IN THE INCOME TAX APPELLATE TRIBUNAL
Mumbai "K" Bench, Mumbai.

Before Shri B.R. Baskaran (AM) & Shri Narender Kumar Choudhry (JM)

I.T.A. No. 2398/Mum/2021 (A.Y. 2013-14)

DCIT, Circle 4(2)(1) Room No. 642 6th Floor, Aayakar Bhavan, M.K. Road Mumbai-400 020.	Vs.	M/s. Hamon Cooling Systems Pvt. Ltd. 3A-8A, Main Frame Royal Palms Complex Goregaon East Mumbai-400 065. PAN : AAACT2254Q
(Appellant)		(Respondent)

Assessee by	Shri Sanjay R. Parikh
Department by	Shri Ashish Kumar
Date of Hearing	16.08.2023
Date of Pronouncement	06.09.2023

O R D E R

Per B.R.Baskaran (AM) :-

The Revenue has filed this appeal challenging the order dated 14.10.2021 passed by the learned CIT(A)-56, Mumbai and it relates to A.Y. 2013-14. The Revenue is aggrieved by the decision of the learned CIT(A) in deleting the transfer pricing adjustment made by the TPO/AO in respect of

(a) Research and Development Expenses paid and

(b) Management Fees paid by the assessee to its associated enterprises (AE).

2. The assessee company is engaged in the business of manufacturing, designing, engineering and supplying cooling towers and its spares. It also provides engineering services and air pollution control units. The assessee is 50:50 joint venture between M/s Hamon D'Hondt Group, Belgium and M/s. Shriram Group, India. During the year under consideration, the assessee paid Rs.1.31 crores to its AE named M/s. Hamon Thermal Europe (Belgium)

SA for Research & Development expenses. It also paid a sum Rs. 2.06 crores to another AE named M/s Hamon & CIE - Belgium towards management fees. The TPO determined arm's length price (ALP) of both the above expenses as Nil and accordingly proposed TPA of Rs. 1.31 crores in respect of R&D expenses and Rs. 1.03 crores in respect of the management fees. Besides the above the TPO also made transfer pricing adjustment of Rs. 48,136/- towards purchase of raw material.

3. In the appellate proceedings the learned CIT(A) noticed that the transfer pricing adjustment made in respect of R&D expenses and management fees has been deleted by the Tribunal in the assessee's own case, vide its order dated 27.5.2020 passed for A.Y. 2007-08, 2010-11 & 2011-12. Following the same the learned CIT(A) deleted the adjustment made in respect of the above said two items. The learned CIT(A), however, confirmed the transfer pricing adjustment made on account of purchase of raw material. Aggrieved by the relief granted by the learned CIT(A), the Revenue has filed this appeal before the Tribunal.

4. Learned DR submitted that the assessee did not furnish evidences in order to prove the receipt of services from its AE and the details of exact cost incurred by the Associated Enterprises. Hence the TPO has determined the ALP of the R&D expenses and Management fees as NIL. He further submitted that the Tribunal, in the earlier years, has deleted the adjustment on the ground that the TPO has not determined ALP of the international transactions under any of the methods prescribed in the income tax rules. The Learned DR submitted that the Tribunal has to ensure that the methodology prescribed in the Act is duly followed and accordingly, deficiency, if any, committed by the tax authorities should be corrected by the Tribunal. Accordingly, he contended that the Tribunal should restore the

matter to the file of the TPO directing him to determine ALP under any of the method prescribed under the Income tax rules.

5. The Learned AR, on the contrary, strongly objected to the submissions made by learned DR. He submitted that the learned CIT(A) has followed the decision rendered by the ITAT in earlier years and hence his order cannot be found fault with. With regard to the ALP of international transactions, learned AR submitted that the assessee has taken its foreign AE as tested party and followed internal CUP as most appropriate method. The assessee has demonstrated that the fees charged by the AE for providing similar services to unrelated parties was more than that charged to the assessee herein. The Learned AR submitted that it is not the case of the TPO that the assessee did not receive any services at all from its AE. He submitted that the assessee has furnished all the details in its transfer pricing study, but the same has not been properly looked into. He submitted that under the Principle of Consistency, the order passed by the Coordinate Bench in the earlier year in assessee's own case should be followed by this Tribunal also.

