INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "I-1": NEW DELHI
(Through Video Conferencing)

BEFORE
SHRI R.K. PANDA, ACCOUNTANT MEMBER
AND
SHRI SUDHANSHU SRIVASTAVA, JUDICIAL MEMBER

ITA Nos. 5444, 5445/Del/2016
Asstt. Years 2009-10, 2010-11

Minda Furukawa Electric Pvt. Ltd. Plot No. 68, Echelon Industrial Area, Sector -32 Gurgaon 122001 PAN AAFCM1986R	Vs.	DCIT Circle – 6(1) New Delhi.
Respondent		(Respondent)

Assessee by:	Shri Ajay Vohra, Sr. Advocate Shri Neeraj Jain, Advocate and Shri Ramit Katyal, Advocate
Department by:	Shri Surender Pal, CIT(DR)
Date of Hearing	14/09/2020
Date of pronouncement	27/11/2020

O R D E R

PER SUDHANSHU SRIVASTAVA, JUDICIAL MEMBER:

ITA No. 5444/Del/2016 is the assesee's appeal against order dated 27.4.2016 passed by the Ld. Commissioner of Income Tax (Appeals) – 44, New Delhi {CIT (A)} for assessment year 2009-10 whereas ITA No. 5445/Del/2016 is assessee's appeal against order dated 27.4.2016 passed by the Ld. CIT (A) – 44, New Delhi

{CIT (A)} for assessment year 2010-11. Since, both the appeals involved identical issues, they were taken up for hearing together and are being disposed of by this common order for the sake of convenience.

2.0 The brief facts of the case pertaining to assessment year 2009-10 are that the assessee is a 51:49 % joint venture between Minda Capital Limited (owning 49% of shareholding) and Furukawa Electric Co. Ltd and Furukawa Automotive Parts Inc. (jointly owning 51% shareholding). The assessee operates as a manufacturer of wiring harness and supplies the same to its customers which are mainly original equipment manufacturers operating in Indian Automobile Industry. For the purpose of manufacturing, the assessee has a plant at Bawal in Haryana where wiring harness for four wheelers and other components related to wiring harness for example couplers, terminals, relay box, junction box and steering roll connectors etc. are manufactured.

2.1 The return of income was filed declaring a loss of Rs. 34,41,93,072/- which was subsequently revised to a loss of Rs. 36,18,55,901/-. The case of the assessee was selected for scrutiny and since the assessee had entered into international

transactions during the year under consideration, a reference was made in terms of section 92CA(1) of the Income Tax Act, 1961 (hereinafter called the Act) to the Transfer Pricing Officer (TPO) for determining the Arms Length Price (ALP) of the international transactions undertaken by the assessee. The international transactions of the assessee were as under:-

Type Of International Transaction	Method Selected	AEs as Tested Party		Comparables	
		Total Value Of Transaction (Transfer Price)(Rs.)	Price/Margin	Findings	
				Arithmetic Mean Price/ Margin	Within 5%Range Of Transfer Price
Import Of Raw Materials, Components And Consumables	TNMM using Operating Profit/Operating Cost as PLI	60,75,17,457	6.60%	6.76%	NA
Import Of Machinery From Manufactured Stock	TNMM using Operating Profit/Operating Cost as PLI	61,28,139	6.60%	13.56%	NA
Import Of Machinery From Purchased Stock	CPM using Gross Proifit/ Cost of goods sold as PLI	4,10,11,392	6.70%	17.32%	NA
Payment Of Royalty	CUP method	52,74,122	3%	3.38%	NA
Reimbursement Of Expenses By AEs	No benchmarking required	14,84,001	cost recharge	NA	NA
Reimbursement Of Expenses To AEs	No benchmarking required	85,41,888	cost recharge	NA	NA

2.2 Although, the assessee had selected the foreign Associated Enterprise (AE) as the tested party, the TPO selected the assessee as the tested party and selected 99 companies having mean operating margin of 7.42% as comparable and made an adjustment of Rs. 28,48,58,529/- on account of international transactions undertaken by the assessee. The assessee's transfer pricing adjustment was computed by the TPO as under:-

