

**IN THE INCOME TAX APPELLATE TRIBUNAL, DELHI 'I-1' BENCH,
NEW DELHI (THROUGH VIDEO CONFERENCING)**

**BEFORE SHRI N.K. BILLAIYA, ACCOUNTANT MEMBER, AND
SHRI LALIET KUMAR, JUDICIAL MEMBER**

ITA No. 907/DEL/2021 [A.Y 2016-17]

Ikea Services India Pvt. Ltd.
Unit No. 421, DLF Tower -A,
Jasola District Centre
South Delhi, New Delhi

Vs.

The A.C.I.T.
Circle - 12 (2)
New Delhi

PAN : AACCI 8376 C

[Appellant]

[Respondent]

Date of Hearing : 28.09.2021
Date of Pronouncement : 01.10.2021

Assessee by : Shri Kanchan Kaushal, Adv.
Shri Ravi Sharma, Adv

Revenue by : Shri Surenderpal, CIT- DR

ORDER

PER N.K. BILLAIYA, ACCOUNTANT MEMBER,

This appeal by the assessee is preferred against order dated 29.06.2021 framed u/s 143(3) r.w.s 144C(13) r.w.s 144B of the Income-tax Act, 1961 [hereinafter referred to as 'The Act'] pertaining to A.Y. 2016-17.

2. The grievances of the assessee read as under:

"1. On the facts and circumstances of the case, and in law, the order passed by the National e- Assessment Centre, Delhi (Ld. AO) is bad in law and void ab-initio.

2. On the facts and circumstances of the case, and in law, the Deputy Commissioner of Income Tax - Income Tax & Transfer Pricing Delhi 2(1)(2) ('the Ld. TPO') (following the directions of the Ld. DRP), erred in enhancing the income of the Appellant by INR 43,01,97,828 holding that the Appellant's international transaction pertaining to provision of sourcing support services to its Associated Enterprises ('AEs') does not satisfy the arm's length principle envisaged under the Act and in doing so, the Ld. TPO/ the Ld. DRP have grossly erred in:

2.1 concluding the incorrect functional profile of the Appellant, thereby wrongly characterizing it as a trader and not as a service provider;

2.2 concluding that the Appellant has developed human resource and supply chain intangible for its AEs;

2.3 concluding that the Appellant is engaged in maximizing location savings for its AEs.

3. On the facts & circumstances of the case and in law, the Ld. TPO/ Ld. DRP have erred in disregarding the benchmarking approach adopted by the Appellant in its TP Documentation and including the Free on Board ('FOB') cost of the goods sourced directly by the AEs from the third party vendors in the cost base of the Appellant, for the purpose of computing the arm's length profit margin of the Appellant.

4. On the facts & circumstances of the case and in law, the Ld. TPO/Ld.DRP have erred in considering the cost incurred by unrelated enterprise to compute net profit margin of the Appellant while applying Transaction Net Margin Method ('TNMM').

5. Without prejudice to other grounds raised by the Appellant, on the facts & circumstances of the case and in law, the Ld. TPO/ Ld. DRP have erred in selecting companies carrying out trading activities as comparable to the Appellant's business of provision of sourcing support services for computation of alleged arm's length price and in doing so have grossly erred in selection of:

5.1 Shoppers Stop Limited;

5.2 Isha Natural Beauty Products & Wellness Private Limited;

5.3 Lifestyle International Private Limited;

5.4 Future Enterprises Limited;

5.5 Bioworld Merchandising (India) Private Limited;

5.6 Avenue Supermarts Limited;

5.7 V2 Retail Limited;

5.8 Parin Furniture Limited

All the above grounds are without prejudice to each other. The appellant craves leave to add, amend, vary, omit or substitute any of the aforesaid grounds of appeal at any time before or at the time of hearing of the appeal.

The Appellant prays that appropriate relief be granted based on the said grounds or on the facts and circumstances of the case."

3. The representatives of both the sides were heard at length, the case records carefully perused. Judicial decisions brought to our notice duly considered.

4. Briefly stated, the facts of the case are that the appellant company is a 100% subsidiary of Ingka Pro Holding BV Netherlands and is primarily engaged in the provision of sourcing support services to its Associated Enterprises [AEs]. The appellant operates on an assured return revenue model undertaking minimal/limited risk, making the services of the appellant having least complex operations and bears lesser share of risks.

5. The facts on record further show that the appellant, in the course of provision of sourcing support, is not involved in making any strategic sourcing decisions. It is primarily involved in identification and search of suppliers, obtaining offers and quotations, managing logistics and quality control check in performing its day-to-day functions. We find that the AE(s) undertake functions like strategy formulation for its sourcing business, selecting and approving new suppliers, negotiations with suppliers, claim management etc.

