

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

**BEFORE SHRI SHAMIM YAHYA, ACCOUNTANT MEMBER AND
Ms. ASTHA CHANDRA, JUDICIAL MEMBER**

**ITA No.526/DEL/2021
[Assessment Year: 2016-17]**

SMA Nutrition India Pvt. Ltd. 100/101 World Trade Centre, Barakhamba Lane, New Delhi-110001	Vs	Additional/Joint/Deputy/Assistant Commissioner of Income- tax/Income Tax Officer, National e- Assessment Centre, Delhi
PAN-AAECC8474D		
Assessee		Revenue

Assessee by	Sh Ajay Vohra, Sr. Adv. Mr. Neeraj Jain, Adv. Mr. Abhishek Aggarwal, CA
Revenue by	Sh. Sandeep Kumar, Sr. DR

Date of Hearing	16.06.2022
Date of Pronouncement	02.08.2022

ORDER

PER SHAMIM YAHYA, AM,

This appeal by the assessee is directed against the order of the Assessing Officer, dated 31.03.2021, passed in accordance with DRP direction dated 19.03.2020.

2. Grounds of appeal reads as under:-

"1. That the impugned order of Assessing Officer ["AO"] dated 31.03.2021, passed under section 144C read with section 143(3) of the Income-tax Act, 1961 ("the Act"), is bad in law and unsustainable.

2. That the assessing officer erred on facts and in law in proposing to complete assessment under section 144C read with section 143(3) of the Income-tax Act ("the Act") at an income of Rs. 57,29,061 as against the returned loss of Rs. 2,95,95,477.

3. That the AO/ Transfer Pricing Officer ("TPO") erred on facts and in law in making addition to the income of the appellant of Rs. 3,53,24,538 on account of the alleged difference in arm's length price of the international transactions undertaken by the appellant.

3.1 That the AO/TPO erred on facts and in law in rejecting the segmental profitability of the appellant and proceeding to undertake benchmarking analysis on the basis of entire cost without appreciating that the mandate of transfer pricing provisions is restricted to benchmarking the international transactions undertaken by the appellant.

3.2 That the DRP erred on facts and in law in rejecting the segmental profitability statement of the appellant allegedly holding that the basis of allocation of expenses is not known, without appreciating that detailed segmental profitability statement along-with allocation keys were submitted before the AO/ TPO and the DRP.

3.3 That the AO/TPO erred on facts and in law in rejecting the segmental accounts furnished by the appellant without appreciating that in the domestic segment the functional profile of the appellant is entirely different from the functional profile of the appellant in the services segment and combining the two segments leads to absurd and skewed results

3.4 That the AO/TPO/ DRP erred on facts and in law in holding that no assets have been employed or risk assumed under the distribution segment only on the basis that no revenue has been generated from distribution segment during the year and therefore erred in incorrectly rejecting the separate FAR profile of the business and segmental profitability/ accounts furnished by the assessee

3.5 That the AO/TPO erred on facts and in law in arbitrarily rejecting search conducted by the appellant and undertaking a fresh search for comparable companies.

3.6 That the AO/TPO erred on facts and in law in considering Killick Agencies and Marketing Ltd. as comparable to the appellant not appreciating that the company is engaged in provision of agency services as well as after sales engineering services, earning more than 80 percent of its revenue from commission income and therefore cannot be regarded as comparable for the purpose of benchmarking the international transaction of provision of IT administration and coordination services undertaken by the appellant

3.7 That the AO/TPO/DRP erred on facts and in law in rejecting the following companies on the basis that the companies are engaged in provision of housekeeping and facility management services not appreciating that the companies are comparable to the appellant in terms of the provisions of Rule 10B(2) of the Rules:

- a) JSB Staffing Solutions Pvt Ltd*
- b) Service Max Facilities Management Pvt Ltd*
- c) Checkmate facility & electronic solutions Pvt Ltd.*

3.8 That the TPO erred on facts and in law in rejecting MNR Solutions Private Limited as comparable on the basis that the annual report of the company has not been furnished by the appellant even though the annual report of the company is available in public domain.

3.9 Without prejudice, that the TPO erred on facts and in law in not restricting the adjustment to the cost attributable to the international transaction of provision of IT administration and coordination services.

