

**IN THE INCOME TAX APPELLATE TRIBUNAL  
“C” BENCH : BANGALORE**

**BEFORE SHRI N.V. VASUDEVAN, VICE PRESEIDENT  
AND  
SHRI PADMAVATHY S, ACCOUNTANT MEMBER**

IT(TP)A No. 73/Bang/2017
Assessment year : 2012-13

Denso Kirloskar Industries Pvt. Ltd., 30 <sup>th</sup> KM Stone, Tumkur Road, NH 4, Vishveshwarapura, Nelamangala, Bengaluru – 562 123. <b>PAN: AABCO 0042P</b>	Vs.	The Assistant Commissioner of Income-tax – LTU, Circle 1, Bengaluru.
ASSEESSEE		RESPONDENT

Assessee by	:	Shri T. Suryanarayana, Advocate
Respondent by	:	Shri V.S. Chakrapani, CIT(DR)(ITAT), Bengaluru.

Date of hearing	:	23.06.2022
Date of Pronouncement	:	20.07.2022

**ORDER**

*Per Padmavathy S., Accountant Member*

This appeal is against the final assessment order dated 10.11.2016 passed by the Assessing Officer for the AY 2012-13.

2. The assessee is a company engaged in the business of manufacture of aluminum radiators and air-conditioners for cars and multi utility vehicles for automobile manufacturers in India. During

the relevant year, there were several international transactions between the assessee and its AEs in the manufacturing segment. The assessee selected TNM Method as the most appropriate method and taking certain comparable companies, the assessee concluded the international transactions as at arm's length. In arriving at the profit margin, the assessee made certain adjustments to its operating cost base.

3. On a reference from the AO, the TPO passed an order dated 14.1.2016 determining a TP adjustment of Rs.56,87,83,323 in the manufacturing segment without granting the adjustments made by the assessee to its operating cost base. According to the assessee, the TPO made the adjustment at the entity level by taking into consideration the unrelated party transactions, instead of restricting the adjustment to the value of international transactions. The draft assessment order was passed by the AO incorporating the above TP adjustment. The DRP rejected the objections of the assessee and upheld the TP adjustment. Consequently, the final assessment order was passed sustaining the TP adjustment of Rs.56,87,323. Aggrieved, the assessee is in appeal before the Tribunal.

4. Though various grounds of appeal are raised by the assessee, the Id. AR submitted that the issues that arise for consideration in this appeal pertains to the adjustments not allowed to the operating cost in the manufacturing segment vide ground Nos.5, 6 & 9 are as follows:-

- i. Adjustment towards fluctuation of foreign currency (Ground 5)
  - ii. Adjustment towards customs duty (Ground )
  - iii. Adjustment to the purchase of raw materials not restricted to transactions with AE (Ground 9)
5. The other grounds were not pressed and as such they are dismissed.
6. The assessee has also filed a petition for admission of additional ground for re-computation of operating profit margin pursuant to the MAP resolution covering the international transactions with the assessee and Denso Japan (DNJP). The additional ground reads as under:-

“Without prejudice, the Assessee’s operating profit margin ought to be recomputed considering the revised transfer pricing of international transactions as concluded pursuant to the resolution agreed between the Competent Authorities of India and Japan under the Mutual Agreement Procedure (MAP) and thereby, the resultant downward revision in transfer pricing of international transactions amounting to INR 28,24,62,043 has to be reduced from the cost base while re-computing the operating profit margin of the Assessee. Alternatively, the said amount could be added to the operating income of the Assessee as the same has been offered to tax in India pursuant to MAP resolution.”

7. The ld. AR prayed for admission of the additional ground.
8. We have heard the rival submissions on the admission of the additional ground. The additional ground now raised does not require examination of new facts otherwise than on record and following *the Hon’ble Supreme Court judgment in the case of M/s National Thermal*

*Power Co. Ltd. Vs. CIT, 229 ITR 383 (SC)*, the additional ground is admitted for adjudication.

