आयकर अपीलीय अधिकरण, 'डी' न्यायपीठ, चेन्नई

IN THE INCOME TAX APPELLATE TRIBUNAL
' D' BENCH : CHENNAI

श्री चंद्र पूजारी, लेखा सदस्य एवं श्री
जी. पवन कुमार **न्यायिक सदस्य के समक्ष**

BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER AND SHRI G.PAVAN KUMAR, JUDICIAL MEMBER

आयकर अपील सं./I.T.A.No.2575/Mds./2016
निर्धारण वर्ष /Assessment year :2012-13

M/s. Control Techniques India Pvt Ltd., 117-B,Developed PlotsEstate, Perungudi, Chennai. **[PAN** AAACC 1343 B**]** **(अपीलार्थी/Appellant)**	**Vs.**	The JCIT, Corporate Circle 1(2), Chennai. **(प्रत्यर्थी/Respondent)**

अपीलार्थी की ओर से/ Appellant by	**:**	Mr.Sriram Seshadri C.A Mr.Ashok Shah, C.A
प्रत्यर्थी की ओर से /Respondent by	**:**	Mr.Vivekandandan, CIT,D.R
सुनवाई की तारीख/Date of Hearing	**:**	26-10-2016
घोषणा की तारीख /Date of Pronouncement	**:**	16-12-2016

आदेश / O R D E R

PER CHANDRA POOJARI, ACCOUNTANT MEMBER

This appeal of the assessee are directed against Assessment orders dated 30.06.2016 for A.Y 2012-13, consequent to the directions of the Dispute Resolution Panel-2 (DRP), Bangalore, dated 31.05.2016 u/s. 143(3) r.w.s.144C(1) of the Act.

2. The only issue for our consideration is with regard to Transfer Pricing (T.P) adjustments of ₹78,57,058/- towards "management services".

3. The facts of the case are that the assessee company, i.e. M/s.Control Techniques India Pvt Ltd. is a wholly owned subsidiary of Control Techniques Ltd., United Kingdom(CTL, UK). The assessee company is engaged in the business of manufacturing drives and control applications which are used in controlling speed, voltage etc., and has application in offset printer machines, newspaper printing machines, cement plates, textile industries etc. The Control Techniques Group is involved in the business of electronic control, variable speed and servo drive systems and helps in savings of electricity. In this case, T.P adjustments of ₹78,57,058/- has been made in respect of payments made by the assessee to the Associated Enterprise (A.E). Ld. TPO has segregated certain transactions and applied CUP method for purposes of determining ALP, the issue has been dealt in detail by the TPO in his order wherein he have duly examined the objections raised by the assessee and he has given reasons for not accepting the same. TPO has taken guidance from OECD guidelines in para 1.42 which require that ALP should be applied on a transaction by transaction basis for arriving at the most precise approximation of fair market value. According to DRP, it is very

clear from the TPO's order that the services were either in nature of stewardship services or the assessee failed to substantiate its claim that there services were actually received by it. Further, the assessee's contention is that there was not any motive to shift profits outside India. DRP observed that the transfer pricing rules shall apply when one of the parties to the transaction is a non-resident, even if the transaction takes place within India. Existence of actual cross border transactions or motive to shift profits outside India or to evade taxes are not preconditions for transfer pricing provisions to apply. According to DRP, the authorities, during transfer pricing assessment, are not required to demonstrate the motive of the assessee company to shift the profits outside India by manipulating the prices. Hence, the DRP did not accept the assessee's contention.

3.1 According to DRP, the TPO has examined the agreements entered into by the assessee with its AE as well as the email correspondence between them, but he found that the activities for whichpayments had been made were in the nature of stewardship only and thus do not require to be remunerated separately. The TPO has discussed in detail the nature of various services, claimed to have been received by the assessee from its AE. However, the important fact is that the assessee failed to produce any document to substantiate its claim that many of these services were actually rendered by the AE to it. Wherever necessary details were provided, no adjustment has been made by the TPO. It is not the stand of the TPO that

