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आयकर अपीलीय अधिकरण, मुंबई न्यायपीठ 'के', मुंबई ।

IN THE INCOME TAX APPELLATE TRIBUNAL MUMBAI BENCHES "K", MUMBAI

सर्वश्री आर.एस. स्याल, लेखा सदस्य एवं अमित शुक्ला, न्यायिक सदस्य, के समक्ष ।

Before Shri R.S.Syal, AM and Shri Amit Shukla, JM

ITA No.6460/Mum/2012 : Asst.Year 2008-2009

M/s.ThyssenKrupp Industries India Private Limited 154-C Mittal Towers, 15th Floor 210 Nariman Point, Mumbai – 400 021. **PAN : AAACK1947K.**	बनाम/ Vs.	The Addl.Commissioner of Income-tax Range 3(3) Mumbai.
(अपीलार्थी /Appellant)		(प्रत्यर्थी/Respondent)

अपीलार्थी की ओर से /**Appellant by : Shri P.J.Pardiwalla**

प्रत्यर्थी की ओर से /**Respondent by : Shri Ajeet Kumar Jain & Smt.Sasmita Misra**

सुनवाई की तारीख / **Date of Hearing : 19.02.2013**		घोषणा की तारीख / **Date of Pronouncement : 27.02.2013**

आदेश / O R D E R

Per R.S.Syal (AM) :

This appeal by the assessee is directed against the order dt. 25.09.2012 passed by the Assessing Officer u/s 143(3) read with section 144C(13) of the Income-tax Act, 1961 (hereinafter called `the Act') in relation to the assessment year 2008-2009.

2. First objection of the assessee in this appeal is against the making of adjustment to the tune of ₹5,10,61,123 in respect of international transactions relating to purchase of raw material and

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components and sale of finished goods. Briefly stated the facts of the case are that the assessee is engaged in the business of providing turnkey services for design, manufacture, supply, erection and commissioning of sugar plants, cement plants, bulk material handling equipment and steam and power generation plants. During the previous year relevant to the assessment year under consideration, it entered into certain international transactions with the Associated Enterprises (AEs) which were duly reported. A reference was made u/s 92CA(1) by the Assessing Officer (A.O.) to the Transfer Pricing Officer (TPO) for computation of Arm's Length Price (ALP) in relation to such international transactions. The TPO, vide his order dated 10.10.2011, proposed total adjustments to the extent of ₹11,01,10,403. Accordingly, the A.O. framed the draft assessment order. The assessee raised certain objections before the Dispute Resolution Panel (DRP) in respect of such proposed adjustments. The DRP gave certain directions to the A.O. The matter was reverted to the TPO for giving effect to the DRP's directions. In the order giving effect, the TPO reworked the adjustment on account of import of spares and equipments and sale of equipments / components at ₹5,10,61,123 as against its earlier proposed adjustment on this score at ₹6,72,06,437. The A.O. in his final order passed on 25.09.2012 made adjustment *inter alia,* of ₹5.10 crore on account of import of spares and equipments and also sale of equipments / components, against which the assessee has come up in appeal before us.

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3. The detailed facts leading to this adjustment are that the assessee provided turnkey services for design, manufacture, supply, erection and commissioning of sugar plants, cement plants, bulk material handling equipment, steam generators etc. While executing turnkey projects, the equipments required for installing the plant were either manufactured by the assessee or sourced from various vendors including its AEs. During the year in question the assessee imported spares and equipments from its AEs amounting to ₹23.48 crore and also exported certain equipments and components etc. to its AEs amounting to ₹82.23 crore. The assessee benchmarked these international transactions by using Transactional Net Margin Method (TNMM) as the most appropriate method by considering Profit Level Indicator (PLI) as Net Operating Margin to Sales (OP/Sales). The assessee submitted that it earned margin of 4.63% from its transaction with AEs as under:-

Particulars	Total (₹in million)
Sales / Operating Income	14184.18
Less : Operating Expenses	13527.88
Operating Profit	656.29
Operating profit / sales	4.63%

4. The assessee stated that the international transactions formed a small portion of less than 10% of its total turnover. During the course of hearing before TPO, the assessee submitted segmental data for AEs and Non-AEs as under:-

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(₹ in millions)

Particulars	AE	Non AE	Total
	(A)	(B)	(A+B)
Sales	3,225.85	10,615.19	13,841.04
Duty Drawback	--	1.75	1.75
Excise Duty	--	--	341.39
Operating Income (OI)	**3,225.85**	**10,616.93**	**14,184.18**
Excise duty	--	--	341.39
Material Consumption	2,375.63	9,148.41	11,524.04
Direct cost	244.48	382.83	627.31
Direct Overheads	316.41	375.48	691.88
Adm & Selling Overheads	78.48	264.78	343.26
Total Operating Cost (OC)	**3,014.99**	**10,171.50**	**13,527.88**
Operating Profit (OP)	**210.86**	**445.44**	**656.29**
OP/OC	**6.54%**	**4.20%**	**4.63%**