9. In the course of hearing the Ld AR submitted a paper book with additional evidence supporting its claim for adjustment towards Foreign Exchange Fluctuation and Customs Duty (Ground 3, 4 and 5) . The ld.AR prayed for admission of additional evidences before the Tribunal as these evidences when considered would substantiate the claim of the assessee that the international transactions of the assessee are at arm's length. With regard to various TP adjustments, the additional evidences now produced go the root of the issue and the core reason for not granting adjustment towards the two adjustment by the lower authorities. For a proper adjudication of the issue and for substantial cause, the additional evidence is admitted and taken on record.

10. Ground No.5 reads as follows:-

“5. The learned AO/ learned TPO / Hon'ble DRP has erred in not granting economic adjustments towards adverse effect of forex due to depreciation of Indian Rupees resulting in incremental import costs which is not attributable to the transfer pricing of its purchase of raw materials from its AEs.”

11. The brief facts of the issue are that the assessee imports a considerable amount of raw material for undertaking the manufacturing operations in India in order to meet the stringent quality requirements. In view of the business model it bears significant risk on account of foreign exchange fluctuation. The assessee enters into

contracts with its customers in India which is reviewed and revised year on year. While negotiating the price, one of the aspects taken into consideration is the cost of materials to be imported from Japan for manufacture in India. During the FY 2011-12, Yen rates were fluctuating. Subsequent to its commitment of the sale price with the customers, rupee depreciated significantly and therefore the assessee had to incur additional cost of manufacture, which could not be recouped as the assessee had committed to the sale price under the contractual obligations. This additional cost incurred by the assessee is not a loss which can be debited to the profit and loss account, and therefore it made an adjustment to the operating cost base by reducing an amount of Rs. 41,79,88,435.

12. The TPO denied the adjustment on the following grounds and the same was upheld by the DRP that :-

- i. the loss in the manufacturing segment has arisen on account of high import cost, and the Assessee did not suitably negotiate the purchase cost from its AE;
- ii. the computation made by the Assessee is not in line with AS 21; and
- iii. the Assessee has failed to show the differences between comparables and the Assessee in respect of the exchange fluctuation loss, which the DRP upheld.

13. The observations of the TPO/DRP and submissions of the assessee are summarized below:-

<b>TPO/DRP observations</b>	<b>Assessee's submissions</b>
<p>Forex gain or loss has to be computed as per AS 21 as done in audited P&amp;L. The taxpayer has debited Rs. 1,04,60,347 as forex loss to the P&amp;L account treated it as operating expenses.</p>	<p>Forex fluctuation computed as per AS 21 takes into account the realization loss/gain (fluctuation due to differences between invoice and payment exchange rates) and revaluation loss/gain (translation of closing balances at the year-end exchange rate). Hence such exchange fluctuation does not take into account any adverse exchange fluctuation due to depreciation of Indian currency on a year-on-year basis.</p>
<p>The Assessee's loss is mainly due to higher import cost of raw materials. The Assessee did not suitably negotiate its purchase cost with its AE.</p> <p>The Assessee failed to demonstrate that there exists such losses in the case of comparable companies selected by the Assessee.</p>	<p>The Assessee bears the forex risk and hence it has incurred high forex fluctuation loss which is embedded in the raw material import cost. The fact that forex risk is borne by the Assessee cannot be a valid reason for rejecting the adjustment claimed by it. As the Assessee bears the forex risk, any adverse fluctuation on foreign currency would be borne only by the Assessee. The AE has nothing to do whatsoever with this. In fact, during the year under consideration the per unit price of the materials imported is less than the per unit price paid in the previous year, except in a marginal number of cases. Further, the Assessee has negotiated a better price in the subsequent years with its customers and there is a gradual increase in the selling price in the subsequent years. Such fluctuation being due to external factors, there would be no reason for the AE to revise its rate contracts where</p>

	<p>components have been sold broadly at consistent prices. It is to be noted that there has been an extraordinary and significant depreciation in INR over Yen/USD during the year when compared to the previous years.</p> <p>The Assessee's profitability is significantly impacted as a result of forex fluctuation. As adjustment made was towards exchange fluctuation component included in the raw material cost, even though the purchase rate of raw material has remained constant, the Assessee has paid more in absolute terms merely because of the difference in exchange rate from the earlier year.</p>
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14. In light of the above, the Id. AR submitted that an adjustment for the abnormal impact due to foreign currency fluctuation during the year, ought to be made on the value of import purchases made during the year.

