IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH: 'I-2' NEW DELHI

BEFORE SHRI N. K. SAINI, ACCOUNTANT MEMBER
AND
MS SUCHITRA KAMBLE, JUDICIAL MEMBER

I.T.A .No. 6287/DEL/2012 (A.Y .2007-08)

DCIT Circle-11(1) New Delhi **(APPELLANT)**	Vs	Itochu India (P) Ltd. Ground Floor, World Trade Tower, Barakhamba Lane New Delhi AABCI4829F **(RESPONDENT)**

I.T.A .No. 6288/DEL/2012 (A.Y .2008-09)

DCIT Circle-11(1) New Delhi **(APPELLANT)**	Vs	Itochu India (P) Ltd. Ground Floor, World Trade Tower, Barakhamba Lane New Delhi AABCI4829F **(RESPONDENT)**

Appellant by	**Sh. Vishal Kalra, Adv & Ms. Reena Malik, CA**
Respondent by	**Sh. Sanjay Kumar Yadav, Sr. DR & Sh. T. M. Shiv Kumar, CIT DR**

Date of Hearing	**12.07.2017**
Date of Pronouncement	**18.08.2017**

ORDER

PER BENCH

These appeals are filed by the Revenue against the order dated 30/10/2012 passed by CIT(A)-XX, New Delhi for Assessment Year 2007-08 & 2008-09 respectively.

2. The grounds of appeal are as under:-

(ITA No. 6287/Del/2012)

1. *On the facts and circumstances of the case and in law, the Ld.CIT(A) has erred in deleting the addition of Rs.6,53,22,520/- made on account of Arm's Length Price.*

2. *The appellant craves leave to add, alter or amend any ground of appeal raised above at the time of hearing*

It is prayed that the ord4er of the ld-XX being contrary to the facts on record and the settled position of law, be set aside and that of the Assessing Officer be restored.

(ITA No. 6288/Del/2012)

1. *On the facts and circumstances of the case and in law, the Ld.CIT(A) has erred in deleting the addition of Rs.9,69,43,894/-/- made on account of Arm's Length Price.*

2. *The appellant craves leave to add, alter or amend any ground of appeal raised above at the time of hearing.*

   It is prayed that the ord4er of the ld-XX being contrary to the facts on record and the settled position of law, be set aside and that of the Assessing Officer be restored.

3. The assessee is, inter alia, engaged in rendering business support services to its associated enterprises ("AEs") Sogo Shosha group entities. The assessee renders the following services:

a) Arranging meetings with prospective customers;

b) Interacting with various government officials, industry specialists, potential customers, etc;

c) Providing information to its AEs pertaining to economic, commercial and industrial data, customs and procedures, business trends, market conditions, etc; and

d) Arranging for feasibility studies, industry analysis, and project evaluation for potential projects identified by the AEs.

Sogo Shosha means general trading companies. It is a form of industrial organization, a kind of vertically integrated trading companies in Japan. Sogo Shosha structures are companies with interlocking ownerships, dealing in all products. These structure transact in huge volumes, however, operate on thin margins. Sogo Shosha structures also have direct subsidiaries which specialize in certain types of business, such as rendering of business support services. The Assessee functions as a support service provider to the Sogo Shosha companies and support them procure goods from lndia. The Assessee locates potential local vendors or suppliers and passes the relevant information in relation to the same to its AEs, which then perform the decision making and purchase valuation functions. Further, the Assessee forwards the bid documents to the vendors, if such bid is accepted then the AEs enter into a purchase transaction with the vendor. Post the purchase of goods from suppliers, the AEs identify potential customers for goods purchased from the vendors and sells the same to third party customers. The Assessee's functions are limited to identifying the prospective sellers in India. The Assessee's approach at the time of Transfer Pricing (TP) Documentation:

	A.Y 2007-08	A.Y 2008-09
Value of transactions (INR) :	13,48,00,480	15,32,52,830
Method adopted for benchmarking	Transaction Net Margin Method("TNMM")	TNMM
Profit Level indicator	Net operating profit Margin on cost ("NCP")	NCP
No. of comparables	13	15

NCP of comparables after		
Using multiple year data	15.29%	15.28%
NCP of Assessee	11.91%	123.52%

The Transfer Pricing Officer ("TPO") re-characterized the business profile of the Assessee from a business support service provider to a trader. The TPO included the free-on board ("FOB") value of goods sourced from India in the operating cost of the assessee to compute the NCP. The TPO rejected the analysis undertaken by the assessee in the TP documentation and conducted a fresh search to identify trading companies as comparables to the alleged trading activity of the assessee. The TPO multiplied the FOB value of goods sourced with the arithmetic mean of the margin of comparables. From the amount arrived, the revenue earned by the assessee by rendering business support services to its AEs was subtracted to compute the adjustment. Thus, there was TP Adjustment are Rs. 6,53,22,520/- for A.Y. 2007-08 and Rs. 9,69,43,894/- for A.Y. 2008-09

4. Being aggrieved by the TPO/AOs order, the assessee filed appeal before the CIT(A). The CIT(A), vide order dated October 30, 2012 for AY 2007-08 and 2008-09 held that the Assessee is engaged in the business of rendering business support services and is not a trader. Further, relying on the order of the ITAT in case of GAP International Sourcing India Private limited (ITA No. 5147/Del-2011 and 228/Del-2012), the CIT(A) held that the FOB value of goods sourced by AEs cannot be included in the cost of the Assessee. The CIT(A) also upheld the use of comparables selected by the Assessee in its TP documentation. The CIT(A) held that the international transactions were at arm's length since the margin of the Assessee computed at 110.91% and 123.52% respectively for the AYs were higher than the mean margins of the comparables with current year data, submitted before the TPO by the Assessee, which were 16.91% (for AY 2007-08) and 15.24% (for AY 2008-09). Now the department is in appeal.