Net operating margin of the appellant after considering adjustment on account of labour unrest	-52.76%
Net Sales of the appellant	47,33,44,182
Arm's length margin @ 7.42%	3,51,22,138
Net operating loss of the appellant	24,97,36,390
TP adjustment	28,48,58,529

2.3 Aggrieved, the assessee carried the matter before the Ld. First appellate authority agitating the transfer pricing adjustment. The Ld. CIT (A), however, upheld the transfer pricing adjustment made by the TPO by rejecting the selection of associated enterprise as the tested party and also rejected the claim of the assessee towards comparability adjustment.

2.4 Now the assessee is in appeal before this Tribunal challenging the transfer pricing adjustment and following grounds have been raised in this regard :-

1. *"That on the facts and in law, the Hon'ble Commissioner of Income Tax (Appeals) [herein after referred to as the "Hon'ble CIT (A)]" and the Learned Deputy Commissioner of Income-tax, Circle - 6(1), New Delhi (hereinafter referred to as the "Learned AO") erred in assessing the loss of the Appellant for assessment year 2009-10 at Rs. 75,954,460 as against the returned loss of Rs. 361,855,901.*

2. *That the Hon'ble CIT (A) and Learned Transfer Pricing Officer ("Learned TPO") have failed to appreciate that the Appellant is a 51:49 percent Joint Venture between two unrelated parties (i.e. Furukawa group, Japan and Minda Capital Limited, India), and that all transactions undertaken by the Appellant are rationally driven with a view to protect the commercial & economic interest of the JV partners.*

3. *That the Hon'ble CIT (A) and Learned TPO have arbitrarily rejected the scientific transaction-by-transaction analysis carried out by the Appellant which was consistent with the Indian transfer pricing regulations prescribed under the Income Tax Act, 1961 and Income Rules 1962. Further the Learned TPO erred in law in re-determining a price of the impugned international transactions, without appreciating that the circumstances necessitating such re-determination as mentioned in sub-section (3) of section 92C did not exist.*

4. *Without prejudice, the Hon'ble CIT (A) and Learned TPO have erred on facts and in law in undertaking a fresh transfer pricing analysis using the Appellant as the "tested*

party" ignoring the fact that it was only the first year of operations for the Appellant. Further, the Hon'ble CIT (A) and the Learned TPO committed another mistake by arbitrarily selecting a fresh set of 99 companies as comparable (simply assuming them to be somewhat comparable), without properly evaluating/screening these companies which in reality were completely non-comparable (for reasons such as being functionally different, having persistent losses, having significant related party transactions and /or even dealing in non-comparable products).

5. *Without prejudice to the above grounds, the Hon'ble CIT (A) and Learned TPO have failed to visualize the Appellant's various commercial needs arising out of unforeseen circumstances faced during the year and have myopically rejected the detailed explanations / evidences submitted by the Appellant during assessment and appellate proceedings. The Hon'ble CIT (A) and the Learned TPO have even ignored the jurisprudence that existed during the course of the proceedings on this subject, while rejecting Appellant's claim for appropriate adjustments to account for differences arising out of abnormal circumstances/business exigencies faced by the Appellant.*

6. *That the Hon'ble CIT (A) and Learned TPO have erred on facts and in circumstances in not giving due cognizance that FY 2008-09 is the first year of commercial operation for the Appellant and that reasonable adjustment to exclude expenses incurred prior to commencement of commercial*

production (such as expenses incurred on trial runs, presale samples, testing etc. amounting to INR 10 crores (approx.)) incurred by the Appellant during April to September of the subject year which have been debited to the Profit and Loss account. The Hon'ble CIT (A) and the Learned TPO have conveniently chosen to ignore the guidance provided under the Indian transfer pricing regul; and various decisions of the Hon'ble ITAT in this matter.

