

IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "G", NEW DELHI
BEFORE SHRI I.C. SUDHIR, JUDICIAL MEMBER
AND
SHRI SHAMIM YAHYA, ACCOUNTANT MEMBER
I.T.A. No. 5095/Del/2011

A.Y. : 2007-08

Sumitomo Corporation India Private Limited, 4 th floor, DLF Centre, Sansad Marg, New Delhi (PAN : AABCS 1887M) (Appellant)	vs. Deputy Commissioner of Income Tax, Circle 9(1), CR Building, ITO, New Delhi (Respondent)
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Assessee by	:	Sh. C.S. Aggarwal, Sr. Adv. & Sh. R.P. Mall, Adv.
Department by	:	Sh. Peeyush Jain, C.I.T.(D.R.)

ORDER

PER SHAMIM YAHYA: AM

This appeal by the Assessee is directed against the order of the Assessing Officer passed u/s. 143(3) read with section 144C of the I.T. Act for assessment year 2007-08.

2. The grounds raised read as under:-

1. That the learned Deputy Commissioner of Income Tax, Circle 9(1), New Delhi has erred both on facts and, in law in determining income of the Appellant at Rs. 70,71,96314/- in an order of assessment dated 25.10.2011 framed u/s 143(3) read with section 144C of the Act as against the declared income of Rs. 15,39,50,749/-.

2. That the learned Additional Director of Income Tax, Transfer Pricing Officer -11(2) New Delhi (Ld. TPO)/ Ld. AO have erred both in law and on facts in making an addition of Rs. 55,26,16,748/- on account of alleged understatement of arm's length price in respect of commission income earned by the Appellant from its Associated Enterprises ("hereinafter referred to as AE"). The aforesaid findings and conclusions have been reached without any material and is a vitiated finding.

3. That in making the aforesaid addition the learned Assistant Commissioner of Income Tax had erred in referring the matter to the learned TPO u/s 92CA of the Act on the following amongst other grounds, rendering the order of the TPO as unsustainable both in law and on facts:

a) As none of the pre-conditions laid down under section 92C(3) of the Act were satisfied,. there was no occasion for determination of arm's length price by the AO and the value of the international transactions ought to have been accepted;

b) As the reference made by the learned AO to the learned TPO is not in accordance with the provisions of Section 92CA(1) of the Act;

c) As no opportunity of being heard was granted at any stage of the proceedings for this purpose, whether at the proposal or the approval stage;

d) As no initial opinion was formed u/s 92C(3) of the Act which is a jurisdictional precondition;

e) By not furnishing the Letter of Reference ('LOR') to Appellant.

3.1 That since the reference by the learned AO was bad in law and void-ab-initio, consequentially the entire proceedings by the learned TPO, order of learned TPO, directions of Ld. DRP and, also the impugned addition of Rs. 55,26,16,7481- is vitiated, invalid, illegal and hence, a nullity.

4. The Order of Ld. AO & directions of Ld. DRP along with learned Transfer Pricing Officer's order under section 92CA(3) of the Act is based on complete disregard of the facts of the case of the Appellant and the statutory provisions of law.

4.1 The learned AO/TPO/DRP has in fact erred in their orders by disregarding the following objections apparent on facts and in law on the facts and circumstances of the case of the Appellant:

a) That the learned AO/TPO/DRP has erred in disregarding the transfer pricing approach adopted by the Appellant to determine the arm's length price ("ALP") of its international transactions. The Appellant's use of Transaction Net Margin Method ("TNMM") with Berry Ratio as the Profit Level Indicator ("PLI") has been discarded without any valid justification whatsoever;

b) That the learned AOITPOIDRP has erred in adopting his own method to determine the ALP of the Appellant's international transactions without demonstrating the existence of anyone of the four conditions provided in Section 92C(3) which is a mandatory requirement for making adjustment under section 92CA(3) of the Act;

c) That the learned TPO has erred in arbitrarily assuming and concluding that indent based transactions of the Appellant with its AE's have same functions and, risks as the principal transactions with non-AE's, the action of re-characterization of indent business as trading business is based on no valid basis;

d) That in absence of valid basis much less any valid material, the learned AO/TPO/DRP has erred in holding that, indent based transactions of the Appellant with AE's are comparable to principal transactions of non-AE's;

e) That the learned AOITPO/DRP having found the transactions entered into with non-AE's on identical circumstances are indent transactions i.e. service based transactions, he has erred in holding transactions and therefore, addition IS based on an inconsistent stand and, contradictory approach;

f) That the learned AO/TPO/DRP has failed to appreciate the difference in risk profile of the indent and proper transactions. In particular, in the indent based transactions there are negligible credit risk and foreign exchange risk on account of fluctuation of rate of exchange. In fact, in the indent based transactions, the function is to merely follow up on behalf of the customers and not deal with the prospective customers of the customers of the Appellant; the risk is limited to the commission amount and not to the gross amount of sales;

g) That the learned AO/TPO/DRP has overlooked that in respect of indent based transactions, service tax is applicable and in respect of principal based transactions, sales tax is applicable. Thus, apparently, the two transactions are different class of transactions;

h) Ld. DRP erred in stating that the Appellant has not provided conclusive evidence to show that the principal transactions and indent transactions are significantly different. Ld. DRP further erred in completely overlooking the additional evidences filed by the Appellant before the Ld. DRP on January 21, 2011 along with Form 35A. Thereby, the Ld. DRP operated with a pre-determined mindset to retain the adjustment made by Ld. TPO without adhering to the critical evidences furnished by the Appellant;

i) Ld. DRP erred in stating that the lease agreement dated 05.01.2007 between Omega Global Logistic Pvt. Ltd. & the Appellant is in relation to a fully furnished office space without verifying the Annexure 1 of the lease agreement which states that the premise is an office cum warehouse equipped with electrical connection, telephone connection, tables, chairs etc.

j) That the learned AO/TPO/DRP has failed to appreciate that, accountants report is merely an expression of opinion and, what is determinative is the real nature of transaction as held by Apex Court in the case of National Cement Mines Industries Ltd. v CIT reported in 42 ITR 69;

k) That the learned AO/TPO/DRP has erred in overlooking that, transactions made by the Appellant are of different product segments and, at different intervals and different volumes and, therefore, as such the indent transactions cannot be compared to the proper sales transactions.

l) That furthermore the learned AO/TPO/DRP has erred in comparing indent based transactions of AE's with principal based transactions of non-AE's and not with indent transaction of non-AE after allowing appropriate adjustments and, hence the addition is misconceived, misplaced and, unsustainable;

m) That the learned AO/TPO/DRP has erred in not making adjustments to the uncontrolled transaction to account for the material impact of the economic differences between the controlled and uncontrolled transactions as mandated under Rule 10B(3) of the Income Tax Rules 1962;

n) That the learned AO/TPO/DRP's method of computing the arm's length price is not in accordance with any of the methods specified in Section 92C(l);

o) That the learned AOITPO/DRP's conclusions are arbitrary and based on conjectures and surmises; and

5. That the learned AOITPOIDRP has erred in not making adjustments to the uncontrolled transaction to account for the material impact of the economic differences between the controlled and uncontrolled transactions as mandated under Rule 10B(3) of the Income Tax Rules 1961.