assessee should not have taken these services or in other words TPO is not challenging as to how the assessee runs or wants to run its business but TPO just wants the assessëe to show that the services were actually rendered and the payment made for the same were at arm's length e.g. the assessee has incurred an expenditure of 49,26,678/- as legal and professional charges to various independent parties but at the same time it is paying to AE for similar purposes without bringing anything on record to show as to how, when and for what purpose the same were rendered. Another example of the same is that the invoices submitted by the assessee pertain to fees country with hardly anything to show as to how the assessee benefitted from the same in his consideration. During proceedings before this Panel too, assessee failed to substantiate its claim that such services were actually received or that the services were not in the nature of stewardship services The claim of the assessee that by asking it to substantiate its entire claim of expenditure, it is being put to undue hardship, can also not be accepted for the reason that if the assessee wants to claim that it has received some services and that the same were at arm's length, then onus is on it to prove the same. Of the total expenses of Rs 1,41,48,355/- the assessee failed to substantiate in relation to an amount of Rs 78,57,058/-, which is more than 55% of' the total payment in relation to such services. So assessee cannot run away from the onus cast on it to prove that these services were actually received by it. Before DRP, the assessee's claim (and later in written submissions dt 25 May 2016) that it has not documented its entire communication in relation to services received

by it. Hence, DRP observed that as the onus was on the assessee to maintain sufficient records to prove its claim before the tax above, this Panel does not find any merits in the objections of the assessee and rejected the assessee's claim. Consequently, the AO passed the final order. Against this, the assessee is in appeal before us.

4. We have heard both the parties and perused the material on record. The main plea of the assessee is that the TPO analyses the assessee's profitability and arrived operation margins of the assessee at 13.96% as against the arithmetic mean of the operating margin of 13 comparables at 7.02%. After testing that the operating margin of the assessee is on higher side, he stepped into the bench marked the management services fee by applying the CUP method overwhelming that TNMM is not mot appropriate method. According to him, the TPO is not an Assessing Officer and he is concerned with only in respect of T.P adjustments and he cannot have jurisdiction to decide allowability of expenditure u/s.37 of the Act. Further, he relied on the judgement of Hyderabad Tribunal in the case of DCIT Vs. M/s.Air Liquid Engineering in ITANo.1040/Hyd./2011 & others vide order dated 13.02.2014 wherein held that:-

> *20. Furthermore, we are of the opinion that once TNMM has been applied to the assessee company's transaction, it covers under its ambit the Royalty transactions in question too and hence separate analaysis and consequent deletion of the Royalty payments by the TPO in the instant case seems erroneous. We draw support from the Hon'ble Mumbai ITAT decision, Cadbury*

India Ltd. vs. ACIT (ITA No 7408/Mum/2010 and ITA No.7641/Mum/2010 dated 13-11-2013) wherein the Hon'ble ITAT upheld the use of TNMM for Royalty as well as relied on many of the above decisions to hold adjustment by TPO was erroneous:

> *"33. The TPO has made the disallowance in question mainly on the basis of the benefit test. In this regard, it is seen that the payment of royalty cannot be examined divorced from the production and sales. Royalty is inextricably linked with these activities. In the absence of production and sale of products, there would be no question arising regarding payment of any royalty. Rule 1 OA(d) of the ITAT Rules defines 'transaction' as a number of closely linked transactions. Royalty, then, is a transaction closely linked with production and sales. ft cannot be segregated from these activities of an enterprise, being embedded therein. That being so, royalty cafinot be considered and examined in isolation on a standalone basis. Royalty is to be calculated on a specified agreed basis, on determining the net sales which, in the present case, are required to be determined after excluding the amounts of standard bought out components, etc., since such net sales do not stand recorded by the assessee in its books of account. Therefore, it is our considered opinion that the assessee was correct in employing an overall TNMM for examining the royalty. The TPO worked out the dzfference in the PU of the outside party (the assessee) at 4.09% and the comparables at 7.05%. This has not been shown to fall outside the permissible range.*
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> *34. The decision of the Tribunal in 'Ekla Appliances', 2012-TH-01-HCDe1- TP, has been sought to be distinguished by the TPO, observing that the facts in that case are not in pan matena with those of the assessee's case. However, therein also, the benefit test had been applied by the TPO, as in the present case. The matter was carried in appeal before the Hon'ble High Court. The Hon'ble Delhi High Court has held that the so-called benefit test cannot be applied to determine the ALP of royalty payment at nil and that the TPO could apply only one of the methods prescribed under the law. A similar view has been taken in 'Sona Okegawa Precision Forgings Ltd.' (supra) and in 'KHS Machinery Pvt. Ltd. vs. ITO', 53 SOT 100 (Ahm) (URO).*
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> *35. It is, thus, seen that the royalty payment @ 3% by the assessee is at arm's length. The Technical*