7. *That the Hon'ble CIT (A) and Learned TPO have grossly erred in not giving due cognizance to the fact that the Appellant experienced major labour unrest and strike during December to March of the subject year, due to which the its manufacturing operations were halted and as a result its installed capacity / production lines were fully un-utilized during these months. The Hon'ble CIT (A)/Learned TPO failed to exclude fixed costs (amounting to INR 2 crores (approx.)) which could not be recovered due to a halt in production on account of such unforeseen circumstances and severe business exigencies.*

8. *That the Hon'ble CIT (A) and Learned TPO has grossly erred in restricting the quantum of adjustment warranted on account of abnormal expenses additionally incurred by the Appellant due to strike and labour unrest (such as excess off-shore cost of production, rent for additional premises, legal expenses in relation to court proceedings for strike. other administrative and deputed personnel expenses etc.) to an*

ad-hoc 50 percent without giving any cogent basis for such determination.

9. *That the Hon'ble CIT (A) and Learned TPO has erred in not giving due cognizance to the fact that during the subject year approximately 85 percent of the Appellant's purchases comprised of imports from AEs which were considered necessary and expedient by the Appellant to fulfill its contractual obligations even amidst such business exigency. The Hon'ble CIT (A) and Learned TPO failed to acknowledge that the Appellant incurred significant non-recurring costs (in the form of statutory levy on imported goods, such as basic customs duty amounting to INR 2 crores (approx.) and freight amounting to INR 6.5 crores (approx.) which also need to be excluded while determining the net operating margin of the Appellant for the purpose of the transfer pricing analysis.*

10. *Without prejudice to ground no. 9, the Hon'ble CIT(A) and Learned TPO have erred on facts and circumstances that the Appellant was under strict contractual obligation with its domestic customer to supply goods (i.e. wiring harness) on a "Just-in-Time" basis. The Hon'ble CIT(A) and the Learned TPO failed to acknowledge that the short timelines for supply, extended significantly by the labour unrest, compelled the Appellant to import goods through air transport which costs approx. 9 times higher than freight cost through ship (which is cheaper and widely used mode of transportation in international trade), and thereby failed to allow adjustment on account of excess freight amounting to INR 6.5 crores (approx.).*

11. *That the Hon'ble CIT(A)/Learned TPO have erred in not giving due cognizance to the fact that the Appellant was exposed to unusually high foreign exchange fluctuation on account of imports which were imperative to meet its supply commitments under the contract with Maruti Suzuki India Limited ("Maruti"), and that the foreign exchange loss incurred by the Appellant was not covered for such fluctuations in its contract with Maruti, and these imports were a result of the labour unrest that the Appellant had to face for most of the subject year. The Learned CIT (A)/ Learned TPO failed to allow exclusion of such costs from the computation of Appellant's net operating margins for the year.*

12. *That the Hon'ble CIT(A) and Learned TPO have failed to make appropriate adjustments to account for differences in working capital employed by the Appellant vis-a-vis the comparables and in the process also ignored the provisions of the Indian transfer pricing regulations and judicial pronouncements of the Hon'ble ITAT on this subject.*

13. *Without prejudice, the Hon'ble CIT(A) and Learned TPO have adopted a flawed approach by using single year data and rejected Appellant's claim for use of multiple year data to compute the arm's length price of the international transaction of the Appellant using TNMM as the most appropriate method.*

14. *That the Hon'ble CIT (A) and Learned TPO have erred in not allowing benefit of 5 percent range as provided under the proviso to Section 92C(2) of the Act.*

15. *That the Hon'ble CIT (A) and Learned AO have erred in making an addition by disallowing the 10% of the staff welfare expenses on account of being excessive and high as compare to the previous year. However, such expenses have already been benchmarked by the learned TPO by considering the entire cost base of the Appellant including the staff welfare expenses, which has resulted in economic double taxation in the hands of the Appellant.*

16. *The learned AO has erred on facts and circumstances of the case by initiating the penalty proceedings under section 271(l)(c) of the Act against the Appellant, which is bad in law."*

