IN THE INCOME TAX APPELLATE TRIBUNAL
PUNE BENCH, 'C', PUNE

BEFORE SHRI R.S. SYAL, VICE PRESIDENT AND
SHRI S.S. VISWANETHRA RAVI, JUDICIAL MEMBER

आयकर अपील सं. / ITA Nos.738, 739 & 740/PUN/2017
निर्धारण वर्ष / Assessment Years : 2011-12, 2012-13 & 2013-14

M/s. Sava Medica Ltd., Sava House, 3rd Floor, Lawani Plaza, B-Wing, Plot No.57/58, Sakorenagar, Viman Nagar, Pune – 411007 PAN: AANCS8819F	Vs.	ACIT, Central Circle 2(1), Pune
Appellant		Respondent

Assessee by : Shri Kishor Phadke
Revenue by : Shri Sangram Gaikwad

Date of hearing : 25-08-2021
Date of pronouncement : 30-08-2021

आदेश / ORDER

PER R.S.SYAL, VP :

These three appeals by the assessee are directed against the separate final assessment orders dated 25.01.2017 passed by the Assessing Officer (AO) u/s 143(3) r.w.ss. 144C(13) and 153A of the Income-tax Act, 1961 (hereinafter referred to as 'the Act') in relation to the assessment years 2011-12, 2012-13 & 2013-14. Since some common issues have been raised in these appeals, we are, therefore, proceedings to dispose them off by this consolidated for the sake of convenience.

A.Y. 2011-12 :

2. The assessee is aggrieved by an addition of Rs.37,78,910 made by the AO in the impugned order. Pithily put, the factual panorama of the case is that the assessee is a part of the Sava group of companies, which is engaged in the business of manufacturing, importing and exporting pharmaceutical drugs etc. It filed a return declaring loss of Rs.1,94,792 on 30.11.2011. A search action u/s 132 of the Act was taken up in Sava group of companies including the assessee on 31.10.2012. Pursuant to such search, a notice u/s 153A was issued calling the assessee to file return for the year under consideration. The assessee filed a letter stating that the return originally filed for the year may be treated as a return in response to notice u/s 153A of the Act. The assessee reported an international transaction of "Sale of finished goods" amounting to Rs.3,20,24,659 to Sava Trading FZC, Dubai in Form 3CEB. After taking prior approval of the Competent authority, the AO made a reference to the Transfer Pricing Officer (TPO) for determining the Arm's Length Price (ALP) of the international transaction. The TPO in his three page order passed u/s 92CA(3) of the Act observed that: "*The*

detailed order explaining the business model of the assessee, the facts of the case and resultant adjustment under transfer pricing having been discussed in the case of Anagha Pharma Ltd for the Assessment Year 2007-08. As the facts of the case of this assessee for this assessment year are same these are not reproduced here". In the next para, the TPO concluded by noting that: "*In view of the discussion made in the order of Anagha Pharma Ltd for the A.Y. 2007-08, the adjustment of Rs.94,92,109/- is made to the international transaction and as a consequence of the adjustments, income of the assessee shall be increased by Rs.94,92,109/-.* The draft order incorporating the transfer pricing adjustment of equal amount was notified by the TPO on 29.02.2016. The assessee assailed various facets of the transfer pricing addition before the Dispute Resolution Panel (DRP), which gave certain directions on 30.11.2016. The AO passed the impugned order, giving effect to the directions of the DRP, by making the transfer pricing addition at Rs.37,78,910. Aggrieved thereby, the assessee has come up in appeal before the Tribunal.

3. We have heard both the sides and gone through the relevant material on record. It can be seen from the TPO's order that no separate detailed discussion *qua* the ALP determination has been made in the body of the order except following his own order passed in the case of Anagha Pharma Ltd. now Sava Healthcare Ltd. [hereinafter also called the `other Indian entity (OIE)'] for the A.Y. 2007-08, whose copy has been placed at page 99 onwards of paper book. As such, it becomes imperative to go through this order for deeply understanding the factual matrix of the case before us and the nature of the transfer pricing addition. The TPO in that order has recorded the background of the case by noting that Shri Vinod Jadhav, main person of Anagha group of companies, initially started trading of pharmaceutical drugs. In April, 2010, a diversification was made by acquiring Pharma Division of some company and the assessee group also started a manufacturing facility. Apart from OIE, the group established another company in India, namely, Sava Medica Ltd. (which is the assessee under consideration). In addition, the group set up certain entities in Mauritius, UAE and Singapore. The object behind creation of the entities abroad was

held to be tax avoidance on income in India. Though the management and control of the entire global business of the group was wholly in India, the TPO held that the business was shown to have been carried out in Mauritius and Dubai where taxes were not levied on income. He held that the Associated Enterprises (AEs) ploughed back the income earned by them to India through dividends and remuneration to Shri Vinod Jadhav, who, in turn, claimed such income as exempt on the ground of his Non-resident status. It was further noted that the Settlement Commission rejected the non-resident status claim of Shri Vinod Jadhav and declared him as a Resident. The TPO noted the findings of the Investigation team in relation to the functions performed by the two Indian-based companies of the group along with those situated in Mauritius, Singapore and Dubai. He tabulated such functional analysis done by various group companies in para 27.3 of his order and held that the AEs performed no functions except receipt of sale proceeds and sending the same to the Indian entities. Rejecting the OIE's benchmarking done under the Transaction net margin method (TNMM), he proceeded to determine the ALP under the Profit Split method (PSM). He allocated 3% of the aggregate group profits to the AEs abroad for the services rendered by them and the balance 97% was divided between the two Indian entities. To be more precise, he aggregated the year-wise profits shown by the five group entities from the A.Ys. 2007-08 to 2013-14 and found out the total combined profit of Rs.1,57,23,23,733 as per Table 28.1 of his order. Then he proceeded to split the combined profit through Table 28.2 as under:-