6. During the year under consideration, the appellant has entered into the following international transactions:

S. No.	Nature of transaction	Method	Value of transaction (in Rs.)
1.	<i>Provision of sourcing support services</i>	TNMM	919225248
2.	<i>Receipt of shared accounting services</i>		601559
3.	<i>Services provided to IKEA Foundation in relation to coordination activities</i>	TNMM	34194382
4.	<i>Reimbursement of expenses received/receivable</i>		5004999
5.	<i>Reimbursement of expenses paid/payable</i>	TNMM	6809652

8. The TPO noticed that the FOB value of the goods procured through assessee from India is Rs. 22,60,34,01,600/-. The TPO took this FOB value as cost base to calculate the remuneration of the assessee. Applying the median rate of 5.97% on the FOB value of 2260.34 crores, the TPO computed the remuneration at Rs. 1,34,94,23,076/-. Since the assessee has received compensation of Rs. 91,92,25,248/- the same was deducted and the balance amount of Rs. 43,01,97,828/- was added.

9. The assessee raised objections before the DRP but the same were dismissed.

10. As mentioned elsewhere, the entire TP approach was on the premise that the services of the appellant are akin to that of a trader and therefore, the TPO has selected the comparables identifying traders as comparables. We are of the considered view that the TPO has proceeded on an erroneous premise which has resulted into his TP adjustment erroneously.

11. Services performed by the assessee can be summarized as under:

SEARCHING OF SUPPLIERS

In the event that an AE intends to source a new product from India, IKEA Services (along with other sourcing support entities in respective countries) is informed on the product that needs to be sourced and, on the requirements, that the product which should be met. Search of suppliers is carried out basis guidelines and parameters provided by AE i.e. “The IKEA Way on Purchasing Home Furnishing Products” (IWAY). IWAY has been laid down by the AE, adhering to which all entities within the group conduct their business. AEs have also laid down specific guidelines (written document termed as I-START) which stipulates the procedure which is required to be followed by every sourcing entity within the group for identification, selection and starting up of suppliers.

OBTAINING OFFERS

IKEA Services obtains price quotations, delivery and other contractual terms for the suppliers located in India. IKEA Services then submits this

information to the relevant purchasing company, who alone has the authority to conclude purchase agreements with suppliers.

IKEA Services does not have the right to negotiate with suppliers or to make any decisions in regard to purchasing the goods.

PLACING OF ORDERS AND QUALITY CONTROL

When a purchasing contract has been successfully concluded between a purchasing company (AE) and a supplier, orders are generated electronically up to the maximum amount of products as included in the purchasing contract.

Prior to commencement of full-fledged production by supplier, sourcing entity/ the Appellant is required to ensure that the supplier complies with a working manual, which is formulated by AE namely, 'First Batch Production'. Purpose of First Batch Production is to ensure and verify that supplier understands the IKEA requirements and maintains appropriate production set up to deliver the right quality from the inception.

The Appellant, on direction and working manuals of the AE, inspects the entire manufacturing process including transportation and storage tests. Further, any cost incurred by the Appellant, due to commercial convenience is considered as part of total operating cost of the purpose of computing the margins to be earned.

TRANSPORT AND LOGISTICS

The Appellant scouts for potential transport service providers in India and obtains price quotations, delivery schedules and other terms from the carriers. The Appellant then submits this information to the relevant purchasing company (AE), which alone has the authority to enter into transport agreements with carriers. AE directly enters into contracts with the third party transport service provider and accordingly, all the cost related to transportation and logistics is borne directly by AE.

PAYMENT TO SUPPLIERS

The Appellant does not perform any role with respect to payments to be made by AE for the purchases. Invoices are directly raised by

suppliers on the AE. Accordingly, the AE is solely responsible for directly remitting payment to the suppliers.

OTHERS

The process of settlement of claims is performed by global Quality Support Center (“QSC”) team in China. The Appellant merely coordinates any claims in relation to defective or damaged goods produced by suppliers in its region or goods damaged during transport by the transport service providers in its region. However, any losses are not borne by the Appellant.

12. The assessee does not have any market risk, product liability risk, service liability risk, credit risk and price risk. The facts on record show that the assessee does not take part in purchase decisions. In fact, the assessee is not engaged and does not have any legal right to do so, in the activity relating to maintaining any stock of merchandise manufactured by vendors and/ or reselling the same to group’s retail entities on its own account. In other words, the assessee does not bear any risk associated with carrying/owing/maintaining stock of inventory.