5. On the basis of the above Table, it was claimed that profit margin on sales from AEs segment at 6.54% was at arm's length as against 4.20% from Non-AEs segment. Accordingly, it was claimed that the transactions recorded in the books of account should be accepted at ALP. The TPO observed that the sales transactions were far in excess of the purchase transactions and hence the PLI of OP / Sales chosen by the assessee was incorrect. In his opinion, the correct PLI should be Operating profit to Total cost (OP/TC). On the perusal of the segmental details furnished by the assessee during the course of proceedings before him as tabulated above, the T.P.O. observed that the amount of AEs sales was shown at ₹322.58 crore while that of Non-AEs at ₹1061.69 crore. From the report in Form No. 3CEB, the TPO noticed that the quantum of total international transactions including sales, purchases and services was only at ₹137 crore. The assessee was confronted with this fact, upon which it was

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stated that some of the AE purchases had gone into the Non-AE sales and similarly some of the Non-AE purchases were reflected in the AE sales. The TPO observed that the assessee did not admittedly maintain segmental accounts for AE and Non-AE transactions and it was only for the purposes of transfer pricing proceedings that the audited segmental accounts were furnished by splitting the total figures. Due to such huge difference in the magnitude of international transactions, recording the AE sales alone in the segmental accounts at ₹322 crore and the total of international transactions at ₹137 crore in the report in Form No. 3CEB, the TPO came to hold that the figures of AE and Non-AE segments as produced during the course of proceedings before him, were not mutually exclusive. On further examination, he noticed that the ratio of the material consumed to sales in case of AE segment worked out at 73% whereas that of Non-AE segment was at 86%. This led to the difference of 13% (86% – 73%) in absolute terms and 17.8% in relative terms. In the backdrop of the foregoing factors, the TPO rejected the audited segmental account and entity level results, which were produced by the assessee in support of its contention that the internal TNMM should be applied to benchmark its profit from international transactions with its AEs.

6. As far as external TNMM is concerned, the assessee had originally selected six comparable cases in its Transfer Pricing study with the arithmetical mean of operating profit margin to sales at 4.36% as under:-

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Sr. No.	Name of the company	Average Operating Profit margin
1.	Walchandnagar Industries Limited	1.99%
2.	Gillanders Arbuthnot & Company Ltd.	4.19%
3.	TRF Limited	3.37%
4.	Mcnally Bharat Engg. Co. Ltd.	4.81%
5.	Sunil Hitech Engineers Limited	8.53%
6.	Tata Projects Limited	3.26%
	Arithmetic Mean	**4.36%**

7. As the assessee had chosen multiple year data in respect of the above six concerns for determining the above profit rates, the TPO required the assessee to furnish updated results of the comparable cases using data for the relevant year alone. The assessee furnished the following chart with four comparable cases:-

Sr. No.	Comparables	Operating profit margin for F.Y.2007-08 OP/TC
1.	Mcnally Bharat Engg. Co.Ltd.	6.93%
2.	Walchandnagar Industries Limited	6.35%
3.	Tata Projects	3.51%
4.	Gillanders Arbuthnot & Company Ltd. (Engineering Division)	5.97%
	Average	**5.69%**

8. On the perusal of the comparable cases indicated by the assessee in its transfer pricing report and those given during the course of proceedings, it was noticed that the assessee itself dropped two comparable cases chosen earlier, viz., TRF Limited and Sunil Hitech Engineers Limited. The first case was dropped due to the alleged higher related party transactions and the second due to functional

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differences. The TPO noticed that the assessee had selected Gillanders Arbuthnot & Company Ltd. as one of comparables. This company was found by him to be functionally different from that of the assessee for the reason that it was primarily into Cotton and man-made fibre yarn with 43.62% of its total turnover from this division alone. This enterprise also dealt with saleable tea which accounted for 16.94% of the total sales. In view of these facts, the TPO rejected this case as comparable as also for the reason that the assessee was engaged in the business of turnkey project, which this company was not. As the TPO was left with only three comparable cases from the assessee's list of cases, he conducted a fresh search with key phrase "turnkey project" and found five more comparable cases. After addressing to the assessee's objections to such cases, the TPO short listed total comparable cases to six by also including three cases left from the assessee's list of comparables. One case of TRF Limited, which was originally included by the assessee in its TP study but later on dropped, was also included. Two new cases, namely, Engineers India Limited and Sriram EPC were also included in the final list of six comparable cases as under:-

Sr. No.	Company	OP/TC%	OP/Sales %
1.	Tata Projects	4.98	4.74
2.	Walchandnagar Inds.	11.74	10.5
3.	Mcnally Bharat	11.92	10.65
4.	Engineers India Ltd.	14.17	12.42
5.	TRF Limited	20.85	17.25
6.	Sriram EPC	12.69	11.26
	Average	**12.725**	**11.13**

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9. As the assessee's PLI of OP/TC in respect of international transactions was found much below the average PLI of 12.72% of these six comparable cases, the TPO worked out an adjustment of ₹6.72 crore, which, pursuant to the direction given by the DRP, was subsequently reduced to ₹5.10 crore. It is this final adjustment of ₹5.10 crore, which the assessee is contesting in this appeal.