15. The Ld. AR contended that the assessee had to honour the terms of contract and supply the products at the committed rate for the entire year even though there was significant increase in the cost of the products by virtue of higher cost of the components being imported vis-a-vis be comparable companies selected by the assessee who had less significant imports. The Ld AR also submitted that the assessee had in the in the subsequent years negotiated for a better price with the customers and has realised better margins (**pages 35-36 of additional evidence**). The Ld AR brought to our attention that there is no increase

in the price of raw materials supplied by the AE to the appellant as compared to the previous year which is evident from the analysis of per unit price in foreign currency for financial year 2010-11 and 2011-12 produced at **pages 27 to 34 of the additional evidence compilation**. The Ld AR submitted that considering the movement in the INR as compared to YEN and that there is no increase in price would demonstrate that the loss has arisen solely on account of exchange fluctuation which warrants adjustment in TP for comparables. The details of the economic adjustment claimed on account of adverse fluctuation in foreign currency is furnished at **pages 37-213 of the additional evidence compilation**.

16. The ld. AR further submitted that this issue is covered in the assessee's favour by the decision of this Tribunal in the Assessee's own case for the AY 2011-12 (Order dated 30.03.2022 passed in IT(TP)A No, 649/Bang/2016), wherein the Tribunal directed the TPO to consider foreign exchange fluctuation adjustment for computing ALP of the Assessee.

17. The ld. DR supported the orders of the lower authorities.

18. This issue came up for consideration before this Tribunal in assessee's own case for AY 2011-12 and vide order dated 30.3.2022, it was held as under:-

“20. The Ld DR relied on the written submissions. We heard the rival submissions and perused the materials on record. We notice that the Delhi Bench of the Hon'ble Tribunal in the case of Honda Trading Corp. India Pvt. Ltd., vs ACIT (2013) 33

Taxmann.com 21 (Delhi Trib) has decided on the similar issue as under-

‘19. From the order of the DRP, we observe that the DRP considered the objection of the assessee related to rejection of Orbit Industries as a comparable and held that the assessee has not given any cogent reason for change in the new search process which was essential to have current year data and the filters applied earlier need to be applied now to maintain consistency in approach. The DRP further held that abnormal losses indicate that it was not a normal loss because financial analysis was triggered for FAR and this comparable fails at the very first step. In view of cogent reasons recorded by the TPO and DRP, we are unable to see any infirmity and perversity in these findings in rejection of Orbit Industry as a comparable. On the issue of adjustment of exchange fluctuation, loss incurred by the assessee, we observe that it is a well accepted principle of Transfer Pricing regulations to compare like with like and eliminate the differences if any, by suitable adjustment. The said principle clearly provides for adjustments in margins of the enterprise entering into international transactions for any differences between such international transactions and the transaction of comparables or between the enterprise entering into international transactions and comparable companies. The foreign exchange element also needs consideration. Rule 10B(3) of Income Tax Rules, 1962 provides that an appropriate adjustment is required to be made on account of the differences between the controlled and the uncontrolled transactions. This rule clearly stipulates that an uncontrolled transaction shall be comparable to an international transaction, if none of the differences between the transactions being compared, or between the enterprises entering into such transactions are likely to materially affect the price or cost charged or paid in, or the profit arising from, such transactions in the open market. This rule clearly stipulates that reasonably accurate adjustments can be made to eliminate the material effects of such differences.