13. In our considered view, the glaring fallacy in the approach of the TPO lies on the fact that he has adopted FOB cost of goods procured from India by the AEs through the assessee as cost base. In our considered view, this approach of the TPO is in complete disregard to the functional profile of the assessee. The assessee operates in a limited risk environment providing routine support services to group entities and accordingly, entitled to be remunerated based on assured return.

14. The Hon'ble High Court of Delhi in the case of Li and Fung India Ltd ITA No. 306 of 2012 has considered a similar quarrel. The most relevant part of the judgment is extracted hereinbelow:

"39...This Court is of opinion that to apply the TNMM, the assessee's net profit margin realized from international transactions had to be calculated only with reference to cost incurred by it, and not by any other entity, either third party vendors or the AE. Textually, and within the bounds of the text must the AO/TPO operate, Rule 10B(1)(e) does not enable consideration or imputation of cost incurred by third parties or unrelated enterprises to compute the assessee's net profit margin for application of the TNMM. Rule 10B(1)(e) recognizes that "the net profit margin realized by the enterprise from an international transaction entered into with an associated enterprise is computed

in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise ..." (emphasis supplied). It thus contemplates a determination of ALP with reference to the relevant factors (cost, assets, sales etc.) of the enterprise in question, i.e. the assessee, as opposed to the AE or any third party. The textual mandate, thus, is unambiguously clear.

40. The TPO's reasoning to enhance the assessee's cost base by considering the cost of manufacture and export of finished goods, i.e., ready-made garments by the third party vendors (which cost is certainly not the cost incurred by the assessee), is nowhere supported by the TNMM under Rule 10B(1)(e) of the Rules. Having determined that (TNMM) to be the most appropriate method, the only rules and norms prescribed in that regard could have been applied to determine whether the exercise indicated by the assessee yielded an ALP. The approach of the TPO and the tax authorities in essence imputes notional adjustment/income in the assessee's hands on the basis of a fixed percentage of the free on board value of export made by unrelated party vendors.

41. LFIL's computation of the operating profit margin (OP/TC per cent) by enhancing the cost base, i.e., by increasing the cost of the sales facilitated by LFIL leads to an arbitrary adjustment of its income, as such an alteration resides plainly outside the Rules and the provisions of the Act."

15. This judgment of the Hon'ble Jurisdictional High Court was followed by this Tribunal in the case of Mitsubishi Corporation India Pvt Ltd vide ITA No. 5042/DEL/2011. The relevant findings of the coordinate bench read as under:

"81. Clearly, therefore, it is impermissible to make notional additions in the cost base and thus take into account the costs which are not borne by the assessee. It is so opined by Hon'ble jurisdictional High Court on a careful analysis of rule 10B(1)(e)(i). It is, therefore, no longer open to the revenue authorities to reconstruct the financial statements of the assessee by including the cost of products incurred by the AEs, in respect of which services are rendered, in its reconstructed financial statements, and then putting the hypothetical trading profits, so arrived at in these reconstructed financial statements, to the tests for determining arms' length price. Respectfully following the esteemed views of Their Lordships, we hold that the adjustments carried out in the cost base of ALP computation, in respect of service fee/ commission segment, are indeed devoid of legally sustainable merits."

16. The TPO has not accepted the decision of the Hon'ble Jurisdictional High Court of Delhi in the case of Li & Fund [supra] solely on the ground that an appeal has been recommended before the Hon'ble Apex Court. In our considered view, when the operation of the decision of the Hon'ble Jurisdictional High Court has not been

suspended or stayed, it was mandatory upon the TPO to follow the binding decision of the Hon'ble Jurisdictional High Court.

17. Be that as it may, considering the facts of the case in totality, as discussed hereinabove, in light of the decision of the Hon'ble High Court of Delhi [supra], we set aside the TP adjustment made by the Assessing Officer and direct him to delete the addition of Rs. 43,01,97,828/-

18. In the result, the appeal of the assessee in ITA No. 907/DEL/2021 is allowed.

The order is pronounced in the open court on 01.10.2021.

Sd/-

[LALIET KUMAR]
JUDICIAL MEMBER

Sd/-

[N.K. BILLAIYA]
ACCOUNTANT MEMBER

Dated: September, 2021

VL/

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR

Asst. Registrar,
ITAT, New Delhi

Date of dictation	
Date on which the typed draft is placed before the dictating Member	
Date on which the typed draft is placed before the Other Member	
Date on which the approved draft comes to the Sr.PS/PS	
Date on which the fair order is placed before the Dictating Member for pronouncement	
Date on which the fair order comes back to the Sr.PS/PS	
Date on which the final order is uploaded on the website of ITAT	
Date on which the file goes to the Bench Clerk	
Date on which the file goes to the Head Clerk	
The date on which the file goes to the Assistant Registrar for signature on the order	
Date of dispatch of the Order	