

**INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "I-2": NEW DELHI
BEFORE SHRI I.C.SUDHIR, JUDICIAL MEMBER
AND
SHRI PRASHANT MAHARISHI, ACCOUNTANT MEMBER**

ITA No.499/Del/2013
(Assessment Year:2005-06)

ACIT, Circle-12(1), New Delhi	Vs.	Gillete Diversified Operations Pvt. Ltd., C/o. Jaikumar Tejwani & Co, CA, B-50, East of Kailash, New Delhi PAN:AAACG2469C
(Appellant)		(Respondent)

ITA No.151/Del/2013
(Assessment Year: 2005-06)

Gillete Diversified Operations Pvt. Ltd., C/o. Jaikumar Tejwani & Co, CA, B-50, East of Kailash, New Delhi PAN:AAACG2469C	Vs.	ACIT, Circle-12(1), New Delhi
(Appellant)		(Respondent)

Revenue by :	Sh.Subhakant Sahu, Sr. DR
Assessee by:	Sh. Pradeep Dinodia, Adv Sh. R. K. Kapoor, CA
Date of Hearing	02/02/2016
Date of pronouncement	01/04/2016

ORDER

PER PRASHANT MAHARISHI, A. M.

1. These are the cross appeal filed by the revenue and the assessee against the order of the Id CIT(A)-XXIX, New Delhi dated 12.11.2012 for the Assessment Year 2005-06.
2. In ITA No.499/Del/.2013 the revenue has taken three effective grounds of appeal:-
 - “1. *On the facts and in the circumstances of the case the learned CIT(A) has erred in accepting the submissions of the assessee that part of rates & taxes. Insurance, loss on sale of assets, common Service expenses and Misc. expenses are not attributable to earning of dividend income.*
 2. *On the facts and circumstances of the case and in law the learned CIT(A) has erred in restricting the disallowance out of interest u/s 14A by accepting the percentage of dividend income to total income at 6.65% because the total income taken by the assessee and accepted by the*

CIT(A) included sales of Rs.21,58,73,267/-, thereby restricting the disallowance out of interest at Rs.1,50,670/- only and giving a relief of Rs.12,03,804/-.

3. *On the facts and circumstance of the case and in law the Ld. CIT(A) has erred in restricting the addition of Arm's Length Price of International Transactions with Associated enterprises from Rs.2,82,02,588/- to Rs.71,79,984/-, thereby giving a relief of Rs.2,10,02,604/-."*

3. In ITA No.151/Del/2013 the assessee has raised following two grounds of appeal:-

"1. *The Id. CIT(A)-XXIX, New Delhi has erred in law as well as on the facts and circumstances of the case in confirming the Transfer Pricing adjustment to the extent of Rs.71,99,984/-.*

2. *The Id. CIT(A)-XXIX, New Delhi has erred in law as well as on the facts and circumstances of the case in confirming the addition u/s 14A to the extent of Rs.1,50,670/-."*

4. Now we first take up the appeal of the revenue.

5. The brief fact of the case is that the assessee was incorporated as subsidiary of Gillette Group India Pvt. Ltd which is engaged in the business of manufacturing and trading of wide range of products for personal care and use. The major products line includes oral care products, hair epilating devices, electric shavers and other appliances. It is also engaged in the business of equipment leasing. For AY 2005-06 assessee filed return of income declaring NIL income on 27.10.2005. During the course of assessment year the assessee has undertaken following international transactions with its associated enterprises as under:-

S.No.	Description of transaction	Method	Value Qn Rs.)
1	Purchase of spares	TNMM	90,86,041
2	Export of finished goods	TNMM	19,02,35,076
3	Corporate support services	TNMM	21,64,000
4	Reimbursements		3401534

6. As the international transactions executed are more than prescribed amount the ld AO referred this matter to the Transfer Pricing Officer (TPO) for determining Arms Length Price.

7. For the purpose of determining arms length price the assessee has adopted transaction net marginal method (TNMM) and has identified a list of five independent companies as its comparables stating that functional profile of comparable are similar with functional profile of the assessee which is of distribution function. The assessee adopted financial data of three years to arrive at mean net profit margin of 3.21% and as the assessee's profit

margin itself is 2.77%, according to TP study report it falls within the tolerance limit $\pm 5\%$, hence stated that transaction entered into by the assessee with its associated enterprises (AE) are at arm's length.