A.Y.	**Combined Profit of Anagha and AE's**	**% of Profit earned by the Comparables. As per assessee's T.P. Report**	**Profit Attributable to the Anagha which is equal to the comparable's profit %**	**AE's Share 3%**	**Residual Profit allocated to Anagha Pharma Ltd**	**Anagha's Total Profit**
A	**B**	**C**	**D (B*C%)**	**E (B*3%)**	**F (B-D-E)**	**G (D+F)**
2007-08	2,28,44,905	2.77	6,32,804	6,85,347	2,15,26,754	2,21,59,558
2008-09	17,69,90,270	0.31	5,48,670	53,09,708	17,11,31,892	17,16,80,562
2009-10	32,69,96,892	2.42	79,13,325	98,09,907	30,92,73,660	31,71,86,985
2010-11	8,81,15,771	4.35	38,33,036	26,43,473	8,16,39,262	8,54,72,298
2011-12	48,58,35,923	6.49	3,15,30,751	1,45,75,078	43,97,30,094	47,12,60,845
2012-13	13,32,70,295	5.71	76,09,734	39,98,109	12,16,62,452	12,92,72,186
2013-14	33,82,69,677	5.16	1,74,54,715	1,01,48,090	31,06,66,871	32,81,21,587
TOTAL	**1,57,23,23,733**		**6,95,23,035**	**4,71,69,712**	**1,45,56,30,986**	**1,52,51,54,021**

4. It can be seen from the above table that OIE had shown profit rate of its comparables at 6.49% for the A.Y. 2011-12 which was reflected by him under column C. The TPO first determined the arm's length profit from the transaction of export by OIE in the

column D at Rs.3.15 crore. After reducing the share of AEs at 3% under Column E amounting to Rs.1.45 crore, he computed the Residual profit under Column F at Rs.43.97 crore and then totaled up the arm's length profit of OIE and the assessee under Column G at Rs.47.12 crore. Thus it is manifest, that though the TPO initially talked of piercing the corporate veil and taking all the entities as one, but ended up in attributing separate compensation for the activities done by the foreign AEs at 3% of total profit, thereby maintaining separate independent status of them as distinct from the two Indian entities. It goes without saying that the order needs to be read as a whole. If some observations are made in the body of the order, which are eventually not acted upon, one cannot claim any decision based on such observations.

5. Thereafter, the TPO computed the net transfer pricing adjustment in the hands of OIE, through para 28.3, as under:-

A.Y.	**Anagha's Total Profit**	**Less O.P. shown by the Assessee**	**Total Adjustment**	**Less Adjusted in the hands of Sava Medica Ltd. (As mentioned below)**	**Net Adjt in the hands of OIE**
A	**B**	**C**	**D**	**E**	**F**

2007-08	2,21,59,558	1,30,38,449	91,21,109	0	91,21,109
2008-09	17,16,80,562	1,69,42,134	15,47,38,428	0	15,47,38,428
2009-10	31,71,86,985	4,55,81,486	27,16,05,499	0	27,16,05,499
2010-11	8,54,72,298	73,95,355	7,80,76,943	0	7,80,76,943
2011-12	47,12,60,845	1,66,56,860	45,46,03,985	94,92,109	44,51,11,876
2012-13	12,92,72,186	5,99,91,658	6,92,80,528	54,08,126	6,38,72,402
2013-14	32,81,21,587	4,78,94,987	28,02,26,600	4,66,98,148	23,35,28,452
TOTAL	**1,52,51,54,021**	**20,75,00,929**	**1,31,76,53,092**	**6,15,98,483**	**1,25,60,54,609**

6. Through this table, he found out the amount of year-wise transfer pricing adjustment in the hands of the two Indian entities, namely, OIE and the assessee. Firstly, he computed the total adjustment under Column D collectively in the hands of both the Indian entities at Rs.45,46,03,985 and then he reduced the amount of transfer pricing adjustment made in the hands of the assessee under Column E at Rs.94,92,109 to work out the amount of total adjustment in the hands of OIE at Rs.44,51,11,876 for the A.Y. 2011-12 under Column F. It is this amount of the transfer pricing adjustment of Rs.95,92,109 which has been adopted by the TPO in his order passed in the hands of the assessee for the year under consideration. The working of transfer pricing adjustment in the hands of the assessee at Rs.94,92,109 has come from the Table given on the last page of the TPO's order in OIE. This has been done by taking the value of international transaction of exports

made by the assessee to its AEs at Rs.3.20 crore on which the profit rate of 29.64% (OP/OR of AEs taken as arm's length profit rate) has been applied. The figures of the AE's operating profit at Rs.46.93 crore and operating revenue of Rs. 158.31 crore have been taken from the Table 5.1 on page 2 of the TPO's order in the hands of the assessee.

7. On an overview of the discussion made by the TPO in his order passed in the case of the assessee read in conjunction with the order in the case of OIE, it can be seen that he rejected the adoption of the TNMM and instead chose the PSM as the most appropriate method for determining the ALP. Insofar as the assessee is concerned, the TPO has simply taken the value of the international transaction of exports to the AEs and then applied the profit rate of the AE for determining the ALP. As the assessee reported only one international transaction of `Sale of finished goods' with transacted valued of Rs.3.20 crore, the TPO determined the ALP of such a transaction leading to the transfer pricing adjustment of Rs.94,92,109.

8. The assessee assailed the draft order before the DRP on several issues. The DRP called for comments/reports from the TPO/AO on certain aspects and also the comments of the assessee. After entertaining the entire gamut of the material, the DRP *inter alia* came to hold that:

- The TPO was not justified in holding that the control and management of the affairs of the Sava group was situated wholly in India and the entities abroad were sham.
- The assessee had undertaken only the activities of sale of finished goods as reported in Form No.3CEB.
- The TPO wrongly applied Profit Split Method in the case of assessee by considering OP/OR of the AE's
- The assessee also wrongly applied the TNMM for benchmarking its transactions.
- Both the methods applied by the assessee as well as the TPO were wrong. As the assessee was only into trading exports for the year under consideration, the correct method to be applied was the Resale Price Method (RPM).