20. The counsel of the assessee has placed reliance on the judgment of ITAT Delhi Bench in the case of Transwitch India (P.) Ltd. v. Dy. CIT [2012] 53 SOT 151/21 taxmann.com 257 wherein it has been held that the claim of comparability adjustment on account of abnormal expenses incurred by the assessee on account of relocation expenses should be allowed in

the profitability of the assessee. The assessee has also relied on the judgment of ITAT Pune Bench in the case of Demag Cranes & Components (India) (P.) Ltd. v. Dy. CIT [2012] 49 SOT 610/17 taxmann.com 190 wherein the Tribunal elaborately dealt with the issue of comparability adjustment.

21. From the above submissions and careful perusal of citations and all other relevant judgments we observe that Rule 10(B)(1)(e) of the Act on the one side and other sub-rules in the context of TNMM need to be analyzed for eliminating the difference, if any, in the comparable uncontrolled transaction which materially affect the profit margin of the assessee. Having noticed the difference, the revenue has to quantify the difference, if any, and then revenue authorities must decide if that difference constitutes 'materially affect' the price in open market. As per these provisions, if the answer of the above question is in the affirmative, then the identified difference has to be removed and the margin has to be adjusted for arriving at the credible comparable. It is a well-accepted accounting principle that net margins can be influenced by some of same factors which can influence price or gross margin;. It is the expectations and requirements of the rules/provisions that any difference which is likely to materially affect the net profit margin (NPM) in the open market has to be eliminated. The revenue authorities and TPO are duty bound to know that the TNMM visualizes the undertaking of a thorough comparability analysis and elimination of the differences through the requisite adjustments.

22. In the case in hand, admittedly the average exchange rate of Thai Bhat during October, 2005 to March 2006 was 100 Thai Bhat equivalent to INR 110 and after consideration of said average exchange rate, price of sale of goods had to be agreed upon with the customers. The DR has not disputed the point that during April 2006 to September 2006 at the time of purchase, the exchange rate of Thai Bhat was substantially increased and the average exchange rate of Thai Bhatt was increased to 100 Thai Bhat = INR 119. Accordingly, we can not rule out and ignore this factual matrix emerged from the fluctuation of foreign exchange rates that while prices of purchases and import made by the Assessee have increased, the sale price of exported goods remained on the lower side which is an important element to materially affect the price in the open market. In this situation, we are inclined to hold that the authorities below should have considered the said difference due to foreign

exchange rate fluctuation in favour of Thai Bhat and against the INR and the said difference has to be removed and the margin thereon has to be adjusted for arriving at the credible comparable through the requisite adjustments.

23. During the course of arguments, the DR submitted that the issue of fluctuation in foreign exchange price was considered by the authorities below but from perusal of the impugned order, inter alia, order of the DRP, we observe that the authorities below have not considered the element of abnormal and huge fluctuation in the foreign exchange fluctuation in favour of Thai Bhat and against the INR and the said difference has to be removed and the margin thereon has to be adjusted for arriving at the credible comparable through the requisite adjustments.

24. During the course of arguments, the DR submitted that the issue of fluctuation in foreign exchange price was considered by the authorities below but from the perusal of the impugned order, inter alia, order of the DRP, we observe that the authorities below have not considered the element of abnormal and huge fluctuation in the foreign exchange favouring Thai Bhat and against the Indian currency. Accordingly, in view of the observations made hereinabove, ground nos. 2.7 and 2.8 are allowed with a direction to the Assessing Officer that necessary adjustments pertaining to the huge and abnormal fluctuation in the foreign exchange may be allowed to the assessee in determining the ALP of the international transaction undertaken by the Assessee:’

21. We also notice that the coordinate bench of the Tribunal in the case Continental Automotive Components India Pvt Ltd (Supra) has held that

“39. This issue was also considered by the Chennai Tribunal in the case of Gates Unitta India Company (P.) Ltd. (supra) and it was held as under:—

"7. We have heard both the parties and perused the material on record. In our opinion, forex fluctuations loss in the operating cost of the assessee and also forex gains in the operating income of assessee, both to be excluded from the operating expenses as well as operating income respectively in view of the Order of Tribunal in the case of Motonic IndiaAutomotive (P.)

