IN THE INCOME TAX APPELLATE TRIBUNAL
"B" BENCH : BANGALORE

BEFORE SHRI SUNIL KUMAR YADAV, JUDICIAL MEMBER AND
SHRI INTURI RAMA RAO, ACCOUNTANT MEMBER

1. IT (TP) A No. 159/Bang/2015
Assessment Year: 2010-11

2. IT (TP) A No. 132/Bang/2016
Assessment Year: 2011-12

3. IT (TP) A No. 86/Bang/2017
Assessment Year: 2012-13

M/s. Kaypee Electronics & Associates Pvt. Ltd.,
18/2, Srinivasa Industrial Estate,
7th Mile, Kanakapura Main Road,
Konanakunte Cross, Next to Metro,
Bangalore – 560 062.
PAN: AACCK 1203C **.....Appellant**

Vs.

1. The Deputy Commissioner of Income Tax,
Circle – 4(1)(1),
Bangalore.

2. The Deputy Commissioner of Income Tax,
Circle – 4(1)1),
Bangalore.

3. The Assistant Commissioner of Income Tax,
Circle – 4(1)(1),
Bangalore. **..... Respondents**

Appellant by	:	Shri Chythanya K.K., Advocate
Respondent by	:	Shri G. Kamaladhar, Standing Counsel

Date of hearing	:	23.03.2017
Date of Pronouncement	:	21.04.2017

O R D E R

Per SHRI INTURI RAMA RAO, AM:

These are appeals filed by the assessee-company directed against the assessment orders dated 24.12.2014, 17.12.2015 and 30.11.2016 for the assessment years 2010-11, 2011-12 and 2012-13 respectively u/s. 143(3) r.w.s. 144C of the Act by the Deputy Commissioner of Income-tax / Assistant Commissioner of Income-tax, Circle-4(1)(1), Bangalore.

2. Since the common issue is involved in all the three appeals, we proceed to dispose of same vide this common order. The facts relevant to the assessment year 2010-11 are stated herein for the sake of clarity and convenience.

3. The assessee-company raised the following grounds for the year 2010-11.

A. The Order of the Learned DCIT is not justified in law and on facts and circumstances of the case.

B. The Honourable DRP is not justified in dismissing the objections of the Appellant in an arbitrary manner, without appreciating the contentions of the Appellant and without application of mind and by failing to note that the Learned TPO has passed a stereotyped order.

C. As regards rejecting information and document (TP Document) maintained by the Appellant in accordance with the provisions of section 92D of the IT Act:

1. The Honourable DRP is not justified in upholding the action of the Learned TPO in invoking the provisions of section 92C (3) of the IT Act without satisfying the conditions therein by making extraneous reasoning based on section 92CA(1).

2. The Honourable DRP is not justified, in impliedly upholding the action of the Learned TPO in perversely stating that the Appellant's data are not reliable or correct when he himself has used the very same data for the purpose of making adjustment in respect of payment of royalty and in failing to appreciate that the Learned TPO re-determined ALP even without substantiating as to how and why the Appellant's data are not reliable or correct.

3. The Honourable DRP is not justified in impliedly upholding the action of the Learned TPO in stating that the data are not reliable or

correct without even requiring the Appellant to show cause on this issue.

D. As regards adjustment of Rs. 2,75,25,270/- directed under Section 92CA of the IT Act in respect of Royalty paid to Associated Enterprises:

1. The Honourable DRP is not justified in upholding the action of the Learned TPO in making adjustment of Rs.2,75,25,270/- under Section 92CA of the IT Act in respect of international transaction by way of royalty paid by the Appellant Company.

2. The Honourable DRP is not justified in impliedly upholding the action of the Learned TPO in making adjustment in breach of statutory provisions of Chapter X and Rules provided therein.

3. The Honourable DRP has failed to appreciate that the Learned TPO computed an adjustment of Rs.2,75,25,270/- under Section 92CA of IT Act without even determining arm's length price.

4. The Honourable DRP has failed to appreciate that when the Learned TPO has accepted the ALP determined by Appellant under TNMM in respect of all international transactions including payment of royalty at the enterprise level, the Learned TPO ought not to have made any adjustment in respect of royalty payment separately.

5. Without prejudice to the above, the Honourable DRP & the Learned TPO having accepted the collaboration agreement entered into by the Appellant in all respects including rate of royalty, the Honourable DRP is not justified in disregarding the basis (i.e. fixed % on sales) on which the payment of royalty is agreed between the parties.

6. The Honourable DRP is not justified in failing to appreciate that the basis (i.e. fixed % on sales) on which the payment of royalty is agreed between the parties is the sole prerogative of the Appellant, and neither the TPO nor the Assessing Officer has any role in this regard. Further, the Honourable DRP has failed to appreciate that the legitimate business needs of the Appellant cannot be dictated by the revenue authorities.