10. We have heard the rival submissions and perused the relevant material on record. The objections of the assessee in this regard are two-fold. First, that the internal TNMM ought to have been applied, and second, in the alternative, the AO/TPO were not justified in including certain fresh cases and excluding one case chosen by the assessee and also applying wrong profit rates in respect of such comparable cases finally chosen by the TPO under external TNMM. We would deal with both these objections one by one.

I. <u>Internal TNMM</u>

11.1. The learned Counsel for the assessee contended that the AO / TPO erred in rejecting the assessee's OP / OC at 6.54% in respect of international transactions with AEs which was better than 4.20% in respect of Non-AE transactions. He contended that the objection of the TPO on the difference in figures of ₹137 crore, being, international transactions given in the report by the assessee and quantum of AE sales at ₹322.58 crore given during the course of proceedings before him, was misconceived inasmuch as he failed to appreciate that all purchases from AEs, even if used for Non-AE

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projects, were considered as purchases of AEs and all the sales to AEs even if material used for those projects were purchased from Non-AEs were consolidated by the assessee in the figures of the AEs in the segmental accounts. It was argued that there was no other way out for determining profit margin in respect of transactions with AEs and Non-AEs. He further argued that the TPO was wrong in considering the ratio of material consumed to sales in the case of Non-AE segment at 86% as against that in the case of AE segment at 73%. It was pointed out that the TPO inadvertently considered figures of direct costs apart from material cost for working out ratio of material consumed to sales in respect of the Non-AE segment. He stated that such correct ratio was only 77% as against 86% originally considered by the TPO. In the light of the above arguments it was contended that when profit rate from internally comparable cases was available, then the internal TNMM should not have been disturbed. In the opposition, the learned Departmental Representative relied on the impugned order.

11.2. First thing which we need to determine is the extent of the reliability of the so called segment-wise figures of AE transactions and Non-AE transactions furnished by the assessee during the course of proceedings before the TPO for contending that the internal TNMM should be applied. Admittedly no such segment-wise accounts were maintained by the assessee. Such figures of AE and Non-AE transactions were segregated by the assessee from the common pool of figures. While making such classification and to

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demonstrate that its so-called profit rate under the TNMM from internal comparables was favourable to such profit rate from Non-AE transactions, the assessee also included in the sales of AEs, the amount of sales to Non-AEs for which the material was purchased from AEs and also included in the purchases of the AEs, the amount of purchases from Non-AEs for which the material was sold to the AEs.

11.3. Chapter X of the Act contemplates computation of income from international transaction having regard to arm's length price. Sub-section (1) of section 92 provides that : `Any income arising from an *international transaction* shall be computed having regard to the arm's length price.' Thus it is patent that the ALP is required to be computed in respect of an international transaction. The expression `International transaction' has been defined in section 92B. Sub-section (1) of this section provides that : `For the purposes of this section and sections 92, 92C, 92D and 92E, "international transaction" means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or ………'. The mechanism for computing the ALP in respect of an international transaction has been enshrined in section 92C of the Act. Sub-section (1) of this section provides that : `The arm's length price in relation to an international transaction shall be determined by any of the following methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions

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performed by such persons or such other relevant factors as the Board may prescribe, namely …..'. One of the prescribed methods, as has been applied by the assessee and accepted by the TPO as the most appropriate method, is TNMM. Before we proceed to examine the correctness of the application of this method, it would be apt to note the prescription of rule 10B(1)(e), which provides for the computation of ALP under the TNMM as under :-

> (e) transactional net margin method, by which,—
>
> (i) the net profit margin realised 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 or having regard to any other relevant base ;
>
> (ii) the net profit margin realised by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction or a number of such transactions is computed having regard to the same base ;
>
> (iii) the net profit margin referred to in sub-clause (ii) arising in comparable uncontrolled transactions is adjusted to take into account the differences, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises

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entering into such transactions, which could materially affect the amount of net profit margin in the open market;

(iv) the net profit margin realised by the enterprise and referred to in sub-clause (i) is established to be the same as the net profit margin referred to in sub-clause (iii) ;

(v) the net profit margin thus established is then taken into account to arrive at an arm's length price in relation to the international transaction.