8. Assessee in its T P study Report selected five comparables as under :-
 - i. Argus Cosmetic Ltd.
 - ii. Muller & Phipps India Ltd.
 - iii. Bajaj Consumer Care Ltd.
 - iv. J. K. Helene Curtis Ltd.
 - v. Marvel Hi-Tech Ltd.
9. Ld. TPO rejected comparables namely Argus Cosmetic Limited as the financial data for this company for the year 2005 was not available in the data base Prowess or Capitaline. The Ld. TPO also rejected another comparable of Muller and Phipps India Ltd because it has a negative net worth for the year 2005. Hence, out of five comparables selected by the assessee, ld. TPO rejected two comparables and compared the operating profit margin of the assessee with the operating profit margin of these three comparables. The ld TPO computed the average operating profit margin on sales of the three comparables at 1.09% whereas the assessee incurred a loss of 11.84% on sales, hence an adjustment of Rs. 28202588/- was made by computing the arm's length price of the transaction of Rs. 218437664/-. Against the ALP determined by the assessee of Rs.190235076/- The other international transactions of purchase of spares, Corporate Support services and reimbursement were accepted by the TPO as per TP study of the assessee.
10. On receipt of the order of TPO the AO passed order u/s 143(3) of the Act on 16th December 2008, wherein addition of Rs.28202588/- was made being difference between arms length price determined by the assessee and the TPO. The ld AO further made disallowance of Rs.2 lacs out of repairs and maintenance expenses, Rs.275259 on account of prior period expenses and Rs.1305474 u/s 14A of the Act.
11. The assessee being aggrieved with the order of the AO preferred an appeal before the ld CIT(A) raising against all the grounds of disallowance and additions. The ld CIT(A) deleted the disallowance of Rs.2 lacs on account of repairs and maintenance expenses, Rs. 275259/- on account of prior period expenses. Further out of disallowance of Rs. 13054474/- u/s 14A of the Act

ld. CIT(A) deleted the addition to the extent of Rs.1203804/-. On transfer pricing issues he upheld the rejection of two comparables of Argus Cosmetic Ltd. and Muller & Phipps India Ltd India Ltd. The ld CIT(A) further held that Corporate Support services income of Rs. 2187030/- and other sales of Rs.1214675/- was forming part of the total revenue for the purpose of calculation of PLI which has been excluded by TPO. Further he held that liabilities written back of provisions no longer required amounting to Rs. 5566871/- cannot be part of the operating revenue for the purpose of business activities of the assessee for the year under consideration. Further while calculating PLI TPO had excluded lease rental income from operational income but has not excluded corresponding expenses of lease while working out PLI. For this the ld CIT(A) held that depreciation amounting to Rs. 9877580/- pertaining to leased out asset should be excluded from the operating expenses. He further held that an amount of Rs. 6496093/- being repairs and maintenance expenses pertaining to leases asset should also be excluded from operating cost. The ld CIT (A) further held that loss on sale of fixed assets of Rs. 1037445/- which is in the nature of non operating expenses should also be excluded from the operating cost of the company. After all these adjustment the ld CIT(A) computed the PLI of the assessee by adopting operating profit/ cost at (-) 2.12%. He further held that as the TPO has computed the PLI OP/cost in respect of three comparables at 1.09% and benefit of tolerance range of $\pm 0.5\%$ is not available to the assessee, therefore he confirmed the upward adjustment to international transactions of the assessee of export of traded goods by Rs. 7899984/-.

12. Against this order of ld CIT(A) both the assessee and the revenue are in appeal.

Corporate tax Issues

13. The first two grounds of appeal of the revenue are against the deletion of addition of Rs.1203804/- u/s 14A of the Act on account of various expenditure.
14. The brief fact of the disallowance u/s 14A is that assessee earned dividend income of Rs.16827167/- and the assessee has disallowed expenses of Rs. 7497981/- for earning exempt income. The ld AO was of the view that the assessee has raised borrowed funds on which interest is being paid and on the other hand it has made investment in earning exempt income therefore

interest expenditure on proportionate basis should be disallowed. Regarding other expenditure the AO was of the view that the assessee has not considered many administrative expenses like common services expenses, legal and professional fees for working out disallowance. Therefore the ld. AO determined that out of gross total income 6.66% is dividend income which is exempt and applying the same ratio ld AO determined expenses allocable for earning dividend income amounting to Rs. 2155159/- out of total expenses of Rs. 32344581/-. Hence disallowance u/s 14A of the act offered by the assessee of Rs.799967/- was rejected and disallowance was worked out at Rs. 2155159/- thereby making further disallowance of Rs. 1354474/-. On appeal before the ld CIT(A) he upheld the disallowance of Rs.150670/- on account of proportionate interest and deleted the addition of Rs.1203804/- on account of various expenses holding that these expenses do not appear to be incurred in relation to earning of dividend income. Therefore, the revenue is in appeal before us against deletion of Rs.1203804/- being various expenses u/s 14A of the Act.