6. That the learned AOITPOIDRP has erred in holding that the Appellant has created human and supply chain intangibles for which it is not being adequately compensated by the AE.

7. That the learned AO/TPO/DRP has erred in adopting a transfer pricing approach that is different from the earlier year despite there

being no change in the facts and circumstances of the case of the Appellant.

8. That the Ld. AO/DRP has grossly erred both in law and, on facts in proposing a disallowance of a claim of expenditure of Rs. 3,72,560/- representing legal and, professional charges incurred wholly and exclusively for the purpose of business of the appellant company.

8.1 That the Ld. Assessing Officer and DRP has failed to appreciate that, mere fact that, such expenditure had been disallowed in the preceding years could not be a basis much less valid basis to hold that, expenditure incurred towards Writer Relocations was a personal expenditure. In fact, they have failed to appreciate that, it is well settled position of law that, a company does not have any personal expenditure and as such, entire expenditure incurred ought to have been allowed as such.

8.2 That the Ld. DRP has grossly erred both in law and, on facts in directing the AO to make the addition only if the department has not preferred an appeal before Hon'ble IT AT against the addition deleted by the CIT(A) in the AY 2006-07 on the similar ground.

9. That the Ld AO/DRP has further erred both in law and on facts in making a disallowance claim of deduction of deposits written off of Rs. 2,56,257/- on factually incorrect and, legally erroneous considerations and thus, the same is not tenable.

10. On the facts and circumstances of the case, the Ld. DRP has erred in not examining the validity of initiation of penalty proceedings u/s 271(1)(c).

11. The above grounds of appeal are mutually exclusive and without prejudice to each other.

The Appellant craves leave to add, alter, amend or vary any of the above grounds either before or at the time of hearing as we may be advised. The arguments taken hereinabove are without prejudice to each other.

Ground No. 1 to 7 – Transfer Pricing issue

3. M/s Sumitomo Corporation is a Japanese entity headquartered in Tokyo. Sumitomo Corporation is a main company of the Sumitomo Group. It is one of the largest trading companies or sogo shosho in Japan. A sogo shosho is an integrated business enterprise with the fundamental role of facilitating trade between buyers and sellers market. Sumitomo Corporation undertakes its trading activities in India through Sumitomo India. In case of import of goods for buyers in India, Sumitomo Corporation has a contract with the Japanese suppliers. Sumitomo Corporation also enters into contract with the buyers in India.

3.1 Sumitomo India, established in January, 1997 is a subsidiary company of Sumitomo Corporation. The trading transaction of the Sumitomo India can be classified into two groups - indent sales and proper sales. Indent can also be classified into - import from other country into India, export from India into other countries. In the Transfer Pricing report it was claimed that on its indent trading transactions, Sumitomo India's roles is that of a mere service provider. On these transaction, Sumitomo India earns income in the form of commission, generally based on the total invoice price or quantity of merchandise. Most of Sumitomo India's commission receivable on

these transactions are from Sumitomo Corporation. It was stated in the Transfer Pricing Report that Sumitomo India provides marketing support services for facilitating both exports and imports in India through Sumitomo Corporation. The support services include gathering information about customer requirements, products, local prices, market trend etc. During the financial year 2006-07 the assessee undertook the following international transactions :-

S.No.	Type of International transaction	Method selected	Total value of transaction (Rs.)
1	Purchase of goods	TNMM	102,825,122
2	Sale of goods	TNMM	1,294,773
3	Rendering of support services	TNMM	304,525,711
4	Interest earned	TNMM	722,621
5	Services received	TNMM	10,335,041
6	Reimbursement of expenses (payment)		628,502
7	Reimbursement of expenses (receipts)	TNMM	14,036,868

The assessee has benchmarked its international transaction relating to provision of rendering support services of Rs. 30.45 Crores using TNMM as the most appropriate method with Berry Ratio as PLI. The tested party margin of Sumitomo Corporation has been computed at 1.79%, whereas the result of 23 comparable companies weighted average arithmetic mean using three year data has been computed at 1.18%. The assessee has exercised option of $\pm 5\%$ under proviso to

sec. 92C(2) and has claimed its international transactions to be at arm's length. The assessee has claimed that its OP/TC margin is actually 79% as compared to mean average margin of comparable companies (from the business support segment) at 18%.

3.2 During the financial year 2006-07, the assessee had undertaken the following international transactions:

- i) Import of goods from AE
- ii) Export of goods to AE and
- iii) Rendering of support services to AE.

For benchmarking of the international transactions, the assessee had used Transnational Net Margin Method (TNMM) and PLI of Berry ratio. When the calculation of tested party margin in the TP report was examined by the Transfer Pricing Officer, it was noticed that the transactions relating to sales made in the AE and non AE segment had been aggregated and 'cost of sales' was deducted therefrom to arrive at 'Gross Profit Margin' with respect to the trading sales. With respect to other transactions, in which it was claimed that the assessee had only rendered services to AE, the commission and fee on such services has been calculated. The 'Gross Profit Margin' on the trading sales (AE and non AE segment) had been added to the commission earned (plus other income) to arrive at the numerator of the PLI i.e. Gross Profit on Sales. This numerator was then divided by 'operating expense' to arrive at computation of PLI of Berry ratio. Transfer Pricing Officer observed that on examination of the computation in the case of comparable companies, it was found that PLI had not been computed in the same manner as that of the tested party. Transfer Pricing

Officer observed that however, on examination of the computation of the tested party margin, it was noticed that the entire international transactions relating to sales and purchase of goods and commodities had remained out of computation of PLI. Most importantly, the cost of sales was not included in the denominator of PLI used. Transfer Pricing Officer asked the assessee to furnish the FOB value of goods on which commission had been received for purpose of determination of cost of goods sold. The assessee was also required to explain as to why Berry ratio was used to benchmark international transaction of the tested party. Transfer Pricing Officer noted that the Income Tax Act or Income Tax Rule do not permit the use of 'operating expenses' in the base which do not include the cost of sales. In accordance with the provision of Rule 10B(1)(e)(i) the net profit margin realized by the enterprise from an international transactions entered into with the associated enterprise is computed in relation to 'cost incurred' or 'sales effected' or 'assets employed' or 'to be employed' by the enterprise. He further observed that the provisions of Income Tax Act and IT Rules do not recognize the use of Berry ratio as an appropriate PLI under TNMM.

3.3 Vide submission dated 21.07.2010, assessee furnished the basis of computation of Berry ratio in the case of the tested party. However, it was not explained as to how the 'Gross Profit margin', i.e. the numerator has been arrived at in the case of the comparable companies in a similar manner as that of the tested party. Transfer Pricing Officer observed that numerator in the case of the tested party contains sales, cost of sales, commission and other income whereas in the case of comparables, no such division of incomes exists. Thus, Transfer Pricing Officer found the calculation on PLI in the case of the

tested party and in the case of the comparables has not been carried out as per provisions of the IT Act and it was proposed to reject the PLI adopted by the assessee to benchmark its international transactions.