11.4. It is relevant to note that sub-clause (i) of rule 10B(1)(e), which is first step in the computation of ALP under TNMM, talks of ascertaining the profit margin realised by the enterprise from an international transaction entered into with an associated enterprise. We have noticed the definition of `International transaction' above as a transaction between two or more associated enterprises. A bare perusal of this provision divulges that this step contemplates the determination of actual profit realized on transaction between two AEs. It is this profit margin which is scrutinized for determining as to whether or not it is at arm's length. The margin with which such margin earned by the assessee is compared with for determining the ALP, can be internally available from comparable transaction(s) or from externally available cases. If the enterprise has entered into similar transactions with third parties as are under consideration with

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the AE, then the profit realized from such transactions with third parties is a good measure to benchmark the margin from international transaction. Thus, on one hand we need to have profit margin which is to be compared from transactions with the AEs and on the other hand, we need to find out the profit margin from similar transactions with non-AEs with which comparison is to be made. Both these figures should come from separate watertight compartments. No overlapping is permissible in the composition of such compartments. In other words, neither the first compartment of profit margin from AE transactions should include profit margin from the transactions with non-AEs, nor the second compartment should have profit margin from the transactions with the AEs. If such an overlapping takes place, then the entire working is vitiated, thereby obliterating the finer line of distinction of the profit margin to be compared and the profit margin to be compared with.

11.5. Adverting to the facts of the instant case it is observed that the assessee is claiming sales to AEs at ₹322.58 crore and similar is the position regarding other components of operating costs including purchases. In such figures of purchases and sales from/to the AEs, not only the transactions with AEs but also certain transactions with Non-AEs stand included. Figure of purchases from AEs also includes purchases from Non-AEs where such purchases were used for sales to AEs. Similarly figure of sales to AEs also includes the figure of sales to Non-AEs where purchases from AEs were used for sales to Non-AEs. This shows that the figures of AE purchases and AE sales

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considered by the assessee for working out operating profit margin at 6.54% in respect of AEs also include Non-AE transactions. Such a course of action followed by the assessee to determine the profit margin from transactions with the AEs has absolutely no sanction of law. It rather defies and runs contrary to the very definition of `international transactions' and the mandate of rule 10B(1)(e). Approving the course of action adopted by the assessee for calculating profit margin in respect of AE and Non-AE segments would require rewriting of the relevant provisions as discussed supra. By considering some transactions with Non-AEs also as a part of the AE segment, the computation of the operating profit margin in respect of AE transactions at 6.54% has completely lost its significance. Once the figure of OP/OC margin at 6.54% is itself incorrect, there can be no question of comparing it with that of Non-AE segment at 4.20%, which again stands distorted because of the exclusion of certain purchases and sales from/to Non-AEs from this segment eventually finding their way into the AE segment. We, therefore, uphold the view taken by the authorities below on this count.

11.6. The next objection taken by the TPO in disregarding the figures furnished by the assessee as of AEs and Non-AEs is the difference in the ratio of material consumed to sales. The TPO worked out such percentage at 73% in respect of AE segment and 86% in respect of Non-AE segment in his original order. The DRP reduced such percentage in respect of Non-AE segment to 77%. It is

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this final figure of 77% which has been taken into account by the A.O. while making adjustment in his order u/s 143(3) read with section 144C(13) of the Act. In that view of the matter, there is no need on the part of the assessee to embark upon the ratio of material consumed to sales in Non-AE segment at 86%, which does not constitute the foundation for the ultimate transfer pricing adjustment. Restricting ourselves to the ratio of material consumed to sales in case of AE segment at 73% and in case of Non-AE segment at 77%, we find that still there is a difference of 4% in absolute terms. Once it is found that the ratio of material consumed to sales is different in case of AE and Non-AE segments, the otherwise comparability between two sets of transactions is also lost.

11.7. In view of the foregoing discussion, we are of the considered opinion that the authorities below were justified in rejecting the so called segmental accounts showing internally comparable margin of 4.20% computed by the assessee for the purposes of comparison with the margin of 6.54% from the international transactions with the associated enterprises.

II. <u>External TNMM</u>

12.1. Having held that the there is no valid basis for determining the internally comparable profit margin under TNMM, let us examine the case on the yardstick of external comparable cases. After taking into consideration the rival submissions, we find that the TPO made a final list of six comparable cases including three cases of Tata Projects Limited, Walchandnagar Industries Limited, Mcnally Bharat

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Engg. Co. Ltd. These three cases were included by the assessee in its transfer pricing study and also claimed as comparable during the course of proceedings before the TPO. There is no dispute on the inclusion of these three cases in the final list of comparables. However, the learned Counsel submitted that the TPO was wrong in calculating the ratio of OP / TC in respect of these cases. Certain objections in this regard were taken before the DRP. The A.O. was directed by the DRP to check the correctness of the ratio of OP / TC as contended by the assessee. Before passing final order u/s 143(3) / 144C(13), the A.O. requested the TPO to vet the correctness of the assessee's claim. The TPO verified this aspect and sent his report dated 17.09.2012 to the AO, who in turn gave effect to the working made by the TPO in his final order.