2.5 Likewise, in assessment year 2010-11, the return of income was filed declaring a loss of Rs. 2,87,03,378/- which was subsequently revised declaring a loss of Rs. 3,39,77,500/-. After a reference was made to the Transfer Pricing Officer, an adjustment of Rs. 20,91,32,446/- was made on identical lines as in Assessment Year 2009-10. The assessee's appeal before the Ld. CIT (A) was dismissed in this assessment year as well and against this dismissal of the appeal, the assessee is before the Tribunal challenging the dismissal by raising the following grounds of appeal :-

1. *That on the facts and in law, the Learned Deputy Commissioner of Income-tax, Circle - 6(1), New Delhi (hereinafter referred to as "Learned AO") erred in assessing the income of the Appellant for the assessment year 2010-11 at Rs. 100,595,210 (after adjustment of brought forward losses amounting Rs. 75,954,460) as against the returned loss of Rs. (33,977,500).*

Grounds relating to Transfer Pricing Matters

2. *The Hon'ble Commissioner of Income Tax (Appeals) [herein after referred to as the "Hon'ble CIT (A)]" and the Learned Transfer Pricing Officer (herein after referred to as the "Learned TPO") have failed to appreciate that the Appellant is a 51:49 percent Joint Venture between two unrelated parties (i.e. Furukawa group, Japan and Minda Capital Limited, India), and that all transactions undertaken by the Appellant are rationally driven with a view to protect the commercial & economic interest of the JV partners.*

3. *The Hon'ble CIT (A) and Learned TPO have arbitrarily rejected the transaction-by- transaction analysis carried out by the Appellant which was consistent with the Indian transfer pricing regulations prescribed under the Income Tax Act, 1961 and Income Rules 1962. Further, the Hon'ble CIT (A)/Learned TPO erred in law in re-determining the price of the impugned international transactions, without appreciating that the circumstances necessitating such re-determination as mentioned in sub-section (3) of section 92C did not exist.*

4. *Without prejudice, the Hon'ble CIT (A) and Learned TPO have grossly erred on facts and in law in undertaking a fresh transfer pricing analysis the Appellant as the "tested party" and selecting mature comparable companies vis-a-vis the Appellant who were in there initial phase of commercial operations facing various abnormal circumstance and business exigency.*

5. *The Hon'ble CIT (A) and Learned TPO has erred on facts and in circumstances in not giving due cognizance to the fact that the Appellant experienced labour unrest/ strike in the previous year i.e. financial year 2008-09 which have a roll over effect in the current year as well. On this account, the Appellant has incurred certain exceptional expenditure (like emergency support service etc.) which needs to be eliminated while determining the financial profitability for the year.*

6. *The Hon'ble CIT (A) and Learned TPO has erred in not giving due cognizance to the fact that during the subject year approximately 64 percent of the Appellant's purchases comprised of imports from AEs which were considered necessary and expedient by the Appellant to fulfill its contractual obligations even amidst such business exigency. The Hon'ble CIT (A) and the Learned TPO failed to acknowledge that the Appellant incurred significant non-recurring costs (in the form of statutory levy on imported goods, such as basic customs duty and freight) which also need to be excluded while determining the net operating margin of the Appellant for the purpose of the transfer pricing analysis.*

7. *The Hon'ble CIT (A)/Learned TPO erred in computing the operating margins of the Appellant and has erroneously considered certain item of income/ expenses arising from the ordinary course of business, as non-operating in nature.*

8. *The Hon'ble CIT (A)/Learned TPO has erred in not allowing benefit of 5 percent range as provided under the proviso to Section 92C(2) of the Act.*

9. *The Hon'ble CIT (A)/Learned TPO has erred in the facts and circumstances of the case and in law in rejecting the Appellant's claim to use multiple year data for computing the ALP, and instead used single year updated data to conclude the price of the transaction.*

10. *The Learned AO erred in not allowing the set off of brought forward depreciation/loss pertaining to AY 2008-09 amounting to Rs. 2,14,09,236 against the assessed income for the current year.*

11. *Learned AO erred in giving lower credit of the TDS by Rs 77,754 and fail to give credit of fringe benefit tax deposited of Rs 500,000 while determining the tax demand due from the Appellant.*

12. *The Hon'ble CIT (A)/Learned AO erred in disallowing interest paid on late deposit of TDS.*