4. Based on the aforesaid facts, Assessing Officer issued the detailed show-cause notice dated 30.9.2010. The relevant portion of the same as reproduced in the TPO order is as under:-

“2. During the FY 2006-07, relevant to AY 2007-08, you have undertaken the following international transactions:

- i) Import of goods from AE*
- ii) Export of goods to AE and*
- iii) Rendering of support services to AE.*

3. For benchmarking of the international transaction, you have used Transnational Net Margin Method (TNMM) and PLI of Berry ratio. When the calculation of tested party margin as submitted by you in the TP report was examined, it is noticed that you have aggregated the sales made in the AE and non AE segment and deducted therefrom the 'cost of sales' to arrive at 'Gross Profit Margin' with respect to the trading sales. With respect to your other transactions, in which it is claimed that you have only rendered services to your AE, the commission and fee on such services has been calculated. The 'Gross Profit Margin' on the trading sales (AE and non AE segment) has then been added to the commission earned (plus other Income) to arrive at the numerator of your PLI i.e. Gross Profit on Sales. This numerator has then been divided by 'operating expenses' to arrive at computation of PLI of Berry ratio. On examination of the computation in the case of comparable companies, it is found that

PLI has not been computed in the same manner as that of the tested party.

4. However, on examination of the computation of the tested party margin of the tested party margin, it is noticed that the entire international transactions relating to sales and purchase of goods and commodities have remained out of computation of PLI. Most importantly, the cost of sales is not included in the denominator of PLI used. For purposes of determination of cost of goods sold, you were required to furnish the FOB value of goods on which commission has been received vide this office letter dated 26.05.2010. You were also required to explain the adoption of Berry ratio to benchmark international transactions in the case of the tested party. You were also required to explain as to how 'Gross Profit' has been arrived in the case of the tested party. Further, you were required to state whether similar 'Gross Profit' and 'Cost' have been adopted in the case of comparables also.

5. It may be mentioned over here the Income Tax Act or Income Tax Rules do not permit the use of 'operating expenses' in the base which do not include the cost of sales. In accordance with the provision of Rule 10B(1)(e)(i) the net profit margin realized by the enterprise from an international transactions entered into with the associated enterprise is computed in relation to 'cost incurred' or 'sales effected' or 'assets employed' or 'to be employed' by the enterprise. The provisions of Income Tax Act and IT Rules do not recognize the use of Berry ratio as an appropriate PLI under TNMM.

6. Vide your submission dated 21.07.2010, you have furnished the basis of computation of Berry ratio in the case of the tested party.

However, ii has not been explained as to how the 'Gross Profit margin', i.e. the numerator has been arrived at in the case of the comparable companies. As has been analyzed above, the numerator in the case of the tested party contains sales, cost of sales, commission and other income whereas in the case of comparables, no such division of incomes exists. It is therefore found that the calculation of PLI in the case of the tested party and in the case of the comparables has not been carried out as per provisions of the I.T. Act and it is proposed to reject the P LI adopted by you to benchmark your international transactions.

7. Vide your submission dated 26.08.2010, you have provided FOB value of goods at Rs. 19,244,395,09/- on which you have received a commission of Rs. 221,977,7/1/- at an average commission rate of 1.15%. Vide your submission dated /4.09.2010, you have further provided that the total FOB value of goods traded through you is Rs. 20,102,188,471/- on which you have earned commission of Rs.. 237,656,747/- and service fee of Rs. 86,026,840/- totaling to Rs. 323,683,588/-. Vide your submission dated 14.09.2010, segmental accounts for Sumitomo Corp. India Pvt. Ltd as per Annexure-I have been/furnished as under:

Table-I

<i>Particulars</i>	<i>AEs</i>	<i>Non-AEs</i>	<i>Commission</i>	<i>Other income</i>	<i>Total</i>
<i>Direct income</i>					
<i>Sales</i>	108,020,767	148,125,537	--	--	256,146,304
<i>Commission</i>	--	--	323,683,588	--	323,683,588
<i>Other Income</i>				27,393,863	27,393,863
<i>Total (A)</i>	108,020,767	148,125,537	323,683,588	27,393,863	607,223,755

Direct expenses					
Cost of materials	102,825,123	137,861,103	--	--	240,686,226
Change in stock	--	3,665,508	--	--	3,665,508
Total (B)	102,825,123	141,526,611	--	--	244,351,734
Gross profit (C)= A-B	5,195,644	6,598,926	323,683,588	27,393,863	362,872,021
Segmental gross profit margin (as calculated)	4.80%	4.45%	1.61%		
Operating expenses					
Employee remuneration					61,522,635
Admin and other expenses					137,455,343
Interest and finance charges					343,331
Depreciation					6,199,011
Total operating expense (D)					205,520,320
Operating Profit (E)=C-D					157,351,701

8. From an analysis of the above computation, it is seen that in your trading transaction with your AE, you have earned a gross profit margin of 4.80%. In the segment relating to trading with non AEs, you have earned a gross profit margin of 4.4,%. However, with respect to commission income earned of Rs. 323,683,588/- on FOB value of goods traded through you of Rs. 20,102,188,471/-, which comes to 1.61%.

9. On the basis of detailed examination of FAR analysis in your TP report, it is noticed that there is no significant difference between the functions performed, assets utilized and risks assumed by you in your trading transaction with your AE and other trading transactions viz-a-viz the transactions performed by you wherein you have purportedly earned only commission income or a fixed fee. While analyzing the functions performed by you, it is also noticed that you are creating human intangibles and supply chain intangibles, for which apparently you are not being adequately compensated in your transactions with your AE. From the details mentioned in the TP report, it is found that Sumitomo India is creating following supply chain intangibles:

i) Sumitomo India maintains the relationship with the supplier on regular basis. Sumitomo Group helps in identifying the various customers and accordingly informs Sumitomo India for the requirements.

ii) Sumitomo India helps in connecting the supplier with Sumitomo Group.

iii) Sumitomo India has entered into various arrangements with different subsidiaries of Sumitomo Group and the main services among others include the following:

- Networking with buyers and suppliers of steel*
- Support in after sales services, business promotion*
- Collection of market information*
- Provide knowledge & experience*
- Coordination with customers*

- *Collection of Account Receivables from client on behalf of AE*
- *Administrative Services*

iv) Sumitomo India provides marketing support; service to Sumitomo group.

v) Sumitomo India handles different products and commodity through its different commodity departments.

10. You may therefore show-cause as to why the margin earned in your trading transaction in the non AE segment at 4.45% should not be adopted to compute the margin that you should have earned on the FOB value of the goods transacted through you."