12.2. In respect of Tata Projects Limited, the TPO had earlier computed ratio of OP / TC at 4.98% which was reduced to 4.13% in the fresh calculation. The assessee is disputing this calculation also to the extent of exclusion of Amortization of value of investment and Provision for doubtful debts from the operating cost. Insofar as the Amortization of value of investment is concerned, we hardly see any relevance of this expenditure with the operations of the business. As regards the provision for doubtful debts, it is relevant to note that it is a provision which has been considered as non-operating and not the actual incurring of bad debts. Obviously a provision for doubtful debts cannot be considered as operating cost. We, therefore, uphold

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the calculation of OP / TC at 4.13% in respect of Tata Projects Limited.

12.3. Next is Walchandnagar Industries Limited. The TPO originally calculated OP / TC ratio at 11.74%. However, in the subsequent proceedings, such rate of OP / TC was reduced to 9.63%. Here also the assessee is assailing the exclusion of Depreciation transferred from revaluation reserve, Provision for doubtful debts and Expenditure capitalized from total operating expenses. In our considered opinion these three items have been rightly excluded as these have no relation with the operating cost. Depreciation transferred from revaluation reserve cannot be considered as operating cost. Similarly expenditure capitalized can in no sense be considered as operating cost. Provision for doubtful debts has been discussed above and held to be not an item of operating cost. We, therefore, approve the ratio of OP / TC at 9.63% as computed by the TPO in the second round.

12.4. Third comparable case is Mcnally Bharat Limited. Originally the TPO computed the ratio of OP / TC at 11.92%, which in the second round was reduced to 8.67%. Here again, the assessee is contesting the exclusion of three items of expenses from the total operating costs, viz., Bill discounting, Donation and Fixed assets written off. None of these items has any relevance with the operating costs. These three items again, in our considered opinion, have been rightly excluded by the TPO from the operating cost. Bill discounting is in nature of interest and obviously interest cost is a non-operating

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cost. Fixed assets written off are again a capital expenditure written off, which cannot be considered as operating cost. Donations are patently outside the ambit of operating cost.

12.5. We, therefore, hold that the revised calculation in respect of these three cases of ratio of OP / TC made by the TPO and finally adopted by the AO in his order for making adjustment, is perfectly in order and does not require any interference.

12.6.1. Next is the case of TRF Limited. The assessee's objections to this case are three-fold. First, that this case should not at all be considered as comparable ; second, if at all it is to be included in the list of comparables, then only the profit margin from the concerned segment should be taken as against the entity level margin taken by the TPO; and third, the correct profit margin should be applied.

12.6.2. It is interesting to note that the assessee initially included the case of TRF Limited in its list of comparables. However, in the revised list of comparables submitted during the course of proceedings before the TPO, the said case was excluded. However, the TPO included this case in the final list of comparables. The learned Counsel for the assessee contended that this case should not have been included because the related party transactions in this case are around 20%. It was argued that the assessee adopted filter of 10% of related party transactions for the purposes of inclusion of cases in the list of comparables. As this filter was not disturbed by the TPO,

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the learned AR argued that the case of TRF Ltd. ought to have been excluded. In the opposition, the learned Departmental Representative strongly supported the inclusion of this case in the list of comparables.

12.6.3. Having heard the rival submissions and perused the relevant material on record, we find that the related party transactions in this case are admittedly a little more than 20% but less than 25%. On page 11 of the order passed by the TPO, it can be seen that he adopted filter of related party transactions at 25%. In the case of *ACTIS Advisers Pvt. Ltd. v. DCIT [2012-TII-136-ITAT-DEL-TP],* the Delhi Bench of the Tribunal has held that a case can be taken as uncontrolled if its related parties transactions do not exceed 25% of the total revenue. In reaching this conclusion, the Tribunal took assistance from various provisions of the Act. Thus, it is discernible that the limit of 25%, though not expressly set out in the statute, cannot at the same time be branded as *ad hoc*. The Delhi Bench of the tribunal has taken assistance from certain other provisions of the Act for the adoption of such limit. Respectfully following the precedent, we approve the filter of 25% related transactions as adopted by the TPO in preference to 10% as applied by the assessee on *ad hoc* basis. Going by this filter, we find that since the related party transactions in the case of TRF Limited are less than 25%, the TPO was justified in admitting this case in the list of comparable cases. At this juncture, it is pertinent to mention that the assessee *suo motu* included this case in the list of comparables in its transfer pricing study when made on

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multiple year data (with average profit margin of 3.37%) . However when the TPO required the assessee to furnish data of the comparable cases only for the relevant year, the assessee found this case as incomparable because of a higher entity level/segmental OP/TC ratio for the relevant year. The manifest reason for the assessee's exclusion of this case is not far to seek. We, therefore, accept the filter of 25% as applied by the TPO and admit this case for inclusion in the list of comparable cases.