7. The Honourable DRP having specifically noted that '*the assessee has entered into a collaboration with "Falco" for manufacturing electronic components by using technology, expertise and knowhow of Falco and marketing and selling components under the brand name of Falco in India as well as abroad*', is not justified in upholding the action of the Learned TPO in stating that the royalty paid is only in respect of technical know-how and not in respect of use of brand name and other marketing support.

8. The Honourable DRP is not justified in impliedly upholding the action of the Learned TPO in comparing the case of the Appellant with that of Toyota Motors without bringing on record as to how the latter could ever be called as comparable company particularly when such company is not one of the comparable companies chosen by the Appellant and accepted by the Learned TPO in the TNMM study carried out by the Appellant, when such company failed the test of RPT filter and without countering the Appellant and giving an opportunity to the Appellant to distinguish its case.

9. The Honourable DRP is not justified in impliedly upholding the action of the Learned TPO in failing to appreciate that the payment of royalty by the Appellant to Falco is suffering tax in the hands of Falco on gross basis thereby meaning no flight of tax base so as to warrant addition on account of transfer pricing.

E. As regards exclusion of freight expense of Rs. 28,66,311/- and insurance expenses of Rs. 79,916/- from the export turnover:

The Learned Assessing Officer is not justified in failing to follow the directions of the Honourable DRP as per the mandate under section 144C (13) of the IT Act, when the Honourable DRP has explicitly directed in para 5.2 that the freight expense of Rs.28,66,311/- and insurance expenses of Rs. 79,916/- shall not be excluded from the export turnover when the said expenses are incurred in Indian Rupee.

F. The Honourable DRP is not justified in upholding the levy of interest under sections 234B & 234C of IT Act when the conditions for levying such interest did not exist in the present case.

For the above reasons and for such other reasons which may be allowed by the Honourable Members to be urged at the time of hearing, it is prayed that the aforesaid appeal be allowed.

4. Briefly the facts of the case are that the appellant is a company incorporated under the provisions of the Companies Act, 1956. It is engaged in the business of manufacturing of Magnetic based Electronic Coils, transformers and inductors. It is a subsidiary of M/s. Falco Limited, Hongkong. The return of income for the assessment year 2010-11 was filed on 29.08.2010 declaring a total income of Rs. 6,21,81,210/-. The 80% of equity capital of the appellant is held by the said M/s. Falco Limited. The appellant also entered into Technology Collaboration agreement with M/s. Falco Limited on 29.03.2006 for manufacturing electronic components by using technology, expertise and knowhow of Falco and marketing and selling components under the brand name of

Falco in India as well as abroad. In terms of the said Technology Collaboration Agreement, the appellant was to pay royalty at the rate of 8% on the sales to said M/s. Falco Limited in consideration of technology and Knowhow including technical assistance made available to the appellant company.

5. The appellant company also reported the following international transactions in its Form 3CEB.

Description of the International Transaction	Amount (Rs.)
Purchase of raw materials	20,25,51,853/-
Sales	9,19,13,597/-
Purchase of fixed assets	16,18,591/-
Payment of Royalty	4,39,93,839/-

6. The appellant company sought to justify that the above international transaction arms length price and for this purpose the assessee's company submitted a TP study report. For the purpose of this TP study report the assessee company adopted TNMM method.

7. The AO had referred the matter to the TPO for the purpose of bench marking the above international transactions. The TPO vide order dated 30.01.2014 passed u/s. 92CA of the IT Act, determined the ALP in respect of the royalty at Rs. 2,75,25,270/-. According to the ld. TPO, the appellant was not justified in paying royalty at the rate of 8% on sales as there was no value addition made from the AE; it is the contention of the ld. TPO that if the royalty is paid on gross sales it amounts to paying the royalty on the purchases made by the AE also.

Thus the TPO determined the ALP adjustment in payment of royalty as follows.

10. Determination of Arm's Length Price:

10.1 The Arm's Length Price of the international transaction of Payment of Royalty is therefore determined as under:

Particulars	Amount
Gross Sales of the Assessee Company	Rs 55,51,87,248/-
Material Cost	Rs 34,93,30,137/-
Value addition due to operations using Technology and knowhow leased out by the AE M/s. Falco Ltd.	Rs 20,58,57,111/-
Royalty payable @ 8 percent on value addition	Rs 1,64,68,568/-
The Royalty paid by the Assessee Company	Rs 4,39,93,839/-
Therefore the excess Royalty paid by the Assessee Company being adjustment u/s 92CA	Rs 2,75,25,270/-

8. The AO passed the draft assessment order u/s. 143(3) r.w.s. 144C of the IT Act vide order dated 28.02.2014 after incorporating the above TP adjustment. After receipt of draft assessment order the appellant company filed an objection before the Hon'ble DRP contending that the TPO was not justified in rejecting the TP study and further contended that when the appellant company adopted the TNMM at entity level including payment of royalty, there was no need of separate bench marking in respect of royalty payment. It was further contented that the royalty is paid to M/s. Falco Limited for the use of brand name also. The Hon'ble DRP after considering the submissions of the assessee-company had confirmed the findings of the TPO vide directions dated 13.11.2014. The AO passed the final assessment order u/s. 143(3) r.w.s. 144C of the Act vide order dated 24.12.2014. Being aggrieved, the appellant is before us in the present appeals raising the following grounds of appeal.