5. In response to the show cause notice, the assessee submitted that its parent company, Sumitomo Corpn., Japan along with its group companies is a general trading group based in Japan. It was stated that assessee provides support services to its AE such as providing information to AE with respect to prospective supplier/customer economic and business conditions, custom clearance and communication channel between supplier and buyer. The assessee submitted that these are very low end services and decision making authority is the AE who is exposed to risks such as foreign exchange risk, debtors risk, quality risk etc. The assessee earns a service fee for the services it renders in the form of commission. The assessee has listed out the factors on which commission rate is decided. It is stated that commission rate depends upon business segments and market conditions. It was further submitted that in few cases, where volume involved is very small, assessee has taken title of goods. It was submitted that with respect to this small volume, it takes title to the goods which is flash title. The assessee has been characterized as

facilitator and coordinator for the FY 2006-07 and the very small quantity of trading business does not change the true identity of the company as above. Assessee classified transactions wherein trading takes place as Principle transactions and the transactions in which it receives commission as Indent transactions. Assessee submitted that on the basis of FAR analysis it has applied Berry ratio, which measures the gross profit earned in relation to operating expenses. The assessee submitted that it does not trade in any goods while performing the service of facilitation. It merely provides support service to AE. It was claimed that it does not assume title to the goods. Risks related to indenting business are not borne by the assessee. The assets employed in assumption of title of goods are different from service transactions. The reason for not including COGS (Cost of Goods sold) in denominator was that the assessee has characterized it self as a support service provider based on FAR analysis. The assessee submitted that this means that the business of the assessee is predominantly that of a service provider. The assessee claimed that it has selected similar business support comparables. It was claimed that exclusion of COGS in the denominator ensures an apple to apple comparison of the PLI of assessee viz-a-viz the comparables. The assessee submitted that the proposal to include COGS in the denominator by re-charactering commission/fee as return on sales was incorrect, arbitrary and unreasonable and contrary to transfer pricing principles. It was claimed that the cost as mentioned in Rule 10B (1)(e) does not include COGS because no such cost has been incurred by the assessee. The assessee

further quoted from Rule 10B(1)(e)(i) to state that the rules permit, "having regard to any other relevant base". The TPO observed that the assessee has stated that the activities quoted in the show cause notice were routine, preparatory and auxiliary in nature and can not be said to create any intangible. Assessee submitted it was carrying out facilitation service for its AE and does not partake in the supply chain activities. It was also submitted that it was not creating transferrable human intangible. Therefore, it is not creating any human or supply chain intangible. Assessee further submitted a matrix to state that the non AE trading segment cannot be compared with the service / commission segment. Assessee submitted following reasons for rejecting the argument that GP margin of 4.45% earned in the Non AE trading segment should be adopted to compute the margin that assessee should have earned on FOB value of goods on which it has earned commission / service income:

- * Lack of comparability between the two segments makes this approach completely untenable.
- * Higher margin in the non-AE trading segment arises from different functions, costs, assets and risks and other factors like difference in volume.
- * No justification in re-characterizing transactions entered into by the assessee without any reason in disregard to the business model adopted by the assessee. The assessee has selected service fee and commission model as one of its business models which constitute 95% of its business based on commercial factors. Therefore, the approach of thrusting the business model of principle business to service fee/ commission model is not correct.

* Assessee has stated that the AE perform more functions, assumes more risks and deploys more resources as compared to the assessee.

* The factual analysis in the show cause notice fortifies the assessee's stands of being at arm's length in respect of its international transactions. It has earned better margin in its trading transactions with its AE as compared to Non AE trading transactions.

5.1 Assessee submitted that the AE gross profit margin is lower than 4.45% even after performing more functions and more risks as compared to assessee.

6. Assessee submitted that without prejudice to its stand in the TP Study in regard to application of TNMM and Beery ratio and above arguments to justify arm's length nature of international transactions, assessee has stated that it earns commission income from AE and non-AE and therefore by the approach suggested in the how-cause notice (without admitting the same) commission earned by the assessee in the non AE service /commission segment may subject to economic adjustment mandated by law be considered as Benchmark commission to compute arm's length commission from AEs. Assessee submitted that during the financial year 2006-07 assessee has earned commission from Non-AEs @ 2.26% while it earned commission from AE @ 1.58%. The reasons for difference in percentage of commission earned was attributed to volume of business handled in AE segment and non AE segment and credit risk as associated in Non-AE segment. The assessee claimed that it earn commission from Non AEs @ 2.26% on the base value of Rs 847.249,524 whereas it has earned

commission from AEs @1.58% on base value of Rs. 19,254,938,946. In other words, it was claimed that Non AE segment constitutes merely 4.2% of the total commission/service business of the assessee. Therefore, it was claimed that economic adjustment as mandated under law, is required to improve the comparability between commissions earned in AE segment vis-a-vis commission earned in Non AE segment. It was further submitted that it was customary in commercial dealings of broker /commission agent to offer discount on the basis of volume or value of business generated. Similarly, commission/ brokerage charged from low value/small customers is much higher on account of premium rate of commission charged from them. The assessee further submitted that two instances of discount offered on the basis of volume of business. It was submitted that these details have been collected from the information available in the public domain. For the purpose of computing the economic adjustment on account of volume difference, assessee computes the average of the discount on the basis of said examples. Assessee came to conclusion that discount of 50% was applied on Non AE segment commission percentage to arrive at the arm's length commission percentage:

Non-AE commission percentage (A)	2.26%
Less: 50% of 2.26% (B)	1.13%
Arm's length commission percentage (A-B)	1.13%

6.1 It was claimed that the assessee has earned commission @ 1.58% as against the arm's length commission percentage of 1.13%. Therefore, commission earned in the AE segment is at arm's length.

Assessee further submitted that the analysis on the basis of TNMM and Berry ratio to justify arm's length nature of international transaction as per transfer pricing report should be accepted. It was submitted that assessee's business model nature of international transactions and transfer pricing methodology has remained unchanged since A.Y. 2003-04 and the same has been accepted by the Revenue. It was further submitted that before the Revenue embarks upon disturbing the method adopted by the assessee, it was incumbent on it to demonstrate that one of the four condition specified in sec 92C(3) was met.

7. TPO considered the above mentioned replies of the assessee. TPO observed that in understanding the business model of the assessee, it was essential to understand function performed; assets utilized; the risks undertaken (FAR analysis) by the assessee in performing both its functions under the Indent segment and the Principal Transaction segment. TPO observed that what was proposed in the show-cause notice was that the assessee in adopting the PLI of Berry Ratio has compared the gross profit margin it earns in its "Principal Transaction segment" with the commission/service fee it receives in the "Indent segment" and taken it as the numerator of its PLI a comparable. The TPO observed that assessee has clubbed the two incomes i.e. gross profit earned from the principal business and "commission/service fee" from the indent business in the numerator of its PLI. Transfer Pricing Officer further noted that it was explained that the transactions in the "Principle Transaction Segment" are back to back transaction and the FAR of trading transactions and indent transactions was exactly the same and therefore, they have been

clubbed together as overall GP and PLI of GP/OP expense has been selected under TNMM.