13. *Learned AO erred on facts and circumstances of the case by initiating the penalty proceedings under section 271(l)(c) of the Act against the Appellant, which is bad in law.*

3.0 With reference to assessee's appeal for assessment year 2009-10, The Ld. AR submitted that this assessment year was the second year of incorporation of the company but only the first year of operations as the commercial production had started only in September, 2008. It was submitted that the business operations of the assesee were adversely impacted due to labour unrest and strike experienced during the year as a result of which the assessee had incurred huge abnormal costs on account of rent of additional premises, legal expenses in relation to court proceedings and expenses on requisitioning the minimum required labour and administrative support from outside. It was further submitted that due to the strike and labour unrest, the

assessee was unable to utilize its installed capacity as a result of which it had incurred significant fixed costs which particularly remained unabsorbed during the year under consideration. The Ld. AR submitted that the assessee was under a strict contractual obligation with its domestic customer i.e. M/s Maruti Udyog Ltd. (Maruti) to supply wiring harness on just-in-time basis with very short supply time lines. It was further submitted that in order to meet the minimum supply obligations to Maruti, the assessee had no option but to source the supply of wiring harness from the associated enterprises and, therefore, the required supplies had to be imported for the purpose of supply to Maruti. It was further submitted that the non supply of wire harness would not only have meant complete loss of credibility of the assessee but would have also required the assessee to compensate Maruti for the loss borne by it due to non supply of wiring harness on time. It was submitted that, accordingly, the assessee had to incur excess costs such as purchase at a higher cost, air freight, custom duty etc besides incurring abnormal costs on account of labour unrest and strike.

3.1 It was submitted by the Ld. AR that due to various reasons, if the operating margin of the assessee was to be

calculated then due adjustment on account of each such factor needed to be quantified and allowed. It was further submitted that if it is not so done, then the operating margin of the assessee would not be a true indicator of the assessee's transfer price. It was submitted that it was due to these reasons that the assessee preferred the use of the AE as the tested party.

3.2 It was submitted that explanations along with relevant evidences had been submitted before the TPO but the TPO had subjectively brushed aside all the submissions of the assessee and had rejected the assessee's claim for use of the AE of the tested party for the determination of arms length of its international transactions. It was further submitted that the TPO had introduced a set of 99 comparable without proper evaluation. It was submitted that most of the 99 companies selected by the TPO were non-comparable for various reasons such as being functionally different, having persistent losses, having significant related party transactions etc.

3.3 The Ld. AR drew our attention to a chart placed at page 3 of the written submissions and submitted that this working for the adjusted operating margin of the assessee had duly been submitted before the TPO wherein the assessee's

margin, after making the comparability adjustment was 6.08% as compared to the operating loss of -52.76% as computed by the TPO. The said chart is reproduced hereunder for a ready reference:-

Particulars	Amount	Adjusted Margin	Page No.
Operating loss as per TPO (A) (Pg 88 of appeal folder)	-24,97,36,390	-52.76%	
Sales of the appellant	47,33,44,182		
Import Duty adjustment (Pg 16 of TPO order)(B)	1,98,14,011		4
Operating loss after import duty adjustment (C = A+B)	-22,99,22,379	-48.57%	
Freight Adjustment (Pg 16 of TP order) (D)	6,57,98,823		5
Operating loss after above adjustments (E = C+D)	-16,41,23,556	-34.67%	
Material cost adjustment (Pg 16 of TP order)(F)	3,97,17,323		6
Operating loss after above adjustments (G = E+F)	-12,44,06,233	-26.28%	
Pre-operative Expenses adjustment (Pg 16 of TP order) (H)	10,20,12,559		7-8
Operating loss after above adjustments (I = G+H)	-2,23,93,674	-4.73%	
Capacity utilization adjustment (Pg 16 of TPO order) (J)	2,14,75,752		9
Operating loss after above adjustments (K = I+J)	-9,17,922	-0.19%	
Abnormal expenses adjustment (50% allowed by TPO) (Pg 15 of TPO order) (L)	2,97,04,201		10
Operating profit after above adjustments (M = K+L)	2,87,86,279	6.08%	

3.4 It was submitted that adjustment for abnormal loss was allowed only @ 50% which has no basis. It was submitted that even the Ld. CIT (A) had not dealt with the assessee's submissions in the correct perspective and that he had chosen to

ignore the detailed submissions made by the assessee in this regard.