4. That the AO erred on facts and in law in initiating penalty proceedings under Section 271(l)(c) of the Act.

3. Brief facts of the case are that during the year under consideration, the assessee company was engaged in rendering IT administration and Coordination services to NOSW as per the term of the agreement dated 01.10.2014. The assessee had entered into international transaction with its Associated Enterprises. SMA Nutrition is wholly owned subsidiary of Nestle SA and is in the process of setting up distribution business of infant nutrition products. During FY 2015-16 the company is engaged in rendering IT administration and coordination services to NOSW as per the terms of the agreement dated October 1, 2014. The shareholding pattern of the assessee as on 31.03.2014 is as under:-

Nestle. S.A.	97%
Maggi Enterprises Ltd.	3%
Total	100%

4. The international transactions entered into by the assessee company with its associated enterprises during this year are summarized in the table below:-

S. No.	Particulars	Method	Value (In INR)
1.	Service Fee	TNMM	2,55,27,186
2.	Reimbursement of expenses	TNMM	5,26,265
3.	Purchase of IT equipments and services	TNMM	6,85,625
	Total		2,67,39,076

5. Further, the TPO noted that in respect of international transaction representing Services fees, assessee considered TNMM as the most appropriate method and ratio of operating profit to operating cost (OP/OC) was considered as the profit level indicator with the assessee as tested party. The range of the operating margins of the comparables was calculated at 9.11% to 15.10%. Since, the PLI of the tested party was 10.01% being within the Arm's Length range of margin of the comparables. The transactions were considered to be at Arm's Length. The Assessing Officer issued various notices proposed various comparables. Finally, the Assessing Officer computed the Arm's Length as under:-

"10.1. In the light of discussion made above, the following companies are taken into consideration for determination of arm's

length price i.r.o. the international transactions relating to fee for service rendered to AE.

S. No.	Company Name	Weighted Average (OP/OC)
1	Manpower Group Services Pvt. Ltd.	1.85%
2	Kestone Integrated Mktg. Services Pvt. Ltd.	5.89%
3	Aarvi Encon Ltd.	7.65%
4	Pressman Advertising Ltd.	11.36%
5	Ace Integrated Solutions Ltd.	12.84%
6	K H F M Hospitality & Facility Mgmt.	13.82%
7	IC R A Management Consulting Services	13.84%
8	Concept Public Relations India Ltd.	15.01%
9	L E Human Resources Solutions Pvt. Ltd.	15.69%
10	Killick Agencies & Mktg. Ltd.	18.30%
11	E D CIL (India) Ltd.	21.10%
12	Praendex Management Resources Pvt.	23.90%
13	Kitco Ltd.	32.01%
14	Interactive Manpower Solution Pvt. Ltd.	35.54%

35 Percentile	12.84%
65 Percentile	18.30%
Median	14.43

10.2. The Calculation of arm's length price for the business support segment is as given below:-

Particulars	Amount in INR
Operating Cost (A)	5,24,48,000
Arm's length margin (%) (B)	14.43%
Arm's length margin (Rs.) (C=A*B)	75,68,247
Arm's length Price (D=A+C)	6,00,16,247
Price charged by the assessee (E)	2,43,98,000
Difference between ALP and Price	3,56,18,247
Adjustment required	3,56,18,247

10.3 Thus an adjustment of Rs. 3,56,18,247/- is to be made to the income of the assessee, being the difference between the arm's length price and the price charged by the AEs for the international transaction for ;fees for rendering services to AE. The Assessing Officer shall enhance the income of the assessee by an amount of Rs. 3,56,18,247/- while computing its total income.”

6. Against the above order, the assessee placed objection before DRP. The assessee's preparations of segmental accounting were not

accepted by the DRP. Hence, the DRP upheld the action of the TPO and rejected the segmental analysis of the assessee taking the total cost as resulting from and directly attributable to the benchmarked transaction of the AE segment pertaining to provisions of IT administration and coordination services on an entity wise basis is reasonable and justified. Thereafter, as regards selection of comparables, the Ld. DRP accepted some of the comparables and rejected the rest and direct the TPO to compute margin accordingly.