Ltd. (supra) in for assessment year 2009-10 vide order dated 17-8-2016 wherein held that :—

'9. We find force in the argument of the ld. AR. It is normal that exchange rate is subject to fluctuation due to economic conditions. While determining the ALP, one has to consider these factors, more so, our view is fortified by the decision of the Tribunal in the cases of Honda Trading Corp. India Pvt. Ltd. v. ACIT in ITA No. 5297/Del/2011 for the assessment year 2007-08 and DHL Express (India) Pvt. Ltd. v. ACIT in ITA No. 7360/Mum/2010 for the assessment year 2006-07. Accordingly, we direct the TPO to provide considerable exchange fluctuation adjustment while determining the ALP. Accordingly, this issue is remitted to the file of the TPO for determining the ALP after considering the above three components i.e. customs duty adjustment, air freight adjustment and foreign exchange fluctuation adjustment.'

Accordingly, this issue is remitted to the file of AO for fresh consideration."

40. Following the aforesaid decision of the Tribunal, we remit this issue to the AO/TPO with similar directions for fresh decision."

22. Considering the judicial precedence and the materials submitted, we remit this issue to AO/TP with a direction to consider the foreign exchange fluctuation adjustment for computing the ALP of the assessee. This ground is allowed in favour of the assessee for statistical purposes."

19. Following the above order of the Tribunal in assessee's own case for AY 2011-12 (supra), this issue is remitted to the AO/TPO with a direction to consider the foreign exchange fluctuation adjustment for computing the ALP.

20. Ground No.6 raised by the assessee is as follows:-

“5. The learned AO/ learned TPO / Hon’ble DRP has erred in not excluding the additional custom duty costs as a result of increased import costs of raw materials due to forex impact of depreciation of the Indian Rupee.”

21. The assessee has incurred additional costs towards purchase of raw materials due to the adverse exchange rate fluctuation and as consequence of the price increase, the Assessee has incurred significant customs duty charges. The assessee has made adjustments towards the customs duty paid as an extraordinary item while arriving at the operating cost. The TPO rejected the adjustment for the same reasons for rejecting the adjustment towards exchange fluctuation loss which was upheld by the DRP.

22. The Id AR submitted that on account of the exchange fluctuation, the assessee has paid significant non-cenvatable customs duty on its imports, which cannot be passed on to the customer. The effect of the same of Rs. 3,54,68,588/- has been treated as an extraordinary expense while computing the operating margin of the Assessee. This cost is not incurred by the comparable companies who do not undertake significant imports. Therefore, the Id AR prayed that an adjustment to eliminate the difference arising on account of the customs duty paid ought to be granted. In this regard the Id AR drew our attention to the computation of adjustment for non-cenvatable duty set out at **page 279 of the additional evidence** compilation and the details of the imports made by the comparable companies are set out at **page 278 of the additional evidence** compilation.

23. We have heard the Id DR and perused the material on record. We notice this issue was considered by this Tribunal in assessee's own case for AY 2011-12 and it was held as follows:-

"27. We heard the rival submissions and perused the material on record. We notice that the coordinate bench of the Tribunal in the case of M/s. Continental Automotive Components (India) Pvt. Ltd (supra) has considered the similar issue. The Hon'ble Tribunal has held that

'30. This issue came up for consideration before the Chennai Tribunal in the case of Gates Unitta India Co. (P.) Ltd. v. Dy. CIT [2017] 84 taxmann.com 69 wherein it was held as follows:—

"5. Before us, Id. A.R submitted that 90% of the raw materials of the assessee are imported as such customs duty adjustments to be made and it includes Rs. 4.31 crores pertained to the customs duty in the manufacturing segment. In principle the customs duty adjustments is allowed in view of the Co-ordinate Bench decision in the case of Motonic IndiaAutomotive (P.) Ltd. v. Asstt. CIT [2016] 73 taxmann.com 235 (Chennai - Trib.) wherein held that:

'6.1 At this stage, it is pertinent to mention the finding of the Pune Bench in the case of Demag Cranes & Components (India) Pvt. Ltd. v. DCIT (supra) dated 4-1-2012 in ITA No. 120/PN/2011, which is as follows :

"37. We have heard the parties and perused the available material on records in the light of the second limb of the ground 4(b). It is relevant mentioned that we have already analysed the relevant provisions of Income-tax rules vis a vis the scope of the adjustments in the preceding paragraphs in the context of the adjustments on account of the 'working capital'. In principles, our findings on the issue remain applicable to the adjustments on account of the import cost mentioned in ground 4(b) too. The difference between the AL Margin before and after the said adjustments on account of 'import cost' works out to 0.57% (7.18%-6.61%). Revenue has not disputed the

said working of the assessee. In these factual circumstances and in the light of the scope of adjustments discussed above, in our opinion and in principle, the assessee should win on this ground too. One such decision relied upon by the assessee's counsel supports our finding relates to the decision of this bench of the Tribunal in the case of Skoda Auto India P. Ltd. 122 TTJ 699 (Pune) dated March 2009 wherein, it is held (in para 19 of the order) that,-

"No doubt , a higher import content of raw material by itself does not warrant an adjustment in operating margins, as was held in Sony India (P) Ltd.'s case (supra), but what is to be really seen is whether this high import content was necessitated by the extraordinary circumstances beyond assessee's control. As was observed by a Co-ordinate Bench of this Tribunal in the case of E-Gain Communication (P) Ltd. (supra) "the differences which are likely to materially affect the price, cost charged or paid in, or the profit in the open market are to be taken into consideration with the idea to make reasonable and accurate adjustment to eliminate the differences having material effect". We do not agree with the AO that every time the assessee pays the higher import duty, it must be passed on to the customers or it must be adjusted for in negotiating the purchasing price. All these things could be relevant only when higher import content is a part of the business model which the assessee has consciously chosen but then if it is a business model to import the SKD kits of the cars, assemble it and sell it in the market, that is certainly not the business models of the comparables that the TPO has adopted in this case. The adjustments then are required to be made for functionally differences. The other way of looking at the present situation is to accept that business model of the assessee company and the comparable companies are the same and it is on account of initial stages of business that the unusually high costs are incurred. The adjustments are thus required either way. It is, therefore, permissible in principle to make adjustments in the costs and profits in fit cases. We also do not agree with the authorities below that the onus is on the assessee to get all such details of the comparable

concerns so as to make this comparison possible. The assessee cannot be expected to get the details and particulars which are not in public domain. In such a situation, i.e. when information available in public domain is not sufficient to make these comparisons possible, it is inevitable that some approximations are to be made and reasonable assumptions are to be made. The argument before us was that it was first year of assessee's operations and complete facilities ensuring a reasonable indigenous raw material content was not in place. The assessee's claim is that it was in these circumstances that the assessee had to sell the cars with such high import contents, and essentially high costs, while the normal selling price of the car was computed in the light of the costs as would apply when the complete facilities of regular production are in place. None of these arguments were before any of the authorities below. What was argued before the AO was mere fact of higher costs on account of higher import duty but then this argument proceeded on the fallacy that an operating profit margin for higher import duty is permissible merely because the higher costs are incurred for the inputs. That argument has been rejected by a Coordinate Bench and we are in respectful agreement with the views of our esteemed colleagues. This additional argument was not available before the authorities below and it will indeed be unfair for us to adjudicate on this factual aspect without allowing the TPO to examine all the related relevant facts. We, therefore, deem it fit and proper to remit this matter to the file of the TPO for fresh adjudication in the light of our above observations."