12.6.4. Next objection of the assessee is against considering the entity level results of TRF Ltd. The learned Counsel for the assessee contended that in its transfer pricing study, the assessee adopted segment level figures, whereas the TPO chose entity level profit results of this party. Referring to page 431 of the paper book, being, a copy of the annual report of TRF Limited for the relevant year, the learned Counsel submitted that this case has two segments, namely, Product & services and Project & services. As the assessee was engaged in the business of Project and services, the ld. AR urged that the results of Project & services segment should have been considered. In the opposition, the learned Departmental Representative invited our attention towards the same page giving segment-wise results. It was shown that the revenue of "Project & services" segment is ₹29782.65 lakh and that of the "Product & services" is ₹11551.07 lakh. Taking us through the break-up of revenue of Product & services segment, it was shown that it consisted of two parts, namely, External sales at ₹6501.88 lakh and Inter-

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segment revenue at ₹5049.19 lakh. Because of the inclusion of inter-segment revenue in the Product & services segment, the learned Departmental Representative contended that both the segments were rightly considered by the TPO as one unit. In the rejoinder, the learned AR submitted that the Inter-segment revenue was recorded at market driven agreed price as mentioned on the next page and in that view of the matter it would not affect the revenue of Projects & Services.

12.6.5. We find substance in the contention of the learned AR for adoption of results of "Project & services" segment of this comparable case instead of the entity level. There are only two segments of TRF Limited, viz., Product & services and Project & services. It has been rightly pointed out by the ld. DR that the total revenue of ₹11551.07 lakh of "Product & services" segment includes a substantial part comprising of Inter-segment revenue of ₹5049.19 lakh. It is evident that the amount of ₹5049.19 lakh is `Inter-segment revenue', which obviously refers to the goods or services supplied by the Product & services segment to the Project & Services. When the goods or services under Product segment are supplied at market rate, the separate profit of the Project segment will not get affected. It can be understood by a simple example of Product segment producing some goods at cost of say ₹ 90 and selling it to outside customers at ₹100, thereby earning profit of ₹10. When the same goods are sold to the Project division again at the same market rate of ₹100, the profit emerging from the sale of such goods at ₹10 stands included in the

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Product division under the head `Inter-segment revenue'. In so far as the Project division is concerned, it has purchased the goods at ₹100 from its Product division. Because of the transaction of purchase being at market value, the cost of goods to the Project division would have remained at ₹100 even if it had opted to purchase such goods from some outside party. Thus it is apparent that the profit of the Project division will remain neutral irrespective of the fact that the goods are purchased from outside parties or from own division at market price. The position would have been different if such goods had been transferred by the Product division to Project division at cost, in which case the profit of both the Project and Product divisions would have been needlessly affected, thereby deforming their correct profitability. As the revenue under the Project & services segment is complete in itself and is not influenced by the Inter-segment revenue shown under the Product division, in our considered opinion, the case of TRF Limited should have been considered as a comparable case on segment level.

12.6.6. The third objection of the ld. AR on this case is against the correct computation of rate of OP/TC. As we have set aside the action of the TPO in considering this case at entity level, it is directed to consider the segment level OP/TC ratio of this case for the purposes of computing the average profit rate of comparable cases. Needless to say, the assessee will be allowed a reasonable opportunity of being heard in this regard.

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12.7.1. Next is the case of Gillanders Arbuthnot & Company Ltd., which was included by the assessee in its final list of comparables submitted during the course of hearing before the TPO but the same was shunted out by the TPO on the ground that the said company is primarily into Cotton and man-made fiber yarn with 43.62% of total turnover under this segment. This enterprise was also found to have dealt with Saleable tea which accounted for 16.94% of the total turnover. The TPO observed on page 7 of his order that "this entity is not engaged in the business of turnkey project, hence rejected as comparable".