7. Against this order, the assessee is in appeal before us.

8. The primary thrust of ld. counsel for the assessee is that segmental profitability is to be considered for benchmarking analysis. In this regard, the assessee's submissions are as under:-

"I. Segmental profitability to be considered for the purpose of benchmarking analysis

At the outset it is respectfully submitted that during the course of assessment proceedings, the appellant vide submission dated April 18, 2019 furnished segment-wise employee details before the TPO as under:-

S. No.	Employee Name	Designation	Segment	Job Description/ Profile
1	Sharat Kumarij guda	Head of IS/IT Office	Business Support	Overall supervision of the work being undertaken in the segment
2	Rajashekar Venkata Gopala	Senior Manager- IS/IT	Business Support	Rendering IT administration and coordination services to NOSW

3	Suryanarain Malladi	IT Manager	Business Support	<p>-Assistance in overview of Compliance management of services provided by India based External Service Providers (ESP) to NOSW</p> <p>-Follow up of implementation of audit findings</p> <p>-Adherence to Nestle's Security policies/principles</p> <p>-Support ESP's KPI/Service Monitoring, and quality assurance</p>
4	Vineela Readdy Vontari	Officer Techno Operation support	Business Support	<p>-Ensure adequate escalation of issues/incidents</p>
5	Mr. Sachi Thomas	Country Business Manager-Nutrition	Distribution	<p>-Development of entry plan for the business</p>
6	Sourabh Hembrum	Senior Brand & Project Mgr - Nutrition	Distribution	<p>-Building regulatory strategy to ensure successful approvals, wherever required</p> <p>-Planning of prelaunch activities.</p>

It is submitted that two senior employees of the appellant namely Mr. Sachi Thomas, Country Manager, Nutrition and Mr. Sourabh Hembrum, Senior Manager, Brand and Project Manager - Nutrition were engaged in (i) Development of entry plan for the business, (ii) Building regulatory strategy to ensure successful approvals and

(iii) Planning of pre-launch activities. Further, the appellant also furnished the extract from General Ledger along with cost center codes for the purpose of allocating the employee benefit cost.

The appellant also submitted segment wise details of invoices raised by Nestle India Limited for provision of various services to the appellant. It was submitted that Nestle India renders services in the nature of finance, HR and Legal to the IT Administration and coordination services division and supply chain, regulatory, IS/IT services for the distribution business of the appellant. Accordingly, it is submitted that detailed submissions and evidence with respect to differences in the functionality of the IT Administration and Coordination services segment and the distribution segment of the appellant were placed on record before the TPO. (Page No 159 and 162-169 of paper book volume II).

Further, vide submission dated April 02, 2019 (page 47 of paper book Vol I) the appellant placed on record segmental workings and basis of allocation of costs between business support and distribution segments. It is submitted that entire details relating to segmental financial statements has been submitted by the appellant before the TPO and the TPO has not pointed out any defect or deficiency in the segmental financial statements furnished by the appellant.

However, the TPO/DRP arbitrarily rejected the segmental financial statements of the appellant and considered the entity level financial statements for the purpose of benchmarking analysis. The TPO while rejecting the segmental analysis stated that the entire turnover of the appellant was derived from the international transactions undertaken with the associated enterprises and therefore concluded that the appellant is operating in only a single segment not appreciating that segregation of segments is to be based on FAR of business activities carried by the appellant in different segments, and not solely on the revenue earned from a particular segment ignoring the cost and FAR completely.

It is submitted that in terms of section 92 of the Act the TPO is required to determine the arm's length price of an international transaction undertaken by the appellant. However, by considering the entity level financial statements of the appellant the TPO has proceeded to benchmark the transactions undertaken by the appellant with independent entities/third parties and thereby exceeding the mandate provided under section 92 of the Act.

It is submitted that the entity level financial statements of the appellant includes cost and revenue derived from the international transaction of provision of services to the associated enterprises as well as cost incurred in connection with setting up of the local distribution business of the appellant. It is submitted that the TPO has included the cost incurred for local distribution business in the cost base for the purpose of benchmarking the international transaction of provision of IT administration and coordination services without appreciating that such cost has no connection with

the international transaction of provision of services undertaken by the appellant.

It is submitted that the functional profile of the appellant within the domestic business is entirely different from the functional profile of the appellant in the services segment. The comparison of functional profile of a distributor and a captive service provider is as under:

Particulars	Distributor	Captive Service Segment
Functions		
Procurement of finished goods	Yes	No
Pricing w.r.t. sales to final customers	Yes	No (Captive service provider)
Selling and distribution/maintaining distribution channel	Yes	No
Assets		
Distribution infrastructure	Yes	No
Risk		

Particulars	Distributor	Captive Service Segment
Functions		
Market Risk	Yes	No
Product liability risk	No	Yes
Inventory risk	Yes	No

In view of the aforesaid, it is submitted that the functional profile of the appellant in the 2 segments is entirely different from each other and accordingly, the segments cannot be aggregated for the purpose of benchmarking analysis.

It is submitted that it is a settled legal position that for the purpose of undertaking benchmarking analysis, the relevant segment of the tested party is only required to be taken into consideration.