3.5 The Ld. AR also drew our attention to another chart at page 4 of the written submissions wherein it has been depicted that the excess import duty paid by the assessee due to increased imports was at Rs. 1,98,14,011/-. The said chart is also being reproduced herein under for ready reference:-

Particulars	Amount (Rs)
Basic custom duty paid by the appellant (A)	2,37,96,210
Imported goods as % of total raw material consumption in case of appellant (B)	85%
Imported goods as % of total raw material consumption in case of comparable companies (C)	14.22%
Adjusted import duty (D = A*(C/A)	39,82,198
Excess import duty paid (A-D)	1,98,14,011

3.6 Likewise, the Ld. AR submitted that due to strike and labour unrest the assessee had to incur excessive costs on freight and as per the assessee's calculation the assessee had to incur an excess expenditure of Rs. 6,57,98,823/- with respect to freight on air transport . It was also submitted that suitable adjustment with respect to material cost also needed to be allowed because in view of the production facilities having been halted, the assessee had to requisition the manufactured products from its AEs for which extra cost had to be incurred. The Ld. AR submitted that

suitable adjustment with respect to material cost also needed to be allowed. Apart from this, it was also the submission of the Ld. AR that suitable adjustment towards pre-operative expenses also needed to be allowed as the assessee was in the very initial stage of operations whereas the comparables selected by the TPO were all established players who were not required to incur such expenses.

3.7 It was also argued that due to labour unrest and strike, the assessee had operated at a significantly lower level of capacity utilisation of 32.60% as against the capacity utilisation of 68.50% of the selected comparable companies and, therefore, adjustment for capacity under-utilisation also needed to be allowed to the assessee company.

3.8 The Ld. AR also submitted that the assessee had incurred abnormal expenses to the tune of Rs. 5,94,08,402/- with respect to expenditure like rent, legal and professional fee, support services, travelling and conveyance due to strike and labour unrest and suitable adjustment in this regard was also required to be allowed while determining the arms length price.

3.9 With regard to the selection of comparable companies, the Ld. AR submitted that the selection by the TPO of 99 companies was totally incorrect in as far as the comparables were selected without undertaking the FAR analysis and qualitative screening of the business of such companies or examining the specific characters of products sold by companies and, therefore, the entire search process of the TPO was flawed. It was submitted that the assessee, during the course of proceedings before the TPO undertook a detailed qualitative screening of the business profile of the companies selected by the TPO and on the basis of said screening only 4 out of the 99 companies may be regarded as appropriate comparable for the purpose of benchmarking analysis which were namely Motherson Sumi, Suparjit Engineering, Minda Corporation and Remson Industries having an average mean margin of 7.57%. The Ld. AR drew our attention to a chart at page 12 of the written submissions having a reject/accept matrix wherein it has been stated that 7 companies were having high related party transactions, 13 companies were having insufficient information for undertaking the required analysis, one company was a persistent loss making company and 74 companies were having

non-comparable products. The Ld. AR submitted that in assessment year 2010-11, i.e. the subsequent assessment year, the TPO had selected only 5 companies as comparables as against 99 companies selected for this year.

3.10 The Ld. AR also submitted that the assessee should be allowed the benefit of working capital adjustment.

4.0 With respect to ITA No. 5445/Del/2016 for assessment year 2010-11, the Ld. AR submitted that the arguments advanced by him for assessment year 2009-10 would also apply *mutatis mutandis* in assessee's appeal for assessment year 2010-11 and that for the sake of brevity, the arguments were not being repeated. The Ld. AR submitted that the issues in assessment year 2010-11 being identical to issues in assessment year 2009-10, a similar view may be taken in both the appeals of the assessee.