7.1 The TPO referred to the following table to better understand the computation of margin of the assessee

Table-I

Particulars	AEs	Non-AEs	Commission	Other income	Total
Direct income					
Sales	108,020,767	148,125,537	--	--	256,146,304
Commission	--	--	323,683,588	--	323,683,588
Other Income				27,393,863	27,393,863
Total (A)	108,020,767	148,125,537	323,683,588	27,393,863	607,223,755
Direct expenses					
Cost of materials	102,825,123	137,861,103	--	--	240,686,226
Change in stock	--	3,665,508	--	--	3,665,508
Total (B)	102,825,123	141,526,611	--	--	244,351,734
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Segmental gross profit margin (as calculated)	4.80%	4.45%	1.61%		
Operating expenses					
Employee remuneration					61,522,635
Admin and other expenses					137,455,343
Interest and finance charges					343,331
Depreciation					6,199,011

<i>Total operating expense (D)</i>					<i>205,520,320</i>
<i>Operating Profit (E)=C-D</i>					<i>157,351,701</i>

8. The Transfer Pricing Officer referred that in the show cause notice it was proposed that PLI as demonstrated in the table above does not capture the cost base on which the commission / service income has been earned whereas the gross profit margin of the trading segment contains cost of goods sold in the numerator. The cost base on which commission income has been earned, i.e. FOB value of goods traded through the assessee is Rs. 20,102,188,471/- on which commission /service fee of Rs. 323,683,588/- had been earned @1.61%. TPO observed that that the assessee was performing identical function utilizing the same assets and assuming nearly identical risks in both the 'Principle Transaction Segment' and the 'Indent Segment'. The assessee was required to show-cause as to why the margin it had earned in its non-AE trading segment at 4.45% should not be taken as a margin for the indent segment as well. In this connection, TPO referred to the FAR analysis in the TP Report. TPO further observed that assessee has itself stated that in the principal transaction segment the assessee Sumitomo India normally does not purchase product for re-sale, maintains no inventory. The purchase-sale transactions are essentially back to back transactions. Transfer Pricing Officer further noted that it was stated by the assessee in this segment the assessee performs high sea sales wherein no possession of the goods is taken by the assessee. TPO further observed from in the TP Report that assessee procures the

finished goods upon receiving the conformed order from its customers and the buy and sale price is also determined. Hence, such transactions are back to back involving minimal risk. Accordingly the gross profit margin earned for such sales and purchased can be compared with profitability of a service provider. TPO noted that assessee has thus submitted that the functional profile of 'Principle Transaction' and 'Agency Transactions' are comparable. TPO further referred to the transfer pricing report of the assessee and noted that it was evident from the same that the assessee has itself stated that assessee is performing the comparable functions or in effect similar function in both the segment. However, the assessee was earning GP margin @ 4.45% in its trading function in the non AE segment and a GP margin of 4.80% in its trading function in AE related trading as against it a GP margin of only 1.61 % in its Indent segment. TPO further referred to the function performed, assets utilized and risk assumed by the assessee. From this TPO mentioned that it was obvious that assessee was performing identical transactions in both the segments. TPO further observed that he had examined the compensation model along with the facts of the case and reached a conclusion, that In this case commission should be expressed as percentage of FOB price of goods sourced through the assessee for the following reasons:-

“(a) It is evident from the FAR analysis discussed earlier in this order that the assessee has played a major role in identifying suppliers, raw material, networking with buyers and suppliers, support in after sales services, business promotion, collection of market information, collection of accounts receivable on behalf of AE, handling of precuts and commodities etc. has been in constant touch with the buyer. It has assumed significant risks and has used

both its tangibles and unique intangibles. These facts clearly prove that value addition activities of the assessee can only be expressed as a percentage of FOB of goods sourced through the assessee.

(b) The assessee is operating in a low cost country like India and its operating cost is so low that it is a very poor proxy of the value it adds.

(c) The assessee has developed unique intangibles like supply chain management intangibles and human asset intangible which has resulted in huge commercial and strategic advantage to the AE and these intangible have enhanced the profit potential of the AE. However, these intangibles did not form part of the operation cost. Accordingly, the value addition made by the assessee to the FOB value the goods sourced through it remained unremunerated and commission/service income model does not capture the compensation for value addition made through these intangibles. Accordingly commission should be computed on FOB value of goods.

(d) Most importantly, as has been discussed above, part of the income in the numerator has been calculated as gross margin on cost of goods sold. However, for the commission / service income i.e. FOB value of goods traded through the assessee of ₹ 20,102,188,471/- on which commission/ service fee of Rs. 323,683,588/- has been earned has been completely ignored while calculating the said income.”

9. In view of the above finding, TPO held that the correct compensation model at arm's length price, in this case, would be commission of FOB cost of goods sourced from India. TPO further observed that the of IT Act and IT Rules do not recognize Berry ratio as

appropriate PLI under TNMM. TPO referring to the Rule 10B()(e)(i) observed that the rules prescribed that net profit margin should be computed in relation to the cost incurred or sales effected or the assets employed or to be employed. He observed that the rules do not prescribe for value added cost or value added or cost added expenditure to be considered as base for computing the net profit margins. Accordingly, TPO held that the claim of the assessee for use of berry ratio was not acceptable being contrary to Rule 10B(1)(e). TPO reiterated that the PLI used by the assessee does not capture the FOB value of the goods transacted through the assessee.

10. TPO further observed that assessee is creating the human chain and supply chain intangible for which it is not being adequately compensated by the AE. TPO further observed in this case the assessee has borne all the major risk associated with above referred to functions. In addition to this the assessee has also borne following major business risks such as single customer risk; risk associated with development and use of intangibles. He observed that assessee has used its assets including human assets (technical manpower) to discharge the function. TPO observed that on examining the compensation model in this case, it was noted that the assessee was allowed a very nominal and routine compensation of 1.6% on the service it renders (which does not include cost of development and use of intangibles) without allocating any profit component for development and use of unique intangibles by the assessee which has resulted in huge commercial and strategic advantage to the AE in the form of low cost of goods, high profit margin and assured timely supply and demand of quality goods and orders i.e. these intangibles have enhanced the profit potential of the AE, without any corresponding

markup to the assessee. Accordingly, he held that he was of the opinion that compensation model used by the AE is not the appropriate model because it does not capture the compensation for the development and use of intangible.

10.1 TPO further observed that there was no difference in the FAR of the trading segment as compared to the service / commission segment. He observed that assessee has not been able to offer any explanation as to why it has earned gross margin of 4.80% in identical transactions of trading with AE (where goods are not even transferred and the sales and purchase take place on high seas). TPO further referred to the assessee's arguments regarding the volume. He noted that assessee has argued that the indent segment constitute 95% of its business, whereas the trading segment constitute only 5% of its business. The TPO further noted that assessee company only provides marketing support and other support services in the indent segment. He noted that as per the assessee there is no assumption of title in the indent segment and therefore, the commission earned is adequate compensation for service provided. TPO noted that assessee in its TP report has calculated the return earned on its total costs to demonstrate that it has been adequately compensated for its services as compared with similar business support service providers.