5. The Ld. DR relied upon the orders of the TPO & the AO and submitted that the TPO rightly held that the business profile of assessee is a trader and not that of business support service provider. The Ld. DR further submitted that the TPO has rightly made an adjustment of Rs. 9,69,43,894/- in relation to the international transactions entered into by the assessee. The Ld. DR further submitted that the TPO rightly rejected the Transfer Pricing Analysis undertaken by the Assessee and made addition to the income of the assessee by including the FOB price of the goods sourced by the assessee's AE in the operating cost of the assessee while computing operating margins of the assessee. The Ld. DR further submitted that the CIT(A) erred in deleting the addition on account of Arms' Length Price.

6. The Ld. AR furnished a chart and explained the approach of all the authorities with the issues contested in the present appeals for subsequent years as under:

A.Y	TPO	CIT(A)	Remarks
2007-08	TPO proposed a Transfer Pricing adjustment amounting to INR 6,53,22,520/-	CIT(A) rejected the impugned approach Of TPO and deleted Adjustment proposed by The TPO on account of Transfer Pricing.	Revenue authorities filed an appeal before the ITAT
2008-09	Adjustment amounting to INR 9,69,43,894/- was proposed by TPO		
2009-10	Adjustment amounting to INR 9,69,43,894/- was proposed by TPO		
2010-11	Adjustment amounting to INR 9,69,43,894/- was proposed by TPO.		
2011-12	TPO did not draw any adverse		TPO assessing

	inference to any international transaction and issued a clean Transfer Pricing order.	the case for A.Y 2007-08 and A.Y 2011-12 is same.
2012-13	TPO did not draw any adverse inference to any international transaction and issued a clean Transfer Pricing order.	
2013-14	TPO did not draw any adverse inference to any international transaction and issued a clean Transfer Pricing order.	

7. The Ld. AR submitted that the Assessee undertakes limited business functions in the nature of liaising and facilitation of business of the AEs and, therefore, the functions performed by the Assessee are very different from Sogo Shosha traders. The Assessee undertakes limited functions of arranging meetings of AEs with prospective customers, facilitation of the transaction of sourcing between the third party customers in India and the AEs, etc. Further, the Assessee assumed limited risks and did not bear any risk in the nature of credit risk, price risk, inventory risk, storage and handling risk, etc. The Assessee has not developed any intangibles or accorded locational savings to its AEs. Locational savings are effected by the third party buyer who purchases the goods from the AEs. It can be seen from the TP documentation that the Assessee has been adequately compensated since, it has earned a net operating profit margin on cost of 110.91% and 123.52% against the arithmetic mean of the margins of comparable companies at 15.29% and 15.28% for AY 2007-08 and 2008-09, respectively. The provisions of the law do not warrant such Inclusion of costs which do not form part of the Assessee's operating cost and is artificial enhancement of the cost base of the Assessee. The Ld. AR submitted that the TPO has erred in re-characterizing the business functions of the Assessee to be that of a trader. The TPO failed to appreciate that the Assessee has not undertaken

the activity of purchase and resale. Further, the companies adopted by the TPO as comparable are undertaking trading operations which is not comparable to the inter-company transactions undertaken by the Assessee. The TPO has artificially enhanced the cost base on the Assessee and proposed a mark-up on the FOB value of goods sourced by AEs, such approach does not correspond to any one of the five methods, as provided under the ACT. Further, the Assessee has earned a net operating profit margin on cost of 110.91% and 123.52% for AY 2007-08 and 2008-09, respectively. Computation of an adjustment (over and above the existing remuneration) to the tune of INR 6,53,22,520 and INR 9,69,43,894 by the TPO for the relevant AYs, has required the Assessee to earn an NCP of 202.35% and 246.09% for AY 2007-08 and 2008-09, respectively which is practically impossible to achieve.