12.7.2. We find that the observations made by the TPO that Gillanders Arbuthnot & Company Ltd. is not engaged in the business of turnkey project, is incorrect. It is relevant to have a glance at page 681 of the paper book, being a copy of the Annual report of Gillanders Arbuthnot & Company Ltd., which contains information about its various business segments, such as, Trading, Tea, Property, Plastic Container, Textile and "Engineering Division". The same page contains information about the further break-up of the Engineering Division as comprising of manufacture and sale of "Steel Structurals, Pipes and equipments and Designing, Supplying, erectioning and Commissioning of projects on turnkey basis". From the above extract of the information given by the said company under the Engineering Division, it is vivid that it is also engaged in the business of projects on turnkey basis. It can further be noticed that the total revenue of this concern from Engineering Division is at ₹74.17

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crore. The TPO has excluded this case by mentioning that the said company is primarily engaged in man-made cotton fibre yarn and also saleable tea. We fail to appreciate this reason for the exclusion of this case on segment level because the revenue from the Engineering segment is ₹74.17 crore, which is much more than the assessee's uncontroverted filter of ₹25 crore minimum turnover. The revenue from the Engineering Division may be less in percentage terms on the entity level, but is substantial on the segment level. In our considered opinion, segmental results of Engineering Division of Gillanders Arbuthnot & Company Ltd. should have been included in the list of comparables. We, therefore, overturn the order of the authorities below on the exclusion of this case and direct to include the segmental results of the Engineering division of Gillanders Arbuthnot & Company Ltd. in the final list of comparables.

12.8.1. Next is the case of Engineers India Limited, which was included by the TPO at his own. The learned Counsel for the assessee contended that this case should be ignored because it is a Government Undertaking. It was further pointed out that most of its customers of the `Turnkey project division' are related parties, being, other Public Sector Undertakings, which is much more than the filter of 25%. The learned Departmental Representative, however, accentuated that the TPO was right in including this case in the list of comparables.

12.8.2. We find it as undisputed that Engineers India Limited is a Government company. It has several segments which also include `Turnkey project'. Page 700 of the paper book is a copy of annual

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report of Engineers India Limited on turnkey project. It can be seen that the revenue has arisen from completing Paraxylene Plant of IOCL and further that company is engaged in execution of other unit of IOCL's Panipat Naphtha Cracker Project. In our considered opinion, this case should not have been included in the list of final comparables for two reasons. First reason is that profit motive is not a relevant consideration in case of Government undertakings. Many Government Undertakings even operate on losses in furtherance of the social obligations of the government. The second reason is that Engineers India Limited earned income from turnkey project by successfully completing the project of IOCL and other Public Sector Undertakings. In that sense of the matter, the related party transactions are much more than the filter of 25%. We, therefore, order for the exclusion of this case from the list of comparables.

12.9. Last case which has been included by the TPO in his list of comparables is that of Sriram EPC Limited. This company is focused on providing turnkey solution for ferrous and non-ferrous, cement, aluminum, copper and thermal power plant. When we consider TNMM, it is the broader functional similarity which is considered. As the assessee is also engaged in the business of turnkey project, in our considered opinion, the TPO was right in including this case in the list of final comparables.

12.10. We, therefore, sum up our conclusion on inclusion or exclusion of cases in the final list drawn by the TPO. The cases of Tata Projects Limited, Walchandnagar Industries Limited, Mcnally

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Bharat Engg. Co. Limited and Sriram EPC Limited are held to have been rightly included. The case of TRF Limited is held to have been rightly included, but it should be considered on segment level instead of entity level as adopted by the TPO. The case of Engineers India Limited is directed to be excluded. The case of Gillanders Arbuthnot & Company Ltd. (on segment level) is directed to be included. In view of change in the list of comparable cases and also the composition in some cases, the AO / TPO are directed to re-compute the ALP in the light of our above discussion.

13.1. The next issue is against denying plus minus 5% benefit available under the proviso to section 92C(2) of the Act despite the direction issued by DRP to allow the same. The facts apropos this issue are that the TPO did not allow plus minus 5% benefit. The assessee challenged this aspect before the DRP contending that standard deduction of 5% ought to have been allowed. The DRP, vide para 15 of its order, directed to give the benefit of standard deduction of plus minus 5% to the ALP finally computed after giving effect to other directions given by it. However, when the matter came up before the AO for passing final order u/s 143(3) read with section 144C(13), he did not allow standard deduction of 5%.

13.2. The learned AR contended that the direction given by DRP was binding on the AO and the same ought to have been given effect to. In the opposition, the learned Departmental Representative

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submitted that there cannot be any question of allowing plus minus 5% standard deduction as such adjustment up to +-5% is allowable if the difference between the price charged or paid and the ALP is within this range.

13.3. We find no infirmity in the order passed by the A.O. in not granting any standard deduction of 5%. A statutory amendment has been carried out by the Finance Act, 2012 by inserting sub-section (2A) to section 92C with retrospective effect from 01.04.2002. The earlier confusion as to whether plus minus 5% is a standard deduction or allowable only if the difference between the price charged/paid in international transaction and ALP as determined is not more than 5%, has been put to rest by the Parliament. Now it has been mandated through the Finance Act, 2012 w.r.e.f. 1.4.2002 that plus minus 5% is not a standard deduction. It is significant to note that when the AO passed the impugned order on 25.09.2012, such amendment had already come into force. The consequences would have been different if the AO had allowed standard deduction of +-5% and the Revenue had orally challenged the grant of such standard deduction contrary to the provisions of law, without there being any legal recourse available to file appeal against the order of the AO u/s 143(3) read with section 144C(13) at the relevant point of time. The case before us is that the AO did not grant such standard deduction and we are required to ascertain as to whether or not his action is sustainable in law. As has been noticed above that the law as on the date as also retrospectively applicable to