10.2 TPO further observed that the compensation model of the assessee is not based on the service that it renders. For each and every transaction the assessee enters into, a separate contract is signed the compensation model of the assessee was determined based on the value or volume of the individual transaction/ contract that the assessee enters into with its AE. TPO further observed that this

compensation is not linked to the cost of the service but to the value or volume of each individual transaction. Therefore, the compensation received by the assessee for each individual transaction in the indent segment in the form of commission / service fee is the controlled international transaction in the case of the assessee. Thus, TPO observed that the compensation model of the assessee was thus clearly linked to the FOB value of the goods transacted through it. TPO further observed that the arguments of the assessee that volume of business in the case of indent segment is much larger than the trading segment, was also therefore, not found to be correct. He observed that assessee enters into a separate contract with respect to each and every transaction / trade i.e. carried out through the assessee. The compensation basis is mentioned in that contract. TPO observed that it is not the case of the assessee that the volume in single transaction is more than in similar transaction in the trading segment. Therefore, the TPO observed that the correct comparison was therefore, the gross margin that the assessee is making in the trading segment (Principle Transaction Segment) with the commission / service income earned in the indent segment.

10.3 TPO further observed that on the basis of FAR analysis it has been established that the assessee was performing identical function in both the segments, it is utilizing common assets (including supply chain and human intangible assets) and was performing identical risks in both the segments. He observed that in the trading segment the assessee does not also take possession of goods as sales made are high seas sales. TPO further noted that another argument taken by the assessee that its service / commission model has been re-characterised. Referring to his findings in the preceding paragraphs,

the Transfer Pricing Officer observed that it has been explained above that the compensation model of the assessee has been analysed based on each international transactions and not re-characterisation has been done. The TPO further noted that assessee has submitted the AE performs more functions, assumes more risks and deploys more resources as compared to the assessee. In this connection, assessee gave risk matrix between the assessee and the assessee AE. Based on FAR matrix, assessee has stated that the AE's gross profit margin is lower than 4.45% even after performing more functions and more risks as compared to assessee. Assessee further submitted that assessee cannot earn more gross profit margin than AE itself. TPO observed that assessee has stated AE's gross profit margin is lower than the @4.45% proposed in the case of the assessee. TPO noted that however, the AE generates huge turnover from its global business and large number of AEs located across the globe. The business that is carried out in India is leveraged out of the presence of the assessee in India since 1997 wherein assessee has established huge intangibles as discussed above on account of doing business in India for a long period of time.

11. In the following paragraph, the TPO dealt the without prejudice stand of the assessee:-

"7 Without prejudice stand :

Assessee has stated that without prejudice to its stand in the TP study in regard to application of TNMM and Berry ratio and above arguments to justify arm's length nature of international transactions, assessee has stated that it earns commission income from AEs and non-AEs and therefore by the approach suggested in

the show-cause notice (without admitting the same), commission earned by the assessee in the non-AE service/commission segment may, subject to economic adjustments mandated by law, be considered benchmark commission to compute arm's length commission from AEs.

The above stated stand taken in the letter dated 19.10.2010 has been considered. Herein the assessee has although without prejudice, but has admitted that for some minor transactions of Rs. 84.72 Crs (as compared with total trading transaction of Rs. 2010 Crs) which the assessee has carried out with non-AEs, assessee has earned a higher margin of @ 2.26% as compared with commission @ 1.58% from AE transactions. However, assessee has again without prejudice stated that 'volume' may impact the rate of commission. Assessee has stated that as the volume in non-AE segment was lower, it had earned a higher rate of commission.

It has already been demonstrated above, in Para 8.6.2 that 'volumes' do not impact the rate and amount of commission that the assessee receives. For each and every single transaction, a separate contract is entered into and the commission rate / service fee is mentioned in the contract. Even at the risk of repetition, it is found that it is not the case of the assessee that the volume of a single transaction is more than a single transaction in either the non-AE commission segment, non AE trading segment or the AE trading segment. It has been demonstrated in the order above, that the assessee is earning less gross margin for goods transacted with AE on which it earns commission / service income as compared with gross margin in the trading segment. The assessee in its alternative, without prejudice submission has also demonstrated that the commission / service income earned from AE does not

represent arm's length remuneration as compared with commission / service income earned under uncontrolled circumstances in the non-AE segment."

12. TPO further referred to the assessee's submission that its business model, nature of international transactions and transfer pricing methodology has remained unchanged since A.Y. 2003-04 and the same has been accepted by the Revenue. In this regard, TPO held that the assessee has misdirected itself in placing reliance of the earlier order. He noted that assumption of risk and function carried out by the assessee with respect to trading segment of indent segment had been independently reexamined in the case of the assessee, based on the facts and circumstances of its case in this order.

13. In view of the above discussion in the TPO's order the TPO has concluded as under:-

"9. Determination of arm's length price:

Based on above analysis and detailed arguments made in the order, it is therefore held that the assessee has not received arm's length remuneration in the form of commission/service income in the AE segment. The assessee in its submission dated 19.10.2010 has calculated that it has earned commission from AE @1.58% on base value of Rs. 19,254,938,946/- (the original figure of FOB value of goods given by the assessee in submission dated 14.9.2010 was Rs. 20,102,188,471/-. However, assessee in its submission dated 19.10.2010 has stated that this figure also contains certain non-AE transactions on which it has earned commission income also. The correct FOB value of transactions with AE and rate of commission earned is as stated). The gross margin earned in the non-AE trading

segment @ 4.45% shall be taken to be the arm's length rate at which assessee should have earned its commission income.

Commission Income earned from AE @1.58% on Rs. 19,254,938,946/- = Rs. 304,228,035/-

Arm's length commission income @4.45% on Rs. 19,254,938,946/- RS.856,844,783/-

Difference = Rs .552,616,748/-

% of arm's length margin to international transaction= 181.64%

The difference of adjustment required is more than 5% therefore proviso to sec. 92C(2) is not attracted. The international transaction reported by the assessee is to be adjusted by ₹ 552,616,748/- to bring it at arm's length price.

Since the price charged by the assessee varies by more than 5% from the arm's length price, an adjustment of ₹ 552,616,748/- is to be made to the income of the assessee, being the difference between the arm's length price and the price charged by the assessee from its AEs for trading and indent segment. The Assessing Officer shall enhance the income of the assessee by an amount of ₹ 552,616,748/- while computing its total income."

14. The assessee filed objections against the draft assessment order framed by the DCIT read with section 144C of the I.T. Act to the DRP. The DRP held that objections have been duly dealt with by the TPO in the draft assessment order and accordingly, the DRP did not find any reason to differ with the TPO's view. The DRP concluded that no

interference was needed in the adjustment proposed by the Assessing Officer /TPO on transfer pricing issue.

15. We have heard the rival contentions in light of the material produced and precedent relied upon. Ld. Counsel of the assessee submitted that the activity of purchase and sale involves risks and finances; whereas in the activity of 'indenting transactions' which are undertaken by the assessee, the assessee has either not to incur any such financial obligation or carry any significant risks; that the nature of the two activities are thus evidently and entirely different. It has further been submitted that in respect of indenting transactions with Non AE's, the average mean margin of profit is 2.26% which has duly been accepted by the TPO; that in respect of activity of purchase and sale of transactions with Non-AE's margin profit is 4.45%, which too has duly been accepted by the TPO; that the assessee is engaged in purchase and sale of various items which are highly insignificant in volume and as compared to the main activity of indenting, which constitutes the core business activities of the assessee; that the TPO has glossed over the vital contentions of the assessee, and had merely been swayed above by the fact that, in the report of the Accountant u/s. 92D of the Act, nature of the transaction has been stated by the Accountant to be the same functionally; that TP study mentions that trading transaction are functionally similar to indent transactions; that while stating so in the TP Study, it had never been admitted that, they are comparable; that though transactions of trading and, indent are in two different segments but since no separate meaningful analysis is required on account of miniscule volume, they were clubbed together for purpose of TP study.