6. We heard rival contentions and perused the record. We noticed earlier that the TPO has determined the ALP of both the international transactions as NIL, i.e., the TPO did not determine the ALP under any of the prescribed methods. The question as to whether the TPO can determine the ALP of international transactions as NIL was examined by Hon'ble Delhi High Court in the case of CIT vs. M/S. CUSHMAN AND WAKEFIELD (INDIA) PVT. LTD (367 ITR 730)(Delhi), wherein it was held as under:-

"34. The Court first notes that the authority of the TPO is to conduct a transfer pricing analysis to determine the ALP and not to determine ITA 475/2012 Page 25 whether there is a service or not from which the assessee benefits. That aspect of the exercise is left to the AO. This distinction was made clear by the ITAT in Dresser-Rand India Pvt. Ltd. v. Additional Commissioner of Income Tax, 2012 (13) ITR (Trib) 422:

> *"8. We find that the basic reason of the Transfer Pricing Officer's determination of ALP of the services received under cost contribution*

arrangement as 'NIL' is his perception that the assessee did not need these services at all, as the assessee had sufficient experts of his own who were competent enough to do this work. For example, the Transfer Pricing Officer had pointed out that the assessee has qualified accounting staff which could have handled the audit work and in any case the assessee has paid audit fees to external firm. Similarly, the Transfer Pricing Officer was of the view that the assessee had management experts on its rolls, and, therefore, global business oversight services were not needed. It is difficult to understand, much less approve, this line of reasoning. It is only elementary that how an Assessee conducts his business is entirely his prerogative and it is not for the revenue authorities to decide what is necessary for an Assessee and what is not. An Assessee may have any number of qualified accountants and management experts on his rolls, and yet he may decide to engage services of outside experts for auditing and management consultancy;

it is not for the revenue officers to question Assessee's wisdom in doing so. The Transfer Pricing Officer was not only going much beyond his powers in questioning commercial wisdom of Assessee's decision to take benefit of expertise of Dresser Rand US, but also beyond the powers of the Assessing Officer. We do not approve this approach of the revenue authorities. We have further noticed that the Transfer Pricing Officer has made several observations to the effect that, as evident from the analysis of financial performance, the assessee did not benefit, in terms of financial results, from these services. This analysis is also completely irrelevant, because whether a particular expense on services received actually benefits an Assessee in monetary terms or not even a consideration for its being allowed as a deduction in computation of income, and, by no stretch of logic, it can have any role in determining arm's length price of that service. When evaluating the arm's length price of a service, it is wholly irrelevant as to whether the assessee benefits from it or not; the real question which is to be determined in such cases is whether the price of this service is what an independent enterprise would have paid for the same. Similarly, whether the AE gave the same services to the assessee in the preceding years without any consideration or not is also irrelevant. The AE may have given the same service on gratuitous basis in the earlier period, but that does not mean that arm's length price of these services is 'nil'. The authorities below have been swayed by the considerations which are not at all relevant in the context of determining the arm's length price of the costs incurred by the assessee in cost contribution arrangement. We have also noted that the stand of the revenue authorities in this case is that no services were rendered by the AE at all, and that since there is No. evidence of services having been rendered at all, the arm's length price of these services is 'nil'."

35. The TPO's Report is, subsequent to the Finance Act, 2007, binding on the AO. Thus, it becomes all the more important to clarify the extent of the TPO's authority in this case, which is to determining the ALP for international transactions referred to him or her by the AO, rather than determining whether such services exist or benefits have accrued. That exercise - of factual verification is retained by the AO

under Section 37 in this case. Indeed, this is not to say that the TPO cannot - after a consideration of the facts - state that the ALP is 'nil' given that an independent entity in a comparable transaction would not pay any amount. However, this is different from the TPO stating that the assessee did not benefit from these services, which amounts to disallowing expenditure. That decision is outside the authority of the TPO. This aspect was made clear by the ITAT in Delloite Consulting India Pvt. Ltd. v. Deputy Commissioner of Income Tax, [2012] 137 ITD 21 (Mum):