15. Before us, ld DR contended that all such expenses are part of the common expenses of the assessee and therefore the ld AO has rightly worked out disallowance. The ld DR further stated that legal and professional fees expenses were excluded by the assessee amounting to Rs. 3445078/- is not acceptable as these expenses are part of the profit and loss account.
16. Against this the ld AR submitted that the assessee has given detailed chart of total expenses incurred by assessee submitting reasons which expense are having nexus with the exempt income and which are not. that these expenses are whether they are having nexus with the dividend income or not. He also submitted that at Page 164 of the PB the assessee has given details of expenditure which are having any nexus in relation to exempt dividend income and they have been proportionately disallowed. It was his further submission that the assessee has not made any investment during the year therefore even otherwise there is no expenditure incurred during the year by the assessee.
17. We have carefully considered the rival contentions. Main grievance of ld. AO is that the ld CIT(A) has deleted the disallowance by holding that expenditure in the nature of legal and professional fees, travelling and conveyance, rent and insurance, common services expenses and other

miscellaneous expenses have been held to not having any nexus with the earning of dividend income. Before us the Id DR could not point out that rent and taxes, insurance etc could have any nexus with the dividend income earned where only expenditure which could reasonably be linked to earning is expenditure incurred for collection of dividend. It is to be noted that there is no investment made by assessee during the year therefore there cannot be any expenditure on legal and professional fees as well as common expenditure. Impugned appeal is for AY 2005-06 and in that year there was no prescribed methodology for disallowance of expenditure, therefore direct or indirect relationship between expenditure incurred and exempt income requires to be established for the purposes of disallowance. Ld DR could not point out any instances of expenditure which are excluded by appellant for disallowance showing that they are directly or indirectly related to earning of exempt income. In view of this we do not find any infirmity in the order of the Id CIT(A) in deleting the disallowance of Rs.12,03,804/- in respect of various expenditure. In the result the ground No.1 and 2 of the appeal of the revenue is dismissed.

18. Ground No.3 the concurrently we also take up the ground No.2 of the appeal of the assessee on the issue of confirmation of disallowance by Id CIT(A) on account of interest expenditure of Rs.1,50,670/-.
19. The Id AR submitted before us that while working out the disallowance u/s 14A of the Act the assessee has not disallowed any expenditure on account of interest because of the reason that no interest expenditure have been incurred for making an investment in the investment yielding tax free income. He submitted that the assessee has reserve and surplus of Rs. 1,36,15,29,740/- whereas the investment in tax free income earning assets made is Rs. 42,81,98,183/-. It shows that the interest free sources of funds available with the assessee were far more than the amount invested in tax free income yielding securities. He submitted that there is an error in the order of the Id CIT(A) in holding that it would have utilized the funds in more prudent ways as that cannot be the reasons for disallowance of interest u/s 14A of the Act. Therefore he submitted that interest disallowance of Rs.150670/- made by the AO and confirmed by Id CIT(A) u/s 14A of the act is erroneous.
20. Ld DR relied on the order of AO.

21. We have carefully considered the rival contentions. On perusal of the balance sheet of the appellant company it is apparent that assessee has its own interest free funds of Rs. 135.15 crore against investment made of only Rs. 482 crores, therefore the presumption should be available with the assessee that as funds invested in this investment is out of its interest free funds. For this hypothesis we draw support from the decision of Hon'ble Bombay High Court in the case of Reliance Utilities Ltd. Vs. CIT 313 ITR 340, wherein in Para 16 it has been held as under:-

"16. If there be interest-free funds available to an assessee sufficient to meet its investments and at the same time the assessee had raised a loan it can be presumed that the investments were from the interest-free funds available. In our opinion, the Supreme Court in East India Pharmaceutical Works Ltd. v. CIT [1997] [224 ITR 627](#) had the occasion to consider the decision of the Calcutta High Court in Woolcombers of India Ltd. [1982] [134 ITR 219](#) where a similar issue had arisen. Before the Supreme Court it was argued that it should have been presumed that in essence and true character the taxes were paid out of the profits of the relevant year and not out of the overdraft account for the running of the business and in these circumstances the appellant was entitled to claim the deductions. The Supreme Court noted that the argument had considerable force, but considering the fact that the contention had not been advanced earlier it did not require to be answered. It then noted that in Woolcombers of India Ltd.'s case [1982] [134 ITR 219](#) the Calcutta High Court had come to the conclusion that the profits were sufficient to meet the advance tax liability and the profits were deposited in the over draft account of the assessee and in such a case it should be presumed that the taxes were paid out of the profits of the year and not out of the overdraft account for the running of the business. It noted that to raise the presumption, there was sufficient material and the assessee had urged the contention before the High Court. The principle, therefore, would be that if there are funds available both interest-free and over draft and/or loans taken, then a presumption would arise that investments would be out of the interest-free fund generated or available with the company, if the interest-free funds were sufficient to meet the investments. In this case this presumption is established considering the finding of fact both by the Commissioner of Income-tax (Appeals) and the Income-tax Appellate Tribunal."