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the relevant assessment year is against the granting of such standard deduction, we see no reason to hold that the assessee be allowed +- 5% standard deduction in contravention of the legal provisions. This benefit of up to 5% can be allowed only if the variation between the price charged / paid in respect of international transaction and ALP determined by taking the results of comparable cases does not exceed 5%. In case such variation is more than 5%, then no such benefit of 5% can be allowed on standard basis. As the matter of computation of ALP and the resultant addition, if any, has been restored by us to the AO/TPO in earlier paras, we direct that this point may be considered in accordance with our above observations.

14.1. The next issue is against the adjustment of ₹4,29,03,966 pertaining to payment of royalty. The facts concerning this issue as recorded in the order of the TPO are that the assessee obtained know-how and project-engineering drawings from its Associated Enterprise vide collaboration agreement dated 23.07.1996. As per this agreement, the assessee availed technical and engineering support for cement plant equipment and machinery. For availing the said manufacturing drawings and project engineering services, the assessee paid 2% of contract value to its AE and for know-how. It also paid royalty at 5% of the selling price to its AE. Royalty agreement between the assessee and Krupp Polysius AG was approved by Reserve Bank of India and FIPB. The assessee selected itself as the tested party and TNMM as the most appropriate method for benchmarking this transaction. The TPO noted that similar issue

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was involved in assessee's case for the assessment year 2007-2008. Following the view taken by him in earlier year, the TPO determined ALP at ₹Nil thereby proposing adjustment of ₹4.29 crore. The DRP also, following the view taken by it in the earlier year, declined to interfere with the order of the AO / TPO in respect of royalty payment.

14.2. The learned Counsel for the assessee contended that the said earlier year came up for adjudication before the Tribunal. Placing on record a copy of the order dated 27.11.2012 passed by the Tribunal in assessee's own case in ITA No.7032/Mum/2011 for the A.Y. 2007-08, the learned AR stated that this point has been decided in assessee's favour. The learned Departmental Representative, however, relied on the impugned order.

14.3. After considering the rival submissions and perusing the relevant material on record, we find that the assessee entered into collaboration agreement with its AE for payment of 2% of contract value for manufacturing, drawing and engineering services and 5% of the selling price as royalty. The assessee applied to the RBI seeking approval in respect of payment of royalty and technical fee through Central Bank of India. A copy of letter addressed by the Central Bank of India to the RBI dated 26.03.2008 is available on page 240 of the paper book. Through this letter, the Central Bank of India forwarded relevant documents along with a copy of the agreement. The RBI

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vide its letter dated 21.04.2008 requested Central Bank of India to consider the assessee's case in accordance with its AP(DIR Series) No.76 dated 24.02.2007. It is in pursuance to the deemed approval by RBI under the automatic approval scheme that the assessee made payment of royalty and technical fee to its AE. It is relevant to note that such payment has been approved or deemed to have been approved by the RBI. When a payment is made after obtaining due approval from the RBI, how its ALP can be computed at ₹Nil, is anybody's guess. The fact of approval of the payment by the RBI has been succinctly recorded by the TPO in his order as well. He still chose to propose adjustment in respect of full payment. In our considered opinion, when the rate of royalty payment and fee for drawings etc. has been approved or deemed to have been approved by the RBI, then such payment has to be considered at ALP. We, therefore, direct to delete addition of ₹4.29 crore made by the A.O. in this regard.

15. The next issue is against not giving credit of ₹23,30,040 for demand adjusted against refund for the assessment year 2007-2008 while determining the tax payable by the assessee. The Assessing Officer is directed to verify the factual aspect in this regard and pass appropriate order after allowing a reasonable opportunity of being heard to the assessee.

16. Last issue in this appeal against the charging of interest u/s 234B is consequential and accordingly disposed off.

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17. In the result, the appeal is partly allowed.

Order pronounced on this 27th day of February, 2013.
आदेश की घोषणा दिनांकः को की गई ।

Sd/-	Sd/-
(Amit Shukla)	**(R.S.Syal)**
न्यायिक सदस्य / JUDICIAL MEMBER	**लेखा सदस्य / ACCOUNTANT MEMBER**

मुंबई Mumbai; दिनांक Dated : 27th February, 2013.
Parida/Devdas*

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

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. आयकर आयुक्त(अपील) / The DRP-II, Mumbai.
4. आयकर आयुक्त / CIT
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, मुंबई / DR, ITAT, Mumbai
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

सत्यापित प्रति //True Copy//

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