> *"37. On the issue as to whether the Transfer Pricing Officer is empowered to determine the arm's length price at "nil", we find that the Bangalore Bench of the Tribunal in Gemplus India P. Ltd. 2010-TII-55-ITAT-BANG-TP, held that the assessee has to establish before the Transfer Pricing Officer that the payments made were commensurate to the volume and quality service and that such costs are comparable. When commensurate benefit against the payment of services is not derived, then the Transfer Pricing Officer is justified in making an adjustment under the arm's length price.*
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> *38. In the case on hand, the Transfer Pricing Officer has determined the arm's length price at "nil" keeping in view the factual position as to whether in a comparable case, similar payments would have been made or not in terms of the agreements. This is a case where the assessee has not determined the arm's length price. The burden is initially on the assessee to determine the arm's length price. Thus, the argument of the assessee that the Transfer Pricing Officer has exceeded his jurisdiction by disallowing certain expenditure, is against the facts. The Transfer Pricing Officer has not disallowed any expenditure. Only the arm's length price was determined. It was the Assessing Officer who computed the income by adopting the arm's length price decided by the Transfer Pricing Officer at "nil"."*

This is a slender yet crucial distinction that restricts the authority of the TPO. Whilst the report of the TPO in this case ultimately noted that the ALP was 'nil', since a comparable entity would pay 'nil' amount for these services, this Court noted that remarks concerning, and the final decision relating to, benefit arising from these services are properly reserved for the AO.

36. In this case, the issue is whether an independent entity would have paid for such services. Importantly, in reaching this conclusion, neither the Revenue, nor this Court, must question the commercial wisdom of the assessee, or replace its own assessment of the commercial viability of the transaction. The services rendered by CWS and CWHK in this case concern liaising and client interaction with IBM on behalf of the assessee - activities for which, according to the assessee's claim - interaction with IBM's regional offices in Singapore and the United States was necessary. These services cannot - as the ITAT correctly surmised - be duplicated in India insofar as they require interaction abroad. Whether it is commercially prudent or not to employ outsiders to conduct this activity is a matter that lies within the assessee's exclusive domain, and cannot be second-guessed by the Revenue.

37. At this point, it is noteworthy that the circumstance that the assessee had market research facilities in India does not correspond to the performance of services abroad, especially in relation to client interaction services located outside India - albeit for ultimately sourcing them into the Indian market. The e-mails considered by the ITAT from Mr. Braganza and Mr. Choudhary so far as they deal with specific interaction with IBM by those persons, and relate it to benefits obtained by the assessee, provide a sufficient basis to hold that benefit accrued to the assessee. However, this determination remains unclear and inchoate. The devil here lies in the details. The details of the specific activities for which cost was incurred by both CWS and CWHK (for the activities of Mr. Braganza and Mr. Choudhary), and the attendant benefit to the assessee, have not been considered till date. This must be provided, in addition to a consideration of the ALP vis-à-vis the total cost claimed by these AEs. ***To this extent, for the consideration of ALP in respect of these transactions, the matter is remanded back to the file of the concerned AO, for an ALP assessment by the TPO, followed by the AO's assessment order in accordance with law."***

7. A careful perusal of the above said decision rendered by Hon'ble Delhi High Court would show that the TPO is required to determine the ALP of international transactions under any of the methods prescribed under the Income tax Rules, i.e., the TPO is not correct in determining the ALP at Nil without establishing that a third party would not have paid any money under similar circumstances. The TPO is not empowered to disallow the expenses.

8. Admittedly, in the instant case, the TPO did not examine the ALP of the impugned international transactions under any one of the methods prescribed under the Income tax Rules. Hence, he was not justified in determining the ALP of the impugned international transactions as NIL. Though the co-ordinate benches have deleted the TP adjustments made, yet we notice that the Hon'ble Delhi High Court in the above said case has restored the matter of determination of ALP of transactions to the file of AO/TPO. Accordingly, following the decision rendered by Hon'ble Delhi High Court, we set aside the order passed by Ld CIT(A) with regard to the determination of ALP of Research and Development Expenses and Management Fees and restore both the issues to the file of AO/TPO with the direction to determine the ALP of both the transactions under any one of the methods prescribed under the Rules. The assessee is also directed to furnish

all the information and explanations in support of the claim that the payments are at arms length.

9. In the result, the appeal of the assessee is treated as allowed for statistical purposes.

Order pronounced on 06.09.2023.

Sd/-	Sd/-
(Narender Kumar Choudhry)	(B.R. Baskaran)
Judicial Member	Accountant Member

Mumbai.; Dated : 06/09/2023

Copy of the Order forwarded to :

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

BY ORDER,

//True Copy//

(Assistant Registrar)

PS ITAT, Mumbai