the computation of total income. The assessee claimed that unallocated project expenses amounting to Rs.1.12 crore (consisting of travelling expenses, legal & professional charges and other expenses) were non-operating and hence required exclusion from the operating cost base. The TPO rejected the contention and considered the same as operating cost. The Id. CIT(A) affirmed the decision of AO.

6.2. Having heard the rival submissions and perused the relevant material on record, it is seen from the nature of expenses that they

are otherwise of the revenue nature as they cater to travelling, legal & professional and other small heads. The assessee admittedly claimed deduction for such amount in the computation of total income, which has not been denied. A case has been set up that such expenditure related to the setting up phase of the manufacturing unit and hence, should be considered as non-operating. We are unable to countenance this contention for the reason that the Manufacturing unit was already in existence, which fact is borne out from the assessee's Profit & loss account for this year, which shows the figure of 'Revenue from operations' in the preceding year at Rs.7.75 crore as against Rs.7.99 crore for the year. This manifests that the unit was already set up in an earlier year and was in operation even in the preceding year much less the year under consideration. This appears to be the reason for the assessee claiming deduction for such expenses in its Profit & loss account and not capitalizing the same. But for that, there is no dispute that the expenses are otherwise of the operating nature. We, therefore, uphold the view taken by the Id. CIT(A) in treating Rs.1.12 crore as operating cost and including it in operating cost base. This is not allowed.

7. The only other ground taken by the assessee in its Cross Objection is against non-adjudication by the Id. CIT(A) of the exclusion of consultancy charges from the total AE cost while computing the proportionate adjustment. The assessee had raised ground No.3 in Form No. 35 before the Id. CIT(A) in this regard, which remained to be adjudicated. In view of the fact that we have given directions hereinabove concerning the ALP of the Manufacturing segment, which would require a re-do of the exercise, the AO / TPO will examine this claim of assessee also in such fresh proceedings. Needless to say, the assessee will be given reasonable opportunity of hearing.

8. In the result, the appeal of Revenue and the CO of assessee are partly allowed.

Order pronounced in the Open Court on 28th April, 2022.

Sd/-
(S.S.VISWANETHRA RAVI)
JUDICIAL MEMBER

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

पुणे Pune; दिनांक Dated : 28th April, 2022
GCVSR

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

1. अपीलार्थी / The Appellant;
2. प्रत्यर्थी / The Respondent;
3. The CIT(A)-13, Pune
4. The PCIT-3, Pune
5. DR, ITAT, 'C' Bench, Pune
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,**// True Copy //**

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

		Date	
1.	Draft dictated on	28-04-2022	Sr.PS
2.	Draft placed before author	28-04-2022	Sr.PS
3.	Draft proposed & placed before the second member		JM
4.	Draft discussed/approved by Second Member.		JM
5.	Approved Draft comes to the Sr.PS/PS		Sr.PS
6.	Kept for pronouncement on		Sr.PS
7.	Date of uploading order		Sr.PS
8.	File sent to the Bench Clerk		Sr.PS
9.	Date on which file goes to the Head Clerk		
10.	Date on which file goes to the A.R.		
11.	Date of dispatch of Order.		

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