Collaboration Agreement stands approved by the Government of India. The royalty payment has been accepted by the department as having been made by the assessee wholly and exclusively for its business purposes. For Assessment Years 2004-05 and 2005-06, such payment of royalty has been allowed by the CIT (A). As per the FEMA Regulations, royalty can be paid on net sales @ 5% on domestic sales and @ 8% on export sales. The royalty payment by the assessee falls within these limits. ft also falls within the limits of payment of royalty in the auto mobile sector, as per the market trend. This payment of royalty is at the same percentage as that paid by other auto ancillaries in the automotive industry. Then, in 'Ekia Appliances' (supra) and in 'Ericsson India Pvt. Ltd. vs. DCIT', 2012-TII-48-ITAT-Del-TP, it has been held that royalty payment cannot be disallowed on the basis of the so-called benefit test and the domain of the TPO is only to examine as to whether the payment based on the agreement adheres to the arm's length principle or not. That being so, the action of the TPO in the present case, to make the disallowance mainly on the ground of the benefit test, is unsustainable in law.

36. Keeping in view all the above factors, the disallowance made on account of royalty is found to be totally uncalled for and it is deleted as such. ... ".

21. Hence, following the ratio of the Honb'le Delhi High Court in CIT vs. EKL Appliances (supra) and various other decisions as noted above and given the facts and circumstances of the instant case, we hold that the addition made by the TPO and upheld by the DRP is unsustainable and is to be deleted. Hence Ground No. 2 is held in favour of the assessee. Hence, the appeal of the Revenue ITA.No.1040/Hyd/2011 is dismissed and Assessee's appeal in ITA.No.1159/Hyd/2011 is allowed."

5. Further, he drew our attention to case of CIT Vs. EKL APPLIANCES LTD.in [2012] 345 ITR 241 (Del) wherein the Hon'ble Delhi High Court had occasion to consider an issue of disallowance of royalty by TPO because the assessee in that case had been suffering losses; the Delhi High Court, while holding that so long as the expenditure or payment by assessee has been demonstrated to have been incurred or laid out for the purpose of business, it is no concern of the TPO to disallow the same on any extraneous reasoning. Thus, according to the ld.A.R, the AO has no jurisdiction to nullify the transaction, when the expenditure was incurred for the purpose of business and operating margin of assessee higher than the arithmetic mean of the operating margin of the comparables. In principle, we agree with the argument of the ld.A.R. However, we find from the order of lower authorities that TPO wanted the assessee to show that services were actually rendered to the assessee and payment was made for the same, also it was noted by the DRP that the invoices submitted by the assessee pertaining to the fees paid by the assessee to its AE for registration of patents developed by AE in their own country with hardly anything to show as to how the assessee benefitted from the same in its business. Similarly, in relation to invoice for MIS, the same had been pertained to the year under consideration and assessee failed to substantiate its claim of service were actually received or that services are not in nature of stewardship services. Further, DRP observed that the TPO had discussed in detail the nature of various services, claimed to have been received the assessee from its A.E. Hence, the DRP directed the AO for disallowance of ₹78,57,058/-. In our opinion, if the

assessee produces the particulars of actual expenditure for availing these services, then it is to be allowed. With this observation, we remit the issue to the file of AO for fresh consideration.

6. In the result, the appeal of the assessee is partly allowed for statistical purposes.

Order pronounced on 16th December, 2016, at Chennai.

Sd/-	Sd/-
(जी. पवन कुमार)	**(चंद्र पूजारी)**
(G.PAVAN KUMAR)	**(CHANDRA POOJARI)**
न्यायिक सदस्य/JUDICIAL MEMBER	**लेखा सदस्य /ACCOUNTANT MEMBER**

चेन्नई/Chennai
दिनांक/Dated: 16th December, 2016
K S Sundaram

आदेश की प्रतिलिपि अग्रेषित/Copy to:

1. अपीलार्थी/Appellant
2. प्रत्यर्थी/Respondent
3. आयकर आयुक्त (अपील)/CIT(A)
4. आयकर आयुक्त/CIT
5. विभागीय प्रतिनिधि/DR
6. गार्ड फाईल/GF