38. The perusal of the impugned orders shows that the above cited guidelines by way of decision of this bench of the Tribunal in the case of Skoda Auto India P. Ltd. (supra) were not available to the revenue authorities. Therefore, we are of the opinion, the issue should be set aside to the files of the TPO with direction to examine the claim of the assessee relating to the import cost factor and eliminate the difference if any. However, the TPO/AO/DRP shall see to it that the difference in question is 'likely to materially affect' the price/profit in the open market as envisaged

in sub-rule (3) of rule 10B of the Income-tax Rules, 1962. Accordingly, ground 4(b) is allowed pro tanto.'

Accordingly, we direct the A.O. to give suitable adjustment against the custom duty component while determining the ALP.'

Hence, to bring uniformity, the customs duty was to be eliminated from the comparable price also to arrive at correct PLI. Accordingly, we remit the issue to the file of AO for fresh consideration."

31. In view of the above finding of the Tribunal in Gates Unitta India Company (P.) Ltd. (supra), we are inclined to remit this issue to the AO/TPO with similar directions.'

28. Respectfully following the decision of the coordinate bench of the Tribunal, we are remitting this issue to the AO/TPO for fresh consideration. This is ground is allowed in favour of the assessee for statistical purposes."

24. Respectfully following the decision of the coordinate bench of the Tribunal, we remit this issue to the AO/TPO for fresh consideration with similar directions. This ground is allowed in favour of the assessee for statistical purposes.

25. Ground No.9 by the assessee is as follows:-

"9. The learned AO/ learned TPO / Hon'ble DRP has erred in not appreciating that the transfer pricing adjustment, if any should be restricted to the international transactions of the Assessee."

26. The Id. AR submitted that the action of the TPO in determining an adjustment by taking into account the transactions with unrelated parties is wholly erroneous and is contrary to the provisions of the Act and the rules made thereunder. It is submitted that in terms of Section 92CA of the Act, the Assessing Officer can refer the matter to the TPO

for computation of ALP only in relation to international transaction and the TPO is empowered to compute the ALP only of the said international transaction. It is submitted that no adjustment can be made in respect of transaction entered into with non-AEs as the same are presumed to be at arm's length and are not subject to transfer pricing provisions. Therefore the action of the TPO is wholly without jurisdiction. Moreover, it is submitted that the TPO had restricted the transfer pricing adjustment to the purchase of raw materials in the Assessee's own case for the AY 2011-12. The Id AR placed reliance on the decision of the Hon'ble High Court of Bombay in *CIT v. Phoenix Mecano (India) Pvt. Ltd.* (Order dated 07.06.2017 passed in ITA No. 1182/2014) wherein it was held that the determination of ALP ought to be restricted to transactions with AEs and the SLP preferred by the Revenue against the said order came to be dismissed by the Hon'ble Supreme Court vide order dated 05.02.2018 in SLP No. 4205/2018. Therefore the Id AR submitted that the issue has reached finality

27. The Id. DR supported the orders of the lower authorities.

28. We heard both the parties and perused the material on record. We notice that the coordinate bench of the Tribunal in the case of *IKA India (P.) Ltd.* (98 taxmann.com 312, Bang. Trib) considered a similar issues and held that section 92 of the Act can be applied only in respect of international transactions *i.e.*, transactions with AE. The relevant observations are as follows:-

**“54.** We have heard the rival submissions. The ld. counsel for the assessee reiterated submissions made before the CIT(A) that transaction with non-AE cannot be subject matter of determination of ALP because section 92 clearly speaks of determination of ALP only in respect of transactions with AE. He also referred to certain decisions of the Tribunal for the proposition that section 92 of the Act is not applicable to non-AE transactions. These decisions have already been extracted in the earlier paragraphs. The ld. DR relied on the order of the CIT(Appeals).