5.0 In response, the Ld. CIT (DR) drew heavy support from the observations and findings of the Ld. CIT (A) while dismissing the assessee's appeal and submitted that the Ld. CIT (A) has given a categorical finding that the data given by the assessee to butteress its contentions were insufficient, evidences filed were sketchy and quantitative details were not available in

the audit report. The Ld. CIT (DR) submitted that the findings of the Ld. CIT (A) were findings of facts and the same deserved to be appreciated while considering the merits of the assessee's appeal with respect to the number of comparables selected by the TPO. The Ld. CIT (DR) submitted that the TPO has taken the entire spectrum into consideration and, therefore, selecting 99 comparables would have evened out the differences, if any. It was submitted that the assessee has challenged the comparables in a general manner without specifically pointing out facts in respect of each comparable. The Ld. CIT (DR) argued that when the relevant details were not properly made available, the assessee cannot plead to have been aggrieved. The Ld. CIT (DR) prayed that the assessee's appeals for both the years deserve to be dismissed.

6.0 We have heard the rival submissions and have also perused the material on record. We have gone through the findings and observations of the Ld. CIT (A) for both the years under consideration. We note that while rejecting the assesee's plea for not accepting the foreign AE as the tested party, the Ld. CIT (A) has relied on the reasoning given by the TPO in this regard wherein the main reason for rejection by the TPO is stated to be the absence of relatable data of foreign company. The Ld. CIT (A)

has also noted that the activities of the AE are as complex as the activities of the assessee and, therefore, it was always preferable to choose Indian comparables for benchmarking the international transactions. It has also been observed by the Ld. CIT (A) that only because there was a strike in the premises of the assessee during the year, the assessee cannot be left from being chosen as the tested party. However, we are of the view that although the Indian regulations do not lay down any specific procedure or guidelines for the choice of tested party, the OECD Transfer Pricing Guidelines and the US regulations provide some guidance for selection of the tested party. The OECD Guidelines on transfer pricing state that the least complex of the transacting entities shall be selected as the tested party for the purpose of undertaking benchmarking analysis. The relevant extract of the OECD Transfer Pricing Guidelines is as under:

> *"3.18 ……..The choice of the tested party should be consistent with the functional analysis of the transaction. As a general rule, the tested party is the one to which a transfer pricing method can be applied in the most reliable manner and for which the most reliable comparables can be found, i.e. it will most often be the one that has the less complex functional analysis. "*

6.1 We note that the TPO has not pointed out any deficiency in either the functional analysis undertaken by the assessee for the purpose of selection of tested party or in the reliability of data furnished by the assessee for undertaking benchmarking analysis taking the associated enterprise as the tested party. Accordingly, no cogent reason has been provided by the TPO for rejection of the associated enterprise as the tested party. From a perusal of Rule 10B(l)(e) it is seen that the Rules do not give priority to the selection of either the assessee or the associated enterprise as the tested party. The OECD guidelines on transfer pricing provide that the entity with simpler functional profile and for which most reliable comparables can be found should be selected as the tested party for the purpose of the benchmarking analysis:

> *"3.18 When applying a cost plus, resale price or transactional net margin method as described in Chapter II, it is necessary to choose the party to the transaction for which a financial indicator (mark-up on costs, gross margin, or net profit indicator) is tested. The choice of the tested party should be consistent with the functional analysis of the transaction. As a general rule, the tested party is the one to which a transfer pricing method can be applied in the most reliable manner and for which the most reliable comparables can be found,*

i.e. it will most often be the one that has the less complex functional analysis. ”

6.2 This view is also endorsed by the UN guidelines on transfer pricing. Para 5.3.3.1 of the guidelines states as under:

“5.3.3.1. When applying a cost plus, resale price or transactional net margin method it is necessary to choose the party to the transaction for which a financial indicator (mark-up on costs, gross margin, or net profit indicator) is tested. The choice of the tested party should be consistent with the functional analysis of the controlled transaction. Attributes of controlled transaction(s) will influence the selection of the tested party (where needed). The tested party normally should be the less complex party to the controlled transaction and should be the party in respect of which the most reliable data for comparability is available. It may be the local or the foreign party. "

6.3 It is further seen that the US TP regulations also provide for selection of the least complex entity as the tested party requiring fewest adjustments.