9. Accordingly, the assessee was directed to furnish benchmarking analysis of its international transaction by applying the RPM. The assessee submitted the same which has been reproduced at page 83 of the DRP's directions. As per this exercise, the assessee computed its GP/Sales margin at 25.22%. The DRP made alterations to certain figures and hence re-worked out the amended GP/Sales at 16.52%. The assessee had identified 33 companies as comparables. The DRP removed 13 companies from such list and computed the average GP/Sales of the remaining 20 comparables at 28.32%. This is how, the differential profit rate of 11.80% (28.32% of the comparables and 16.52% of the assessee) was applied to the value of international transaction of exports made by the assessee at Rs.3.20 crores for determining the transfer pricing adjustment at Rs.37,78,910. It is this amount of transfer pricing adjustment which has been made by the AO in the final assessment order, against which the assessee has come up in appeal before the Tribunal.

10. On an overview of the above discussion, it is ostensible that the assessee applied the TNMM for determining the ALP of the international transaction of `Sale of finished goods' worth Rs.3.20

crores. The TPO rejected such a method and applied the PSM. The DRP has finally held that the RPM is the most appropriate method. Now the assessee is in appeal challenging the correctness of the RPM as the most appropriate method. There is no cross appeal by the Department. Thus the view of the TPO in applying the PSM no more stands. Even otherwise, there are certain flaws in the application of the PSM by the TPO, which we will touch very briefly.

11. Rule 10B(1) of the Income-tax Rules, 1962 (hereinafter also called `the rules') deals with the determination of the ALP as per section 92C under different methods. The *modus operandi* for determining the ALP under the `Profit Split method' has been set out in rule 10B(1)(d) reading as under:-

> "(*d*) profit split method, which may be applicable mainly in international transactions or specified domestic transactions involving transfer of unique intangibles or *in multiple international transactions or specified domestic transactions which are so interrelated that they cannot be evaluated separately for the purpose of determining the arm's length price of any one transaction*, by which—
>
> (*i*) the combined net profit of the associated enterprises arising from the international transaction or the specified domestic transaction in which they are engaged, is determined;
> (*ii*) the relative contribution made by each of the associated enterprises to the earning of such combined net profit, is then evaluated on the basis of the functions performed, assets employed or to be employed and risks assumed by each enterprise and on the basis of reliable

external market data which indicates how such contribution would be evaluated by unrelated enterprises performing comparable functions in similar circumstances;
(*iii*) the combined net profit is then split amongst the enterprises in proportion to their relative contributions, as evaluated under sub-clause (*ii*);
(*iv*) the profit thus apportioned to the assessee is taken into account to arrive at an arm's length price in relation to the international transaction or the specified domestic transaction:

Provided that the combined net profit referred to in sub-clause (*i*) may, in the first instance, be partially allocated to each enterprise so as to provide it with a basic return appropriate for the type of international transaction or specified domestic transaction in which it is engaged, with reference to market returns achieved for similar types of transactions by independent enterprises, and thereafter, the residual net profit remaining after such allocation may be split amongst the enterprises in proportion to their relative contribution in the manner specified under sub-clauses (*ii*) and (*iii*), and in such a case the aggregate of the net profit allocated to the enterprise in the first instance together with the residual net profit apportioned to that enterprise on the basis of its relative contribution shall be taken to be the net profit arising to that enterprise from the international transaction or the specified domestic transaction;"

12. Rule 10A(1)(d) expressly sets forth the situations in which the Profit split method can be applied, *inter alia,* `in multiple international transactions or specified domestic transactions which are so interrelated that they cannot be evaluated separately for the purpose of determining the arm's length price of any one transaction'. At this juncture, it is relevant to note that the application of the PSM pre-supposes existence of separate character of the entities performing interlinked parts of one overall

transaction. It is only because of the inherent difficulty in evaluating the arm's length price of the separate parts of the large transaction undertaken by different entities that the individual profit earned by each entity from the overall transaction is aggregated, which is then split between them in proportion of their relative contributions for finding out the ALP.

13. On going through the prescription of the method, it becomes overt that it requires determination of the arm's length profit in two stages, which is then aggregated as per the latter part of the proviso providing for aggregating basic return with the residual net profit remaining after such allocation. The first stage is enshrined in the opening part of the proviso expressly providing for computation of the basic return corresponding to the efforts put in by a particular entity. The second stage is set out in various sub-clauses of rule 10B(1)(d). Sub-clause (i) provides for aggregating net profit earned by the concerned associated enterprises. The TPO on Table 28.1 of his order in OIA has aggregated operating profits of five entities from A.Ys.2007-08 to 2013-14 and the combined net profit has been determined at Rs.157.23 crores as under:-

28.1 Determination of Combined Profits of the Assessee and AE's

	Anagha Pharma - India	Anam Trading Co. Mauritiu	Sava Trading Co. (Sava Pharma Ltd) Mauritiu	Sava Trading FZE (Sharjah) (Westside FZE)	Goldwing Trading FZE	Combined Profit of Anagha and AE's
A.Y	Op. Profit	Op. Profit	Op. Profit	Op. Profit	Op. Profit	
A	B	C	D	E	F	G
2007-08	1,30,38,449	-23,39,606	1,21,46,062	0	0	2,28,44,905
2008-09	1,65,77,014	20,73,403	12,10,74,256	3,72,65,597	0	17,69,90,270
2009-10	4,55,01,112	0	1,05,89,783	27,09,05,997	0	32,69,96,892
2010-11	65,46,516	0	0	8,15,69,255	0	8,81,15,771
2011-12	1,65,14,476	0	0	46,93,21,447	0	48,58,35,923
2012-13	5,98,94,492	0	0	-31,30,45,698	38,64,21,501	13,32,70,295
2013-14	4,72,85,077	0	0	0	29,09,84,600	33,82,69,677
TOTAL	**20,53,57,136**	**-2,66,203**	**14,38,10,101**	**54,60,16,598**	**67,74,06,101**	**1,57,23,23,733**