6. The Ld. AR relied upon the Hon'ble Delhi High Court judgment in case of Li and Fung India Pvt. Ltd. Vs. CIT (2014) 361 ITR 85 (Del) wherein it is held that the approach of TPO to enhance the assessee's cost base by considering the FOB value of contracts entered into by AE with third part vendors is nowhere supported by TNMM under Rule 10B(1)(e) of the Rules. The order of the ITAT, while rejecting the Transfer Pricing exercise of Li Fung India, has not shown the extent to which the significant risks are borne by Li Fung India and the locational savings enjoyed by AEs. Specific findings and materials should be placed on record while concluding on specific facts such as significant risk, functional risk and enterprise risk. Approach of adoption of 3 percent margin over the FOB value of AE's contract is in error of law. Addition of cost plus mark-up on FOB value of exports among third parties for calculation of arm's length price under TNMM is without foundation and liable to be deleted. The principles laid down by the Hon'ble Delhi High Court are squarely applicable to the case of the Assessee since the facts of the Assessee and Li Fung India are almost identical. The Ld. AR further submitted that the TPO in the TP order alleged the following:

- IIPL has undertaken critical functions and assumes significant risks.
- AEs have benefitted form the supply chain and human capital intangibles and location savings developed by IIPL.
- TPO alleged that the IIPL is adding value to the entire supply chain, hence, mark-up must be applied to the direct cost of IIPL along with the FOB value of goods sourced by AE.
- TPO rejected the benchmarking analysis undertaken by IIPL in its TP documentation and proposed a set trading companies as comparables.
- In order to compensate IIPL, for its efforts, the TPO proposed an addition of 2.53% (average net margins of trading companies) mark-up of FOB value of exports made by India manufacturer to overseas third party customers.

The Ld. AR further submitted that the CIT(A) appreciated the functional and risk profile of the Assessee and held that the TPO has erred in treating the Assessee as a trader and including the FOB value of goods sourced in the operating cost of the Assessee. The Ld. AR further submitted that the Hon'ble ITAT in Li Fung's own case for AY 2007-08, 2008-09 reported at [2014] 63 SOT 61 (Del) and 2009-10 reported at [2016] 178 TTJ 10 (Del), following the judgment of the Hon'ble Delhi High Court held that the base of 'total cost' as adopted by the TPO and approved by DRP in considering the FOB value of goods between the third party enterprises cannot be accepted. The Ld. AR submitted that the order of the ITAT in case of GAP International Source India Pvt. Ltd Vs. ACIT 25 Taxman.com 414 (Delhi) has been confirmed by the Hon'ble High Court by dismissing the appeal of the Revenue.

8. We have heard both the parties and perused the material available on record. The CIT(A) has rightly relied upon the decision taken by the Tribunal in case of GAP International Sourcing India Pvt. Ltd wherein the Revenue has

filed appeal before the Hon'ble High Court which is dismissed vide order dated 29/1/2016. The Ld. AR also pointed out that in subsequent years the TPO has accepted the said contentions and granted the relief related to FOB as per the decision of GAP International & LI & Fung India Pvt. Ltd. The case laws referred by the Ld. AR are having similarity on the factual aspect with the assessee company herein. Itochu Corporation, Japan ("ICJ") is a trading organization in Japan and is engaged in trading of various products such as textiles, machinery, information and communications related products, meals, products related to oil and other energy resources, general merchandise, chemicals, provisions and food. IIPL was incorporated as a wholly owned subsidiary of ICJ to render business support services to its AEs in the nature of facilitation services to source goods from India. The TPO failed to appreciate that the Assessee has not undertaken the activity of purchase and resale. Further, the companies adopted by the TPO as comparable are undertaking trading operations which is not comparable to the inter-company transactions undertaken by the Assessee. The TPO has artificially enhanced the cost base on the Assessee and proposed a mark-up on the FOB value of goods sourced by AEs, such approach does not correspond to any one of the five methods, as provided under the ACT. Further, the Assessee has earned a net operating profit margin on cost of 110.91% and 123.52% for AY 2007-08 and 2008-09, respectively. Computation of an adjustment (over and above the existing remuneration) to the tune of INR 6,53,22,520 and INR 9,69,43,894 by the TPO for the relevant AYs, has required the Assessee to earn an NCP of 202.35% and 246.09% for AY 2007-08 and 2008-09, respectively is practically impossible to achieve. These contentions taken by the Ld. AR are accepted. The Revenues appeal agitating the issue of deletion of the addition made on account of Arms Length Price related to FOB value of cost is similar to the case of GAP International Sources India Pvt. Ltd. There is no need to interfere with the order of the CIT(A). The order of the CIT(A) is upheld.

9. In the result, appeals of the Revenue's are dismissed.

Order pronounced in the Open Court on 18th August, 2017.

Sd/- Sd/-

(N. K. SAINI) **(SUCHITRA KAMBLE)**
ACCOUNTANT MEMBER **JUDICIAL MEMBER**

Dated: 18/08/2017
*R. Naheed **

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

ASSISTANT REGISTRAR

ITAT NEW DELHI

		Date	
1.	Draft dictated on	12/07/2017	PS
2.	Draft placed before author	13/07/2017	PS
3.	Draft proposed & placed before the second member	.2017	JM/AM
4.	Draft discussed/approved by Second Member.		JM/AM
5.	Approved Draft comes to the Sr.PS/PS	21.08.2017	PS/PS
6.	Kept for pronouncement on		PS

7.	File sent to the Bench Clerk	21.08.2017	PS
8.	Date on which file goes to the AR		
9.	Date on which file goes to the Head Clerk.		
10.	Date of dispatch of Order.		