6.4 The Calcutta Bench of this Tribunal in the case of Development Consultants (P) Ltd. vs. DCIT, ITAT (Calcutta) (115 TTJ 577) has held as under:

“We agree with the view that in order to determine the most appropriate method for determining the arm's length price, it

is first necessary to select the 'tested party' and the tested party will be the least complex of the controlled taxpayer and will not own valuable intangible property or unique assets that distinguish it from potential uncontrolled comparables.

xxx xxx xxx

11. After due consideration of all the facts, we agree with the view that gross margins of DCIL need to be compared with gross margins of comparable uncontrolled transactions or unrelated enterprises entering into such transactions **"**

6.5 Further, the Delhi Bench the Tribunal in the case of Ranbaxy Laboratories Ltd. vs. Addl. CIT (ITAT Delhi) 299 ITR 175, too, has held that tested party should be the one which is least complex in the international transactional transaction, as under:

"58. We have also given careful thought to the other submissions of Shri Vohra. The tested party normally should be the party in respect of which reliable data for comparison is easily and readily available and fewest adjustments in computations are needed. It may be local or foreign entity, i.e., one parly to the transaction. The object of transfer pricing exercise is to gather reliable data, which can be considered without difficulty by both the parties, i.e., taxpayer and the revenue. It is also true that generally least of the complex controlled taxpayer should be taken as a tested party. But where comparable or almost comparable, controlled and

uncontrolled transactions or entities are available, it may not be right to eliminate them from consideration because they look to be complex…… **"**

6.6 Accordingly, while selecting the tested party for the purpose of applying the TNMM, the functional profile of the transacting entities is required to be taken into consideration and the entity having simpler functional profile i.e. the entity not assuming significant risks and employing non-routine intangibles should be selected as the tested party. We note that the assessee's objection being selected as a tested party were not dealt in the proper perspective by the Ld. CIT (A) and, therefore, this issue needs re-examination by the Ld. CIT (A).

6.7 Further, we also note that the TPO has selected 99 comparables without actually conducting FAR analysis in respect of each comparable and has undertaken the exercise of selection without applying any quantitative and qualitative filters. The TPO has also not assigned any reason for the selection of these comparables and the Ld. CIT (A) has also dismissed the assessee's objection against selection of these comparables without assigning any reason except by making general observations like that the data provided by the assessee was insufficient, the evidences were sketchy and that quantitative details were not

available. We are not in agreement with the summery dismissal of the objections of the assessee in this regard. We also note that the contention of the department that relevant details were not filed is wholly incorrect as we have gone through the voluminous evidences and data supplied by the assessee before the TPO as well as the Ld. CIT (A) in this regard. In a such situation, it is our considered opinion that the entire transfer pricing exercise needs to be done afresh by the TPO and, therefore, we restore the issue of transfer pricing adjustment to the file of the TPO for fresh analysis and verification for deciding the issue afresh after duly considering the detailed workings, arguments and evidences filed earlier by the assessee in this regard. The TPO is also directed to give proper opportunity to the assessee to present its case prior to passing a detailed order as per provision of law.

6.8 Other grounds raised by the assessee regarding initiation of penalty proceedings are dismissed as being premature.

6.9 Thus, ITA No. 5444/Del/2016 stands partly allowed for statistical purposes.

7.0 Since ITA No. 5445/Del/2016 is identical to ITA No. 5444/Del/2016, on similar reasoning, it is likewise restored to

the file of the TPO with identical directions. Thus, ITA No. 5445/Del/ 2016 also stands partly allowed for statistical purposes.

8.0 In the final result both the appeals of the assessee stand partly allowed for statistical purposes.

Order pronounced in the Open Court on 27th November, 2020.

sd/-	sd/-
(R.K. PANDA)	**(SUDHANSHU SRIVASTAVA)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Dated: 27/11/2020

Veena

Copy forwarded to

1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR
ITAT, New Delhi