14. The next step in stage two is enshrined in sub-clauses (ii) and (iii), which provide that the relative contribution by each of the associated enterprises to the earning of such combined net profit is to be evaluated and then the combined net profit is to be split amongst the enterprises in proportionate to their relative contribution. However, before undertaking this exercise, the *basic return* particular to the concerned entity is to be determined as per first part of the proviso, which is to be reduced from the aggregate profit. The TPO in the extant case determined the basic return for OIE (Column D) and the overseas entities (Column E) in Table 28.2 and then worked out the entire Residual profit (Column F). In finding out the figures under certain columns of Table 28.2, the

TPO made some infirmities. Firstly, for calculating the basic return of OIE under column D, the TPO applied percentages of profit earned by the comparables as per the TP report of OIE on the combined operating profit of all the five entities taken together. Instead of that, he should have determined the basic return of OIE by applying the comparables' net profit rate to the amount of sales made by OIE for such years. Similar mistake was committed in computing the amount of basic return appropriate for overseas entities by applying 3% of the combined profit of all the five entities. He mentioned in para 28 that: `The roles of the AEs have been narrated above…. for which not more than 2% to 3% would be charged as commission'. Commission is computed with reference to the amount of sales and not the overall profit of all the entities taken together.

15. Coming back to sub-clauses (ii) and (iii), the TPO is required to split the residual profit between the entities who contribute to the overall transaction. In the instant case, the TPO under Column F of Table 28.2 attributed the entire Residual profit to OIE, which he then aggregated with the basic return of OIE as per Column D to

find out the total arm's length profit of OIE as per Column G of Table 28.2. From 100% allocation of Residual profit to OIE, it is vivid that the TPO attributed all the combined functions only to OIE and none to any other entity including the assessee under consideration or overseas AEs.

16. Another mistake which the TPO committed in Table 28.3 is that he took the figure of OIE's total profit under Column B, which is the same figure as Column G in Table 28.2. After reducing the amount of operating profit shown by OIE under Column C, he determined the total amount of transfer pricing adjustment as per Column D of Table 28.3. From this, he reduced the arm's length profit of the assessee as calculated on the last page of the order in OIE, to find out the amount of transfer pricing adjustment in the hands of OIE Though he reduced the amount of arm's length profit of the assessee in Table 28.3, but forgot to add the amount of profit/loss of the assessee in his Table on 28.1 while calculating the Combined profit of the group entities, for further processing under the PSM.

17. Having pointed out a few weaknesses in implementing the PSM, we leave this issue here only because the ALP determination under the PSM has become academic as the DRP has directed to apply the RPM and the assessee is not seeking the application of the PSM. The only thing which we want to accentuate is that the TPO attributed the entire Residual profit (after excluding the arm's length profits of the assessee and OIE from their respective international transactions of sale; and 3% to overseas entities) only to OIE by opining that all other activities were done by it alone.

18. At this juncture we take note of the following additional ground taken by the assessee :

> *"19. The learned AO erred in law and on facts in referring the alleged international transaction of "Control & Management of Sava Group" to the learned TPO, without complying with the provisions of section 92CA(1) r.w.s. 92C(3) and 92B of ITA, 1961."*

19. The Hon'ble Supreme Court in *National Thermal Power Company Ltd. Vs. CIT (1998) 229 ITR 383 (SC)* has observed that "the purpose of the assessment proceedings before the taxing authorities is to assess correctly the tax liability of an assessee in accordance with law. If, for example, as a result of a judicial

decision given while the appeal is pending before the Tribunal, it is found that a non-taxable item is taxed or a permissible deduction is denied, we do not see any reason why the assessee should be prevented from raising that question before the tribunal for the first time, so long as the relevant facts are on record in respect of that item". Answering the question posed before it in affirmative, their Lordships held that on the facts found by the authorities below, if a question of law arises (though not raised before the authorities) which has bearing on the tax liability of the assessee, the Tribunal has jurisdiction to examine the same. Having gone through the subject matter of the additional ground espoused by the assessee, it is discernible that the same raises a pure question of law. We, therefore, admit the same and take it up for disposal on merits.

20. The ld. AR submitted that the AO went wrong and committed the same mistake as was done in the case of OIE by making a reference to the TPO for determining the ALP of a transaction which was not reported by the assessee in Form No. 3CEB, without granting opportunity of hearing. He relied on the order passed by the Tribunal in the case of OIE for the assessment years 2007-08 to

2013-14 in which the assessment has been held to be vitiated on this count. Another submission was made to the effect that the TPO held the entire network of Sava group companies as *sham* that did not lie in his domain, which, if warranted, could have been done only by the AO. This point also, in his opinion, vitiated the assessment as has been held by the Tribunal in the case in OIE. These contentions were countered by the ld. DR who submitted that there was no illegality in the action of the AO in making a reference to the TPO nor did the TPO commit any mistake in exercising his jurisdiction in the facts and circumstances of the case.