22. We also get support from Hon'ble Bombay High Court's decision in case of CIT v HDFC bank limited in 366 ITR 505 where identical view has been taken. In view of this, we reverse the decision of the Id. CIT (A) in confirming the disallowance of Rs.150670/- on account of interest expenditure u/s 14A

of the Income Tax Act. In the result ground No.2 of the appeal of assessee is allowed.

Transfer Pricing Issues.

23. Now we take up the ground NO.1 of the appeal of the assessee which is against the transfer pricing adjustment confirming to the extent of Rs.71,99,984/- by Id CIT(A) and we also decided simultaneously ground No.3 of the appeal of the revenue wherein revenue is against the relief of Rs.2,10,02,604/- granted by the Id CIT(A). The issues are concerning the rejection of one comparable by Id. TPO and confirmed by Id. CIT (A) and on concerning certain income and expenditure included in PLI of the assessee.

a) Rejection of comparables

24. Ld. TPO rejected two comparables which are discussed as under:-

a. Argus Cosmetic Ltd.

This company is functionally comparable, However assessee could not provide the relevant financial data available for the current data of the comparable. In view of this we confirm the order of the Id CIT(A) that if the current year data is not available this comparable has rightly been excluded by the TPO as well as the Id CIT(A).

b. Muller & Phipps India Ltd.

i. The Id TPO has excluded this comparable stating that it has a negative net worth for the year 2005 hence it is not fit comparable to be taken. On appeal before the Id CIT(A) the assessee submitted that the TP regulation and OECD guidelines do not suggest that loss making company should not be taken as comparable. The Id CIT (A) has hold that this company is not simply the loss making company but is also a company having negative net worth and according to him when a company suffers from erosion of its wealth because of continuous loss, same cannot be taken as comparable. The case laws relied upon by the appellant were also rejected as according to him those were relied upon high loss making company and not for a negative net worth comparables.

ii. Before us the Id AR submitted that merely because a company is having negative net worth it cannot be excluded as

comparable if the functions performed, Assets deployed and risk assumed are comparable with the business of the company. Against this the Id AR relied on the order of the lower authorities.

25. We have carefully considered the rival contentions. According to rule 10(B)(a) of the Income Tax Rules the comparability of international transactions with an uncontrolled transaction shall be judged with respect to the functions performed, taking into account assets employed or to be employed and the risks assumed, by the respective parties to the transactions. According to the Rule 10B(3) a uncontrolled transaction shall be comparable to an international transaction none of the differences, if any, 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. We do not find any such exception provided under the Income Tax Rules 1962. Furthermore neither the Id CIT(A) nor the Id AO had pointed out that how the negative net worth of the comparable make the price of the goods or the profitability arising from such transaction not comparable. Merely because the company is having negative net worth but when the FAR is comparable, it cannot be said to be non comparable unless it is shown that how the negative net worth of the company has impacted the profitability of the comparable company. We have also noted the issue decided by Special bench in the case of DCIT V Quark Systems Limited in 2010-TII-02-ITAT-CHD-SB-TP where in the negative net worth company was considered and it was held that business organization with negative net worth cannot be treated at par with a normal business organization. However while considering that issue the comparable was also functionally not comparable in that case. Therefore there was no view expressed in that decision that though comparable has similar FAR still negative net worth company is required to be excluded without showing the impact of negative net worth on the profitability of the company. In view of this we direct the inclusion of this Company i.e. Muller & Phipp India Limited as comparable for the purpose of determining arms length price.