9. During the course of hearing of the appeal the ld. Counsel Shri Chythanya K.K. for the appellant submitted that when the TPO accepted the TNMM method at entity level there was no need of making a separate bench marking in respect of royalty payment. In this connection, he placed reliance on the decision of Hon'ble Delhi High Court in case of Sony Ericsson Mobile Communications India Pvt. Ltd. Vs. CIT 231 taxman 113(Delhi) coordinate bench decision of the Tribunal in the case of M/s. Siemens VDO Automotive Ltd. Vs DCIT in IT(TP)A No. 923/Bang/2012. Thus he submitted that when TPO has accepted the TNMM method at entity level, there was no need of separate bench marking in respect of royalty payment.

10. On the other hand, the ld. standing counsel placed reliance on the orders of the authorities.

11. We heard the rival submissions and perused the material on record. In the present case, the only issue that arises for consideration before us is whether the TPO was justified in making the ALP adjustment in respect of royalty payment made to M/s. Falco Limited in the given facts of the present case. The royalty payment is made to M/s. Falco Limited for manufacturing electronic components by using technology, expertise and knowhow of Falco and marketing and selling components under the brand name of Falco in India as well as abroad by the assessee-company. In consideration of same, royalty at the rate of 8% of sales was made by the appellant to M/s. Falco Limited. No doubt the law is settled to the extent that an international transaction can be clubbed / aggregated with other international transactions provided such

transactions are closely connected with each other. In the cases cited by the ld. counsel for the appellant, this proposition of law was reiterated. But in the present case, the TPO had not applied TNMM at entity level. The TP study report submitted by the assessee company had been rejected by the TPO. This action of the TPO is confirmed by the Hon'ble DRP. But the TPO proceeded to bench mark the transaction of the royalty payment on stand alone basis. In the process, the cost of production or other transactions are not subjected to bench marking by the TPO. Therefore the contention of the ld. counsel that when the TNMM was applied at the entity level, there was no necessity of separate bench marking in respect of royalty transactions cannot be accepted. This submission made by the assessee-company is factually incorrect. On mere perusal of order of the ld. TPO it is manifest that the TPO had picked up the transaction royalty alone for the purpose of bench marking. The statement made by the ld. Counsel for the appellant is nothing but attempt to mislead the court. This conduct on the part of the counsel is highly deplorable. It is a fundamental duty of an advocate / counsel to assist the court in adjudicating the matter before the court in accordance with the law. It is highly unbecoming of counsel to mislead the court. We leave the issue here with these observations.

12. Now on the issue of bench marking the transaction of royalty the ld. counsel chosen not to point out any fallacies in the reasoning of the TPO or of the ALP analysis in the working of the ALP adjustment. The ld. counsel also failed to establish that the transaction royalty payment is closely linked with the other transactions carried out with AE. It is trite

law that a justification should be shown for clubbing the transactions. In the absence of such justification clubbing other transactions is not possible. The onus always lies on the assessee-company to establish the justification for clubbing and aggregation of the transaction of payment of royalty with other transactions. As mentioned (supra) the assessee-company had failed to discharge such onus, in the circumstances we confirm the orders of the lower authorities in this respect of ALP adjustment on payment of royalty.

13. In the result, the grounds of appeal filed by the assessee-company challenging addition of ALP adjustment on account of royalty payment are dismissed for all the three years.

14. In assessment years 2010-11 and 2011-12 in IT(TP) Nos. 159/Bang/2015 and 132/Bang/2016 the other grounds of appeal relates to the reduction of the expenditure incurred under telecommunication freight and travelling incurred in foreign currency from export turnover. This issue is covered in favour of the assessee-company by the decision of the jurisdictional High court in case of Tata Elxsi Ltd 349 ITR 98. Respectfully following the decision of the order we direct the AO / TPO to exclude the expenditure from both export turnover and total turnover. These grounds of the appeal are allowed.

15. In the result, the appeal for assessment years 2010-11 and 2011-12 are partly allowed and for the assessment year 2012-13 the appeal filed by the assessee is dismissed.

Pronounced in the open court on this 21st day of April, 2017

Sd/-	Sd/-
(SUNIL KUMAR YADAV)	**(INTURI RAMA RAO)**
JUDICIAL MEMBER	**ACCOUNTANT MEMBER**

Bangalore,
Dated, the 21st April, 2017.

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Copy to:
1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore.
6. Guard file

By order

Assistant Registrar,
ITAT, Bangalore.