**55.** We have considered the rival submissions. The reasoning of the CIT(A) for considering the entire sales in manufactured finished goods segment for determination of ALP is that certain components and raw materials used in manufacture of finished goods are also sourced from AE and there is a possibility of the cost of such component having been bargained at a price which is not at arm's length. This presumption of the CIT(Appeals) is without any basis. He has not demonstrated with actual figures as to how there would be impact on profit margin on sale of finished products to AE because of purchases of some components from AE. He has given examples which are imaginary figures. Apart from this, the TPO has accepted that purchase of raw material and components by the assessee from its AE is at arm's length. Therefore, the basis on which the CIT(A) proceeded to apply the ALP test for transactions with non-AE is neither correct on facts nor permissible in law. As rightly contended by the assessee, section 92 of the Act can be applied only in respect of international transactions *i.e.*, transactions with AE.

**56.** In view of the above transfer pricing provisions and various judicial precedents, we hold that the transfer pricing adjustment should be restricted only to the AE related transactions of the assessee.”

29. Respectfully following the above decision of the coordinate bench of the Tribunal, we hold that the transfer pricing adjustment

should be restricted only to the international transactions with the AE. This ground is allowed in favour of the assessee.

30. The next issue for consideration is recomputation of operating profit margin pursuant to the MAP resolution which is raised by the assessee in the form of additional ground.

31. During the year under consideration, the assessee entered into international transactions with its AEs situated in Japan, and in countries other than Japan. Initially, the TPO determined an aggregate adjustment of Rs. 56,87,83,323/- in respect of the transaction with the AEs both in Japan and elsewhere. Thereafter, the mutual agreement procedure (MAP) under the India-Japan DTAA came to be invoked and the TP adjustment determined in respect of the transactions with the AEs in Japan came to be resolved. Under the resolution, the amount of Rs. 36,13,79,077/- which was considered as being the adjustment made in respect of the transaction with the AEs in Japan stood reduced to Rs. 28,24,62,043/-, and relief was granted in respect of the balance adjustment of Rs. 7,89,17,034/-. Now through additional ground the assessing is praying that the segmental margin of the assessee needs to be re-computed taking into the account the adjustment determined under MAP.

32. The Id AR submitted that pursuant to the MAP resolution, the returned loss of the Assessee stood reduced and thereafter in the assessment years 2015-16 and 2016-17, the assessee set off the said brought forward losses against the income of those years. The Id AR

also submitted that the segmental margin of the assessee ought to be recomputed, taking into account the adjustment determined under MAP, either by reducing the operating cost base to that extent, or increasing the operating income. Reliance was placed on the decision of this Tribunal in the assessee's own case for the assessment year 2011-12 (supra).

33. The ld. DR supported the order of the lower authorities.

34. We have considered the rival submissions and perused the material on record. This issue was considered in assessee's own case for AY 2011-12 (supra) wherein it was held as under:-

“**33.** We have heard the rival submissions and perused the materials on record. We notice that the MAP resolution which resulted in the reduction of the cost (thereby reduction in the returned loss) and as contended by the Ld AR will have an impact on the other TP adjustment done with AEs other than Japan. The argument of the Ld AR that the impact of reduced loss which resulted in additional income being offered to tax should be given effect in re-computing the segmental margin requires looking at the matter afresh. Hence we remit the issue back to the AO for re-computation of the operating margins. The AO is directed accordingly. This ground is allowed in favour of the assessee for statistical purposes.”

35. Following the above order of the Tribunal, we remit this issue to the AO with a direction to re-compute the operating margins pursuant to the MAP resolution.

36. In the result, the appeal by the assessee is partly allowed.

Pronounced in the open court on this 20<sup>th</sup> day of July, 2022..

Sd/-

Sd/-

( N V VASUDEVAN )  
VICE PRESIDENT

( PADMAVATHY S )  
ACCOUNTANT MEMBER

Bangalore,  
Dated, the 20<sup>th</sup> July, 2022.

*/Desai S Murthy /*

Copy to:

1. Assessee 2. Respondent 3. CIT 4. CIT(A) 5. DR, ITAT,  
Bangalore.

By order

Assistant Registrar  
ITAT, Bangalore.