16. It has further been submitted that the TPO committed an error when he compared the gross margin of negligible value of trading transactions of non-AE with high volume of indent transactions, genuineness of transactions of either indent / trading has not been disputed. That mere fact, that it was so reported by the Accountant, it could not be held to be binding on the assessee and thus, TPO could not have mechanically proceeded to determine arm's length price on the perception of the Accountant. It was further been submitted the transfer pricing guidelines issued by the OECD also supports the assessee's submissions. In this connection, Id. Counsel of the assessee referred the decision of the Hon'ble Jurisdictional High Court in the case of C.I.T. vs. Ekla Appliances. Referring to it Id. Counsel of the assessee pointed out that except for two circumstances mentioned in para 1.65 of the OECD TP guidelines, business structure of the assessee company should be accepted. It has been further been submitted that the indent business of the assessee was nothing but trade facilitation and is purely of indent nature both in form and substance. It has further been submitted that no material has been brought to regard the indent transactions by any stretch of imagination as trading transactions. It has further been submitted that the TPO has mentioned that assessee is creating human chain and supply chain intangible. It has been alleged by the TPO that by so creating such intangible, the assessee is not being adequately compensated by the AE. In this regard, assessee submitted that despite request, which of the intangible has been created, TPO has failed to identify any such alleged intangible. That the TPO has completely overlooked the assessee is mainly providing support services to its AE's and, there can

be thus no justification to allege that, any human chain and supply chain intangibles have been created.

16.1 It has been submitted that the activities performed by the assessee company are routine, preparatory and auxiliary in nature and do not create any intangibles. It has been submitted that the submission of the assessee is thus that there are two different segments, one of indenting and, another of trading and, both cannot be compared to determine the arm's length price. In this connection, Id. Counsel referred to the decision of the ITAT, Delhi Bench decision in the case of M/s Benetton India (P) Ltd. vs. ITO in I.T.A. No. 3829/D/2010 for A.Y. 2006-07 dated 30.11.2011. Ld. Counsel of the assessee further referred the decision of the ITAT, Mumbai Bench in the case of M/s Buyer Material Science (P) Ltd. vs. ACIT in I.T.A. No. 7977/Mum/2010. The above said case laws were mentioned by the Id. Counsel of the assessee for the proposition that trading and indenting segments are non-comparable. It has further been submitted that gross profit earned in trading transaction with AEs is also comparable to the gross profit earned in the trading transactions with non-AE in uncontrolled circumstances. It has further been submitted that Assessing Officer has nowhere disputed that TNMM adopted by the assessee is incorrect. Ld. Counsel of the assessee further submitted that TPO has failed to appreciate many of the submissions of the assessee company.

16.2 Further it has been submitted that without prejudice to the above (even if it is assumed without conceding) that, a segmental comparison of results of assessee company is warranted to determine the ALP, an appropriate comparison would be to compare the

commission / service income earned from AEs to that of the Non AEs. Thus, it has been submitted that commission earned by the assessee in non-AE services / commission segment may, subject to the various economic adjustments as mandated by law, be considered as benchmark commission to compute the arm's length commission from AEs. That FOB value of goods in indent transactions has not been considered as cost of goods by the assessee while calculating the margin of profit as per the berry ratio, since assessee does not incur any cost and payment made by the customer is not to be made to the assessee as it is not party to the contract. That the commission income earned by the assessee from its AE in the year under consideration was ₹ 30.45 crores on the FOB value of goods of ₹ 1925.49 crores; whereas in the non-AE segment, there are trading transaction are of only ₹ 14.81 crores and therefore, it would be an absurd and, preposterous proposition to treat one group of small isolated transactions as the basis of benchmarking the income of diverse range of commission transaction spread across time, sectors, products and service lines; that in each of the years commencing from A.Y. 2002-03, nature of transaction has been accepted as such by the TPO/Assessing Officer and since there has been no change in the operating model or the business activities of the assessee company, thus, even following the rule of consistency, no adjustment is warranted. In this regard, assessee has placed reliance upon following case laws:

- i) 17 ITR (Trib) 275 (Mum) M/s Bayer Material Science P Ltd. vs. ACIT.
- ii) 144 TTJ 449 (Del) Benetton India Pvt. Ltd. vs. I.T.O.
- iii) 48 SOT 269 (Vishakapatnam) LG Polymers India P Ltd. vs. Addl. C.I.T.

- iv) 26 SOT 226 (Bang) Phillips Software Centre Pvt. Ltd. vs. DCIT.
- v) 294 ITR(AT)32(Bang.) Aztec Software & Technology Services vs. ACIT.
- vi) 118 ITD 243 (Pune) E-Gain Communications Private Ltd. vs. ITO.
- vii) 109 ITD 101 (Del) Mentor Graphics (Noida) Private Ltd. vs. DCIT.
- viii) 114 ITD 448 (Del) Sony India Private Limited vs. DCIT.
- ix) 137 TTJ 539 (Del) DCIT vs. Cheil Communications India P Ltd.

17. Lastly it has been submitted that if the TPO's approach is adopted to work out corresponding return on cost, it would be found, the same is absurdly high which is 345% which is unrealistic and impractical.

18. Ld. Departmental Representative placed reliance on the orders of the DRP, TPO & Assessing Officer. He submitted that it is found that the activities of indenting sales and proper sales are one and the same functionally. That when the assessee itself considers the indenting sales and proper sales to be one and the same, the preferred route of benchmarking was using the internal benchmark, which was available in the form of profit margin in 3rd party sales made by the assessee itself. The internal benchmark is preferable to external benchmark has been laid down in plethora of rulings. In this regard, Ld. Departmental Representative referred the decision in the case of M/s Birla Soft India 136 TTJ Del. 505 and the decision in the case of M/s UCB India Ltd. 317 ITR 292 AT (Mum.). That where the AE is making profits or not is not relevant in a transfer pricing situation. In this regard, Ld. Departmental Representative has placed reliance upon the order of the ITAT Mumbai in the case of M/s Symantec Software Solutions Pvt. Ltd. I.T.A. No. 7894/Mum/2010 dated 31.5.2011. That it

was the assessee who found in its own TP Study Report that the two segments are comparable; that OECD guidelines have mere elucidative value, as we have our own TP legislation on the statute book. Besides, India is not a signatory to OECD itself. That Section 37 and Section 92 operate in different spheres. For this proposition, Ld. Departmental Representative relied upon the case of M/s Deloitte Consulting India (P) Ltd. 137 ITD 21 and decision in the case of M/s Perrot Systems, 5 ITR (Trib.) 106 (Delhi). That the mere difference in turnover is not sufficient for treating two entities, or two transactions, as not comparable to each other. In this regard, Ld. Departmental Representative has placed reliance upon the case of M/s Symantech (Supra).