Further, in the case of Technimount ICB India Pvt Ltd vs ACIT (ITA No 7098/Mum/2010) the Hon'ble Tribunal while upholding the preference of segmental profitability statement over entity level margins held as under (Pg 14 of CL PB):

"24. Now, coming to the main issue whether the segmental results are to be taken into consideration or profit margin at entity level is to be considered, we find that Chapter-X incorporates special provisions relating to avoiding of tax in regard to international

transactions and income from international transactions has to be determined at arm's length price. Therefore, as per the provisions contained under sections 92 to 94, international transactions are to be taken into consideration. Therefore, segmental results are to be considered and not the profit at entity level. "

Reliance in this regard is placed on the decision of Bangalore Bench of the Tribunal in the case of UCB India Pvt. Ltd. v ACIT 121 ITD 131 (Mum) wherein the Hon'ble Tribunal held as under (Pg 45 of CL PB):

"Only in cases where profits of an enterprise are attributable to similar transactions and when an enterprise does not have any other transaction or

activity which is not similar, and which distorts the profits, then probably the net margin derived by an enterprise may also be the net margin of a transaction. In other words, when in an enterprise, only similar transactions are undertaken, i.e., all the transactions are of the same type, same class and of similar variety, and the enterprise does not have any other transaction which is not similar, in such a situation, the operating margins of the enterprise would be the TNMM of a class of transaction. "

Reliance in this regard is also placed on the decision of Mumbai Bench of the Tribunal in the case of Lionbridge Technologies Pvt. Ltd. vs. DCIT (ITA no. 9032/Mum/2010) wherein the Tribunal held that the transfer pricing adjustment can be made only with reference to the segmental profitability of the international transactions undertaken with the AE (Pg 59-60 of CL PB).

Similarly, in the case of DDIT vs Coming SA (ITA No 2564/Del/2011) the Hon'ble Tribunal while holding that functionally different segments cannot be clubbed for the purpose of benchmarking analysis stated as under (Pg 84 of CL PB):

"25. Having regard to the above factual matrix we are thus inclined to uphold the conclusion of the CIT(A) to benchmark the two independent functions separately. We do not find any merit in the contention raised by the learned counsel that these are closely linked transactions undertaken by the appellant. On the contrary the nature of transactions are functionally different and even the risk assumed are different. We thus negate the stand of the assessee and uphold the findings of CIT(A) in benchmarking the distribution/agency function separately. "

Similarly, the Hon'ble Mumbai Bench of the Tribunal in the case of Star India Pvt Ltd (ITA No 3585/Mum/2006) directed the TPO to undertake benchmarking analysis' on the basis of segmental results.

Reliance in this regard is also placed on the following decisions wherein benchmarking analysis on the basis of segmental profitability statement has been upheld by the Hon'ble Tribunal:

(i) *Starlite vs DCIT (ITA No 925/Mum/2006)*

(ii) *Addl CIT vs Tej Diamonds (ITA No 5034/Mum/2007)*

(iii) *Genisys Integrated Systems (India) Pvt Ltd (ITA No 1231/Bang/2010)*

In view of the aforesaid, it is respectfully submitted that the TPO ought to have considered the segmental profitability analysis submitted by the appellant for the purpose of benchmarking analysis.

It is submitted that operating margin of the appellant after considering foreign exchange loss as non-operating in nature is worked out at 12.42% computed as under:

	Amnt (INR)
Receipts	2,55,27,186
Less: recovery of out of pocket expenses	(11,29,654)
Operating income	2,43,97,532
Employee benefit cost	16,850,179
Operational support services	18,85,93
Travel and conveyance(excluding out of pocket expenses incurred on behalf of overseas visitors and travellers, having no relation with rendering of services under contact service agreement dt.01.10.2014)	98,515
Rent	15,03,392
Other administrative expenses	17,36,541
Total	2,20,73,820
Less: Exchange Difference/Forex Loss	(3,72,197)
Operating expenses (B)	2,17,01,623
Operating Profit[C=(A)-(b)]	26,95,909
OP/OC[C/B%]	12.42%

Accordingly, it is respectfully submitted that since the operating margin of the appellant at 12.42% is within the 35th and 65th percentile of 11.36% and 15.69% of the aforesaid comparable companies, the international transaction of provision of IT administration and coordination services may be considered as having been conducted at arm's length.