21. We have heard the rival contentions and gone through the relevant material on record. The Tribunal in its order dated 27-06-2019 (ITA Nos. 1062 to 1068/PUN/2017) passed in OIE, has observed in para no. 84: "That the AO made a reference to the TPO on two aspects, i.e. sale of medicines and drugs by the assessee group which not only included the assessee but various other companies and the second transaction which was reported was the one declared by the assessee in audit report, i.e. export trading of medicines on wholesale basis'. Then allowing the plea of the

assessee vide para 99 of its order, the Tribunal held: "*that where the AO while making reference of an independent to/ and non existing international transactions (as alleged by the ld. AR) had to come to a finding that income arising from the said international transactions needs to be benchmarked, in order to determine its arm's length price and before such reference to the TPO, show cause notice should have been given to the assessee. In the absence of any such show cause notice being given to the assessee, the same is irregularity (as held by the Hon'ble Bombay High Court) and the said irregularity cannot be made good by restoring back the same to the file of AO…….It is the case of violation of principles of natural justice and such an order passed in the hands of the assessee cannot stand and the same is invalid and bad in law*". It can be seen from the order of the Tribunal in the case of OIE that the AO made a reference to the TPO in respect of two transactions viz., the first of sale to the AEs which was declared by the assessee in its Form No.3CEB and the second of worldwide sale by the assessee group, which was not declared. We have reproduced Table 28.2 from the order of the TPO in the case of OIE in which Column

No. D represents profit attributable to OIE for the reported international transactions and then Column No. F with the "Residual profit allocated to OIE". These two transactions determined by the TPO under the Profit split method were clubbed and in table No.28.3 he proposed the transfer pricing addition for them after excluding the arm's length profit in the hands of the assessee under consideration for the assessment years 2011-12, 2012-13 and 2013-14, which amount was, in turn, computed by applying the profit rate of AEs to the exports made by the assessee. Thus, it can be seen that the two transactions were benchmarked in the hands of OIE collectively under the PSM, viz., one being the export made by OIE directly and the other being the allocation of residual profit to it as relatable to the worldwide operations. To put it simply, the TPO combined profit of all the entities for the A.Y. 2011-12 under consideration at Rs.48.58 crore (Table 28.2 column B), from which he reduced 3% profit as allocable to the entities abroad at Rs.1.45 crore (Table 28.2 Column E); then the arm's length profit of the assessee's only transaction of sale made to the AEs at Rs.94,92,109 (Table 28.3 column E); and then the arm's length profit of the reported transaction of the sales made by OIE at Rs.3.15 crore (Table 28.2 column D); and the remainder amount of total profits was taken as the arm's length profit of the second unreported international transaction of OIE, being, the profit allocation for the worldwide operations of the Sava group at Rs.41.36 crore (Total transfer pricing adjustment of OIE of Rs.44.51 crore as per Table 28.3 column E minus Rs.3.15 crore towards the first reported international transaction of OIE). From the above discussion, it is graphically clear that the declared transaction of exports of OIE with arm's length profit of Rs.315 crore lies at the same pedestal as the only transaction of the assessee with the arm's length profit of Rs.94,92,109 and that no international transaction parallel to the second transaction of OIE with transfer pricing adjustment of Rs.41.36 crore is there in the hands of the assessee. To sum up, the TPO proceeded with two distinct transactions in the case of OIE, which were albeit processed jointly under the PSM. The Tribunal in its order in OIE, after observing that there were two transactions, came to hold that the reference made by the TPO in respect of the second transaction, without giving opportunity of hearing to the assessee, vitiated the assessment order. As against that, the assessee has only one international transaction of export made to its AE with transacted value of Rs.3.02 crore and the arm's length profit of Rs.94,92,109/- It is only this transaction which was referred by the AO to the TPO and whose ALP has been determined. As neither any second international exists in the case of the assessee nor has been referred to the TPO, the *ratio* laid down by the Tribunal in the case of OIE has no application here. Had the factual position prevailing in the case of the assessee been similar, following the rule of *stare decisis*, we would have gone with the order passed in OIE. The fact that there is only one international transaction in the case of the assessee which was referred by the AO to the TPO and whose ALP has been determined, there can be no question of declaring the assessment order to be bad in law on this score.

22. The next contention of the ld. AR, relying on the Tribunal order in OIE, is that the assessment order is bad in law because the TPO had no power to conclude that the control and management of affairs was situated wholly in India, which could have been done only by the AO. Again here, we find this argument as not

applicable to the facts of the assessee before us. The contention put forth before the Tribunal in OIE, which got accepted, has to be seen in the background of the facts in which that case was placed. We have noted above that the TPO determined the ALP in the case of OIE of the international transactions of direct exports made to the AEs and also of the remaining worldwide profit from the sales on the premise that the control and management of the group affairs was wholly in India with OIE It was the second transaction, with reference to which the Tribunal declared the assessment order bad in law by holding that only the AO and not the TPO could hold that control and management of affairs was situated wholly in India. As no transfer pricing addition has been made in the hands of the assessee under consideration *qua* the transaction similar to the second transaction in OIE of the profit on the worldwide sales, that part of the decision has no relevance to the instant case. There is no whisper much less any reference in the order of the TPO passed in the case of the assessee holding that the control and management of affairs was situated wholly in India. The contention is, therefore, repelled.

23. The assessee has raised another legal issue contending that the international transaction of the assessee was only worth Rs.3.20 crores. While referring to the certain documents, it was submitted that the AO applied to the CIT u/s 92CA(1) of the Act for seeking permission for making a reference to the TPO for the ALP determination. The CIT, in turn, took note of the fact that the amount of international transaction in the case was less than Rs.5 crores and called upon the AO to assign specific reasons for making such a reference. Thereafter, the AO adduced the reasons vide his letter dated 14.10.2014 as to why the international transaction of less than Rs.5 crores needed to be referred to the TPO. Such reasons were stated to be that the assessee group was subjected to search u/s 132(4) which transpired that it was routing the business to the foreign companies with an intention to evade taxes in India. Since the ALP determination in the case of the assessee for the year under consideration would have bearing on the ALP determination of other entities of Sava group and other years of assessee also in which the amount of international transactions was more than Rs.5.00 crores, it was requested that the reference should be made to

the TPO so as to maintain consistency and a uniform ALP determination. The CIT got convinced with the AO's reasons and accorded his sanction. It was thereafter that the AO made a reference to the TPO for determining the arm's length price of international transaction of Rs.3.20 crores vide his letter dated 19.11.2014, a copy of which has been placed at page 1009 of the paper book. The ld. AR contented that Circular No.3/2003 dated 20.05.2003 expressly provides that reference to the TPO can be made by the AO only when the value of international transaction exceeds Rs.5 crores. It was submitted that since the value of international transaction in the instant case was less than such a threshold, it was incumbent upon the AO himself to determine the ALP. As the AO made a reference to the TPO, and the latter determined the ALP, all the proceedings were vitiated.