b) Inclusion and exclusion of certain income/ expenses

26. The ld TPO while working out PLI has excluded the following income as non operating income.
- | | | |
|----|---|---------------|
| a. | Corporate Support Services | Rs. 2187030/- |
| b. | other sales | Rs. 1214675/- |
| c. | Liabilities no longer required return back | Rs. 5566871/- |
| d. | Profit on account of exchange rate fluctuation. | Rs. 2512001/- |
27. It was noted that while working out PLI of the company the ld TPO has only taken the sale figures of Rs. 215873267/-. However he has excluded items stated in schedule No.13 of the annual account of the company Where the assessee has stated that income from corporate support services amounting to Rs.2187030/-. Profit on foreign exchange fluctuation of Rs.2512001/- and other sales Rs.1214675/- and liabilities written back of Rs.5566871/- should be included as operating income. The ld CIT(A) agreed for inclusion of corporate support services of Rs 2187030/- and other sales of Rs. 1214675/- and foreign exchange gain of Rs 2512001/- As they are related to the distribution function of the assessee and are insignificant. Before us the ld AR submitted that ld CIT(A) has rightly excluded the Corporate Support services and other sales. Further the ld AR submitted that the ld CIT(A) has not held anything regarding the foreign exchange gain to be included in the operating income of the assessee. Regarding the provision no longer written back of Rs 5566871/- he relied on the order of the coordinate bench in ACIT Vs. Conexent Systems Pvt ltd 4359/Del/2009 dated 27.11.2015 and therefore he submitted that all the above four items should be included in working out PLI of the assessee. Against this the ld DR submitted that if Corporate support Service income are excluded in working out PLI then proportionate expenses should also be excluded. On the forex gain he submitted that safe Harbour rules also provided that foreign exchange gain and loss as well as provision written back should be excluded. In rejoinder the ld AR submitted that safe harbour rules are not manadatory but optional. He further submitted that the other sales are also operating income of the assessee.
28. We have carefully considered the rival contentions. We deal with the each of the issue as under :-

Other sales Rs 1214675/-

we do not find any reason that the ld TPO to exclude the other sales of Rs.1214675/- to be excluded while working out PLI. Against this no argument have been advanced by the ld DR that how the order of the ld CIT(A) is incorrect. In view of this we direct that other sales amounting to Rs. 1214675/-shall be included as operating income for working out PLI.

Corporate support service of Rs.2187030/-.

The ld TPO has excluded this sum without giving any reason and the ld CIT(A) has held that Corporate Support Services are aggregated with the distribution function of the assessee and are insignificant in volume therefore included as operating income of the assessee. Ld. DR has fairly agreed that if that income is to included as operating income then proportionate expenses are also required to be included as operating expenses. In our view there is no expenditure has been excluded pertaining to corporate support services. While working out the entity level PLO in case of TNMM method we are of the view that the Corporate Support service income should be included as operating income and therefore we do not find any infirmity in the order of the ld CIT(A).

Liabilities No Longer required written back Rs 5566871/-

This amount has been excluded by the ld TPO without assigning any reason the ld CIT(A) has confirmed his view as it is an extraordinary item. Argument of the ld DR that safe harbour rules also provides for not considering it as operating income. We are of the view that safe harbour rules is optional and if the assessee has opted then only he has covered by it otherwise not. Therefore in the present case the assessee cannot precluded from stating that provision returned back written form part of the operating revenue. Against this the assessee has relied on the decision of the co-ordinate bench of ITAT wherein it has been held that provisions written back should be considered as operative income and provision created during the year should be treated as operative expenditure is normal business activity of business operation. In view of the decision of the coordinate bench we are of the view that provisions no longer required written back of Rs. 5566871/- is to be excluded if the assessee makes the provision and also reverses it as a normal business activity. Further if it is on account of revenue nature it should be included. However if the

liabilities originally created are on account of capital items then their write back cannot be a normal instances of the business and hence to be excluded as operating income. As the fact for such write back are not available on record we set aside this issue to the file of the Ld. AO/ TPO to examine as per above direction and decide the issue afresh. Needless to say that the assessee may be provided reasonable opportunity for providing these details.

Profit on account of foreign exchange on 2512001/ Repairs and maintance expense

This amount has not been considered as operating income by ld. TPO and CIT (A) has not given any finding on the same. It is submitted before us that that such foreign exchange fluctuation has arisen out of trading operation of the assessee on which PLI has been determined. Identically the ld DR object for this inclusion stating that safeharbour rules does not provide inclusion of this item.

We have carefully considered this issue. We are of the view that foreign exchange gain if it is arising out of sales of goods that it should form part of the operating income of the assessee. It was submitted that Forex gain has arisen on account of export of goods. Ld. TPO as well as ld. CIT (A) has not considered this issue and therefore we set aside it to the file of ld. TPO to deal with this issue on merit after giving proper opportunity of hearing to the assessee.

Order pronounced in the open court on 01/04/2016.

-Sd/-

**(I.C.SUDHIR)
JUDICIAL MEMBER**

-Sd/-

**(PRASHANT MAHARISHI)
ACCOUNTANT MEMBER**

Dated:01/04/2016
A K Keot

Copy forwarded to

1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR
ITAT, New Delhi