9. Without prejudice to the above, the assessee had made some objection to the incorrect selection of comparable, Killick Agencies & Marketing Ltd. and he has further without prejudice pleaded that international transaction to be restricted to the value of international transaction. Further, more the Ld. counsel for the assessee has given

rebuttal to the ld. DR's pleading that assessee segmental account is not reliable as under:-

"In the course of hearing, it was pointed out that during the relevant previous year, the company was engaged in provision of IT administration and co-ordination services ('Business Support Segment') and was also in the process of setting up the distribution business of infant nutrition products ('Distribution Segment') and that the appellant vide submission dated April 18, 2019 furnished segment-wise employee details before the TPO. Segment wise details of invoices raised by Nestle India Limited for provision of various services to the appellant were also submitted to the TPO.

Further, vide submission dated April 02, 2019 (page 47 of paper book Vol I) the appellant placed on record segmental workings and basis of allocation of costs between business support and distribution segments. The TPO did not point out any defect or deficiency in the allocation of expenditure by the Appellant for determining the net profit margin in the business support and distribution segment nor the TPO required the appellant to submit any certificate in respect of such segmented profitability prepared in the TP Study.

The Ld. DR had submitted in the course of hearing that the segmental profitability could not be relied upon since the same was not certified by an auditor / CA. The Hon'ble Bench had directed the appellant to file submissions in rebuttal to the aforesaid proposition canvassed by the Ld. DR.

In response thereto, it is submitted that the segmental cannot be discarded merely on the basis that the same are not certified. There is no mandate / direction / requirement in the Act / Rules making it mandatory / compulsory for the segmental to be certified by an auditor / CA before the same can be taken into consideration. The Delhi bench of the Hon'ble Tribunal in the case Birlasoft India Ltd. vs. DCIT (44 SOT 664) held as under:

"16.2 On perusal of AS-17 read with paragraph 5 thereof, we find that AS-17 requires reporting of financial information or result about the different types of products and services that the concerned business segment produces, which includes different geographical areas of business operation. In the present case before us, we find that the appellant-company provides same software related services to both Associated Enterprises and unrelated parties. It is not

anybody's case that the appellant-company is not providing same software related services to both Associated Enterprises and unrelated/uncontrolled parties. Therefore, the appellant was not required for segmental reporting nor for disclosing separate financial information in respect of transactions entered into with AEs and non-AEs. In other words, guidelines provided under AS-17 are not applicable to appellant's case. We, therefore, hold that the lack of segmental reporting for the reason that the transactions with AEs and non-AEs belong to the same item of software related services, cannot be made a basis for rejecting appellant's method of computing the Arm's Length Price by way of internal comparison made between the transaction with AEs and unrelated parties. "

Attention is also invited to the decision of Delhi Bench of Tribunal in the case of Lummus Technology Heat Transfer BV vs. DCIT (ITA No. 6227/Del/2012), wherein the Hon'ble Tribunal has held as under:

"It is not at all necessary that such a computation should be based on segmental accounts in the books of accounts regularly maintained by the appellant and subjected to audit. We are, therefore, of the view that the authorities below were in error in rejecting the segmental results on the ground that the segmental accounts were not audited and that these segmental accounts were not maintained in the normal course of business. "

Having regard to the submission made hereinabove, the transfer pricing adjustments made by the TPO ignoring the segmental results placed on record cannot be sustained, more particularly in view of the fact that the TPO did not point out any defect / deficiency to the allocation of the expenditure towards business segment and the segmental results arrived at, notwithstanding that the segmental results were not certified by an auditor / CA.

10. Upon careful consideration of submissions of both the parties, we find considerable cogency in the submission of ld. counsel of the assessee. The case law cited is germane and support the plea canvassed. The segmental accounting prepared cannot be rejected without pointing out defects in the allocation done by the assessee. Moreover, it is also

noted that accounts are duly audited. There is also no rule that if segmental accounts are certified by CA. the Assessing Officer should stop application of mind and follow it as a gospel truth.

11. Hence, we are of the opinion that the segmental accounting prepared by assessee should be accepted and the consequence shall accordingly follow. Hence, to be fair to the parties, we are remitting the issue to the file of Assessing Officer once again to review the segment account prepared by the assessee and unless he can rebut the same with cogent reasoning, he shall accept the same.

12. In the result, assessee's appeal is allowed for statistical purposes.

Order pronounced in the open court on 02.08.2022.

Sd/-
[ASTHA CHANDRA]
JUDICIAL MEMBER

Sd/-
[SHAMIM YAHYA]
ACCOUNTANT MEMBER

Delhi; Dated: 02.08.2022.

Shekhar,

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR

Asst. Registrar,
ITAT, New Delhi