24. There is no doubt that Circular No.3/2003 provides for making reference to the TPO only where the value of international transaction exceeds Rs.5 crores. In other words, if the aggregate value of international transaction in a case is less than that, then the AO is supposed to benchmark the international transaction at his

own level without making a reference to the TPO. To this extent, the argument of ld. AR is correct. However, the consequence of such a wrong doing, as claimed by the ld. AR to be fatal and vitiating the final assessment order, in our considered opinion is not correct. If some irregularity, which is not a legal infirmity, takes place in the process of assessment, such an irregularity needs to be cured by restoring the matter to the stage at which such an irregularity occurred. The outcome of such an irregularity cannot be to quash the assessment. The Hon'ble Supreme Court in *Pr.CIT vs. S.G. Asia Holdings (India) Pvt. Ltd. (2019) 310 CTR 1 (SC)* came across a situation in which the same the CBDT's Circular No.3/2003 was not followed but in the converse directions, namely, the AO *suo motu* determined the ALP of international transaction with the value exceeding Rs.5 crores. The Tribunal approved the contention of the assessee that the AO failed in following the mandate of the Circular and quashed the assessment order. When the matter reached before the Hon'ble Supreme Court, it approved the view of the Tribunal to the extent that the AO was bound to make a reference to the TPO when the aggregate value of international transaction exceeded Rs.5 crores in terms of Instruction No.3/2003. However, it reversed the Tribunal order on the other issue by holding that "*the Tribunal ought to have accepted the submissions made by the Departmental Representative …. and the matter ought to have been restored to the file of AO so that appropriate reference could be made to the TPO*". Thus, it is evident from the judgment of the Hon'ble Summit Court that if the prescription of Circular No.3/2003 is not followed, the proper course of action is to restore the matter to the stage where irregularity occurred rather than quashing the entire proceedings and the consequential assessment order. We, therefore, respectfully following the Hon'ble Apex Court judgment in *Pr.CIT vs. S.G. Asia Holdings (India) Pvt. Ltd. (supra)*, set aside the impugned order and remit the matter to the file of the AO for determining himself the ALP of the international transaction of 'Sale of finished goods' after allowing a reasonable opportunity of hearing to the assessee.

25. Now, we turn to the application of the Resale Price Method as directed by the DRP through which, it computed the amount of transfer pricing adjustment at Rs.37,78,910. At this stage, it is

pertinent to note the nature of the international transaction, which is `Sale of Finished goods' to its AE. The DRP held in para 66 that: *"Since the assessee is into trading exports of pharma products, Resale Price Method will be the most appropriate method"*. In order to evaluate if the RPM was properly directed to be applied, we need to refer to the relevant part of rule 10B(1)(b), which reads as under:

> "10B(1)…..
>
> (b) resale price method, by which—
>
> (i) *the price at which property purchased* or services obtained *by the enterprise from an associated enterprise is resold* or are provided *to an unrelated enterprise, is identified;*
>
> (ii) to (v) …."

26. Sub-clause (i) of the rule emphatically provides that: `the price at which property purchased … by the enterprise from an associated enterprise is resold … to an unrelated enterprise, is identified'. Thus, it is glaring that this method applies where an Indian entity purchases goods from its foreign/AE and then resells the same. The entire mechanism in the subsequent sub-clauses of rule 10B(1)(b) is a consequence of this foundational fact. If the international transaction is not that of purchase by an Indian entity,

then the RPM cannot be applied. Here is a case in which the assessee sold goods to its AE in the international transaction rather than purchasing the same. In fact, the purchases for such a resale were made from non-AEs. In such a scenario, we cannot countenance the DRP's direction to apply the RPM for the ALP determination of the international transaction of `Sale of finished goods' to the AEs.

27. Once the application of the PSM has been ruled out by the DRP and rightly so and further we have held hereinabove that the RPM is not the correct method to be applied, then there can be no hitch in accepting the assessee's contention of applying the TNMM as the most appropriate method in the facts and circumstances of the case. In fact, the DRP also directed to apply the TNMM for the next two years, which are part of this batch of appeals, in which the international transactions are sale of manufactured goods to the AEs.

28. Now the assessee has came out with a contention that if the TNMM is to be applied, then its original ALP determination in the Transfer pricing study report should be accepted without remitting

the matter to the AO. We cannot concur with this contention because the working done by the assessee in this regard has not been vetted either by the TPO or the DRP. The TPO rejected such a method and went ahead with the PSM and the DRP suggested the RPM. Hence veracity of the calculations made by the assessee under TNMM has yet to pass through the eyes of the authorities below. Under these circumstances, we set aside the impugned order and remit the matter to the file of the AO for a fresh determination of the ALP of international transaction of 'Sale of finished goods' under the TNMM as per law after allowing reasonable opportunity of hearing to the assessee.

A.Ys. 2012-13 & 2013-14

29. The assessee in these two appeals is aggrieved by the transfer pricing additions of Rs.4,34,17,316 and Rs.7,76,19,272 made by the AO for the A.Ys. 2012-13 and 2013-14 respectively in his final orders dated 25.01.2017

30. The factual matrix for the A.Y. 2012-13 is that the assessee filed return declaring loss of Rs.7,36,50,537. International transactions of `Sale of finished goods' amounting to Rs.9.55 crores

and odd were declared in Form No.3CEB. The AO made a reference to the TPO for determining their ALP. The TPO, vide his concise order dated 29.01.2016, determined the amount of transfer pricing adjustment at Rs.54,08,226. He did not separately discuss the merits of the transfer pricing addition but, as done for the preceding year, relied on the discussion made by him in his order passed in the case of OIE for the A.Y. 2007-08. Similarly, for the A.Y. 2013-14, the assessee filed return declaring loss of Rs.20,82,40,706. The assessee reported international transaction of `Sale of finished goods' at Rs.13,25,91,855. The AO made a reference to the TPO for determining the ALP of international transaction. The latter vide his order dated 29.01.2016, passed in the same way as for the preceding two years, determined the amount of transfer pricing adjustment at Rs.4,66,98,148 by mainly relying on his order in the case of OIE for the A.Y. 2007-08. For both the years, the assessee had applied Transactional Net Margin Method (TNMM). The TPO rejected this method and resorted to the PSM. The assessee assailed the drafts orders containing such transfer pricing adjustments before the DRP, which did not countenance the approach of the TPO in applying the PSM. It directed to apply the TNMM for both the years and required the assessee to furnish benchmarking under the TNMM. For the A.Y. 2012-13, the assessee identified three comparables with mean PLI (OP/OC) at 7.63% and its own OP/TC at 49.44%. The DRP observed that the assessee excluded Employee cost and Operating & administrative costs of Rs.10.94 crores in computing its own operating cost base, for which no justifiable reasons were assigned. The assessee tried to support such exclusion by putting forth that: `major expenses for market and brand creation were undertaken in keeping with the long drawn strategy to manufacture Pharma products. Massive efforts of creating domestic market for the SAVA branded products were undertaken. *These efforts were from a futuristic perspective*. Result of these efforts were not reaped in the current year'. Rejecting such a contention and including such costs within the operating cost base, the DRP determined operating loss of the assessee at Rs.7,45,42,027 and the PLI of OP/OC at (-) 39.82%. This is how, the DRP computed transfer pricing adjustment of Rs.4,34,17,316 which was made by the AO in the final assessment order for the A.Y. 2012-13.

Similarly, for the A.Y. 2013-14, the assessee furnished benchmarking under the TNMM by identifying five comparables with mean PLI (OP/OC) at 5.26%. The assessee computed its own OP/TC at 16.61%. In the calculation of its own operating cost base, the assessee again excluded Employee cost and Operating & administrative cost of Rs.23.89 crores with the similar explanation as given for the preceding year. The DRP did not approve the exclusions and re-determined the PLI of the assessee at (-) 52.11% and accordingly computed the transfer pricing adjustment of Rs.7,76,19,272. The AO in his final order made the above referred transfer pricing additions. Aggrieved thereby, the assessee has come up in appeal before the Tribunal.

31. Having heard both the sides and gone through the relevant material on record, it is observed that the assessee in the initial transfer pricing study report applied the TNMM, which was rejected by the TPO thereby treating the PSM as most appropriate method. The DRP overturned the TPO's action and restored the TNMM as most appropriate method. The assessee is not aggrieved by the TNMM application. The only dispute is about the calculation of its

own PLI. We have noted above that while calculating its PLI for the A.Y. 2012-13, the assessee treated Rs.10.94 crores as non-operating costs on the premise that such expenses were incurred for the purpose of brand building, which *efforts were from a futuristic perspective* and *results of these efforts were not reaped in the current year*. The assessee has demonstrated its PLI working on this basis on pages 761 and 762 of paper book. Whereas the above extracted note has been given on page 761, it has been mentioned on page 762 that: "The cost with respect to employees hired for the purpose of brand creation, promotion and marketing in domestic market which has no relevance with the sales of manufactured products sold to AEs, hence the same is carved out to determine operating cost'. The ld. AR attempted to justify the exclusion of sum of Rs.10.94 crores by contending that the assessee incurred these expenses considering the futuristic impact of the market creation made in this year. He elaborated by stating that such costs resulted into the brand building of the assessee, whose benefit was to be reaped in future years. Thus, it can be seen that the assessee adduced two reasons for the carve-out, viz., first that such costs resulted into benefits in future years and second that the exports made to the AEs were neutral to these costs.

32. Before we take up the assessee's argument for consideration, it is *sine qua non* to consider the nature of expenses considered as `Brand building' and hence excluded. Break-up of this amount for the A.Y. 2012-13 has been given on page 762 of the paper book, which consists of Employee cost of Rs.3.69 crore (out of total employee cost of Rs.4.77 crore) and Operating and administration expenses of Rs.7.28 crores (out of total Operating and administration expenses of Rs.8.25 crore). Thus it can be seen that Employees cost and Operating and administration expenses have been treated as `Brand building expenses' . What is the link between these expenses and brand building is difficult to comprehend. It can be seen with naked eyes that roughly 84% of total Employee costs and Operating and administration expenses have been sliced away and given an imaginary nomenclature of `Brand building expenses' for transfer pricing purpose only with an avowed object of shrinking the operating costs and resultantly boosting the operating profits so as to present a rosy picture for benchmarking. Thus we hold that the

expenses carved out by the assessee by claiming them to be towards brand building are ordinary operating expenses connected with the running of business and have no element of brand building. No authentic reasoning for such allocation or correlation has been established before us. The irony is that *por una parte* the assessee is claiming such huge expenses as deductions and filing the returns with spiraling losses of Rs.7.36 crore for the A.Y. 2012-13 and Rs.20.82 crores the A.Y. 2012-13; *por otra parte*, when it comes to the benchmarking, it is showing handsome operating profit rates of 49.44% and 16.61% by slicing away a major component of the operating costs incurred.

33. *Arguendo,* we proceed with the contention of the ld. AR that such expenses were brand building costs qualifying for exclusion. The first reason given is of futuristic perspective. Otherwise, there is no dispute as to the otherwise operating nature of the Employee cost and Operating & administrative expenses carved out by the assessee. On a specific query, it was admitted that the assessee started manufacturing operations from this year onwards and out of total sales of Rs.11.26 crores, domestic sales amounted to Rs.1.71

crores. It, therefore, transpires that the assessee incurred Employee cost and Operating & administrative expenses in relation to its manufactured products, which were sold in the year under consideration both in the domestic market to non-AEs and in the foreign market to the AEs. In such a situation, the assessee cannot justify the exclusion by correlating the same with its impact in the years to come. On a pertinent query, the ld. AR admitted that these costs were not capitalized in the books of account but were taken as revenue expenses for the year under consideration. Once these costs are incurred for the year in question and claimed as deduction in entirety in this year alone, we fail to understand as to how these can be correlated with the sales to be made in future years without capitalizing them for accounting or tax purpose.

34. If the contention is that such expenses, which are otherwise operating in nature, relate to the future years, then naturally such expenses should have formed part of the operating costs base for the future years. On a clarification in this regard, the ld. AR candidly admitted that such costs for both the years were not included in the operating cost base of any of the future years. This shows that albeit

the assessee claims to have incurred Rs.10.94 crores for the A.Y. 2012-13 and Rs.23.89 crores for the A.Y. 2013-14 as operating cost for the future years, but neither capitalized them in the accounts for the years under consideration nor included them in the operating costs base for any of the future years. If we accept the contention of assessee to exclude such expenses, then they will neither form part of operating cost base for the years under consideration nor in the future years though these have actually been granted deduction in the computation of total income for the years in question. As the so-called brand building exercise done by the assessee facilitated making of the sales in the years under consideration, we are in full agreement with the DRP that the expenses so carved out and excluded from the operating cost base were liable to be included back.

35. The second reason given by the ld. AR is that the brand building expenses have no relation with the sale of finished goods to the AEs and hence should be excluded. We again fail to appreciate as to how brand building exercise does not help in facilitating profit from sales to related parties. Every sale to the AEs has a

corresponding manufacturing also. A good brand not only helps in accelerating revenue side by pushing sales across the board to the related and unrelated parties but also reins in economies and efficiencies on the cost side – economies in terms of relatively cost-effective purchases of quality raw material and efficiencies in terms of having good and satisfied work force preferring to stick with an established and reputed brand thereby adding the value. Thus we do not countenance the contention that brand building exercise has no impact on the profitability from sales made to related parties.

36. Notwithstanding the above, we note that the working of the PLI under the TNMM for the A.Y. 2012-13, provided at the instance of the DRP, has been given on page 761 of the paper book. The starting point is total revenue from sale made to AEs and non-AEs in domestic market. In such a scenario all the operating costs – both for AE and non-AE transactions – need to be considered for determining the rate of Operating profit to Total cost. The transfer pricing addition will result only by applying the differential PLI rate (PLI of the assessee and PLI of the comparables) only on sales made to the AEs and not the entity level transactions.

37. The position which finally emerges is that neither the Employee Cost and Operating and administration expenses have any relation with the `brand building' nor even genuine brand building expenses can be excluded from the operating cost base on the facts and in the circumstances of the case. Thus the contention of the ld. AR for reducing the operating cost base with the expenses of Rs.10.94 for the A.Y. 2012-13 and Rs.23.89 crores for the A.Y. 2013-14 is repelled. To sum up, we hold that the DRP rightly ordered the inclusion of such costs in the operating cost base for computing the assessee's PLI for both the years under consideration.

38. But for the above, the ld. AR did not assail any other aspect of its own ALP determination presented before the DRP. We, therefore, accord our imprimatur to the final assessment orders making the above additions.

39. For the two years under consideration also, the assessee has raised additional ground contending that the reference made by the AO to the TPO for the second international transaction, without granting opportunity of hearing to the assessee, was contrary to law

and hence the assessment orders be declared as null and void. We have discussed this issue *in extenso* while disposing of the appeal for the A.Y. 2011-12 above. For the two years instantly before us, again the ALP determination by the TPO is confined to the only reported international transaction of sale made to the AEs. Unlike in the case of OIE, there is no second transaction referred by the AO to the TPO. Following the *raison d`etre* given for the preceding year, the additional grounds for these two years are also dismissed.

40. In the result, the appeal for the A.Y. 2011-12 is partly allowed for statistical purposes and the appeals for the A.Ys. 2012-13 and 2013-14 are dismissed.

Order pronounced in the Open Court on 30th August, 2021.

Sd/-	Sd/-
(S.S. VISWANETHRA RAVI)	**(R.S.SYAL)**
JUDICIAL MEMBER	**VICE PRESIDENT**

पुणे Pune; दिनांक Dated : 30th August, 2021
GCVSR/Satish

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order is forwarded to:

1. अपीलार्थी / The Appellant;
2. प्रत्यर्थी / The Respondent;
3. The DRP-3 (WZ), Mumbai
4. The concerned CIT, Pune
5. DR, ITAT, 'C' Bench, Pune
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

// True Copy //

Senior Private Secretary
आयकर अपीलीय अधिकरण ,पुणे / ITAT, Pune

		Date	
1.	Draft dictated on	25.8.2021	Sr.PS
2.	Draft placed before author	30.8.2021	Sr.PS
3.	Draft proposed & placed before the second member		JM
4.	Draft discussed/approved by Second Member.		JM
5.	Approved Draft comes to the Sr.PS/PS		Sr.PS
6.	Kept for pronouncement on		Sr.PS
7.	Date of uploading order		Sr.PS
8.	File sent to the Bench Clerk		Sr.PS
9.	Date on which file goes to the Head Clerk		
10.	Date on which file goes to the A.R.		
11.	Date of dispatch of Order.		

*