19. Ld. Departmental Representative further placed reliance upon the decision in the case of M/s Bayer Material Sciences (P) Ltd. in I.T.A. No. 3829/Del/2010.

20. With regard to the assessee's contention of adhering to the rule consistency, Ld. Departmental Representative referred to the decision of the Hon'ble Apex Court in Distributors (Baroda) P. Ltd. vs. Union of India & Ors. 155 ITR 120 for the proposition that to perpetuate an error is no heroism. To rectify it is the compulsion of the judicial conscience.

21. We have carefully considered the submissions and perused the records. We agree with the proposition that in transfer pricing analyses internal comparable are preferable over external comparables.

22. We note that assessee has entered into two types of transaction (i) indent/ commission transaction where the assessee earned commission / fixed service fee, (ii) trading / proper transaction

wherein the assessee purchased good and earned trading margin thereon. The above two types of transaction has been entered into both with AEs and Non-AEs.

23. We agree with the assessee's proposition that the nature of indenting transaction is different from the trading transactions. The trading transaction involves risks and finances, whereas in the indenting transaction the assessee has not to incur any such financial obligation or carry any significant risk. Moreover, we note that in respect of indenting transaction with non-AE's, the average mean margin of profit of 2.26% has been accepted by the TPO. We further find that the indent business of the assessee was nothing but trade facilitation and is purely of indent nature both in form and substance. No material has been brought on record to regard the indent transaction as trading transactions.

24. Assessee itself has agreed with the proposition that an appropriate comparison would be to compare the commission/ service income earned by the assessee from AEs to that of the non-AEs. This aspect of assessee's submission has not been rebutted by the Revenue. However, the assessee has contended that the reason of difference between them was attributable to volume of business handled in AE segment and non AE segment and credit risk associated in non AE segment. Therefore, it has been argued that economic adjustment is required to improve the comparability between commission earned in AE segment vis-a-vis commission earned in Non-AE segment. It has further been submitted that it is customary in commercial dealing of broker/commission agent to offer discount on the basis of volume or value of business generated; that similarly

commission/brokerage charged from low value / small customers is much higher on account of the premium rate of commission charged from them. Hence the assessee has come to the conclusion that discount of 50% was to be applied on Non-AE segment commission percentage to arrive at the arm's length commission percentage.

25. However, we do not agree with the proposition that in the facts and circumstances of the case volume impacts the rate of commission. For each and every single transaction a separate contract is entered and the commission rate / service fee is mentioned in this context. It is also not the case of the assessee that volume of a single transaction varies in the AE and Non-AE segment.

26. We find that mere difference in turnover is not sufficient for treating two entities or two transactions as not comparable or warrant any adjustment. In this regard we refer to the follow case laws.

- In the case of M/s Symantec Software (Supra) in para 15 following has been laid down:-

"In the case in hand, the assessee raised these objections only because some of the comparables are having high profit and also high difference in the turnover and not because of the high or low turnover has influenced the operating margin of the comparables. All the objections and contentions raised by the assessee in respect of this issue are general in nature and no specific fact has been brought on record to show that due to the difference in turnover the comparables become non-comparables. The assessee has not demonstrated as to how the difference in the turnover has influenced the result of the comparables.

It is accepted economic principles and commercial practice that in highly competitive market condition, one can survive and sustain only by keeping low margin turnover. Thus, high turnover and low margin are necessity of the highly competitive market to survive.

Similarly, low turnover does not necessarily mean high margin in competitive market condition. Therefore, unless and until it is brought to record that the turnover of such comparables has undue influence on the margins, it is not the general rule to exclude the same that too when the comparables are selected by the assessee itself."

- Similarly in the case of M/s Bayer Material Sciences (P) Ltd. (Supra) in para 23 following proposition was laid down:-

"Now the question is whether these cases, which are otherwise comparables, should be disregarded simply on the ground of smallness of turnover when compared with that of the assessee. Considering the fact that the assessee did not come out with any comparable case to justify its price at arm's length and further the TPO found out these cases having functionally identical activities duly confronted to the assessee, it is not possible to disregard such cases merely on the ground that the volume of turnover is lower in comparison to that handled by the assessee. One more important factor which cannot be lost sight of is that in the case of M/s Rathi Brothers Madras Ltd. indenting commission is 5% to 6% with turnover of ₹ 10.65 crores. The same rate of commission of 5% prevails in the

case of M/s Huntsman International (P) Ltd. and M/s Ineos ABS (India) Ltd. with turnover of around ₹ 75 cores and around ₹ 80 cores respectively. It shows that the rate of commission in such business does not vary on the basis of turnover.”

27. Hence when the indent/ commission transaction with the AE is to be benchmarked, the same should be done with indent / commission transaction with Non-AE. Hence there is a no need to dwell further on the comparison between indenting transaction and trading transaction.

28. On the basis of above discussion and precedents we reject the assessee's contention that discount of 50% is required in commission percentage in the Non-AE segment to make it comparable with commission percentage in the AE segment.

29. Now we come to argument of the assessee that there is no change in the operating model or the business activity of the assessee company, hence, rule of consistency should be followed and hence no adjustment is warranted. In this regard we are of the opinion the res judicata is not applicable to taxation cases. Moreover, as held by Apex Court in Distributors (Baroda) P Ltd. vs. Union of India & Ors. 155 ITR 120 that to perpetuate an error is no heroism. To rectify is the compulsion of the judicial conscience.

30. In light of the discussions and precedents cited above, we are of the opinion that commission percentage in AE segment should be compared with commission percentage in Non-AE segment.

Accordingly, the commission percentage @ 2.26% in Non-AE segment should be taken as the arm's length rate at which assessee should have earned its commission income in the AE segment.

31. The ground no. 8 read as under:-

That the Ld. AO/DRP has grossly erred both in law and, on facts in proposing a disallowance of a claim of expenditure of Rs. 3,72,560/- representing legal and, professional charges incurred wholly and exclusively for the purpose of business of the appellant company.

That the Ld. Assessing Officer and DRP has failed to appreciate that, mere fact that, such expenditure had been disallowed in the preceding years could not be a basis much less valid basis to hold that, expenditure incurred towards Writer Relocations was a personal expenditure. In fact, they have failed to appreciate that, it is well settled position of law that, a company does not have any personal expenditure and as such, entire expenditure incurred ought to have been allowed as such.

That the Ld. DRP has grossly erred both in law and, on facts in directing the AO to make the addition only if the department has not preferred an appeal before Hon'ble IT AT against the addition deleted by the CIT(A) in the AY 2006-07 on the similar ground.

32. On this issue the Assessing Officer noted that from the details furnished, it was observed that assessee has claimed an expense of ₹ 3,72,560/- towards Writer Relocations under the head legal and professional charges. The assessee was required to explain as to why not disallowance be made in view of the facts mentioned in the

assessment orders for earlier years. Assessing Officer noted that the assessee did not furnish any explanation in this regard. He held that the expenditure are personal expenditure and not connected with the business of assessee company. Considering the facts discussed in earlier years and in absence of any explanation, an amount of ₹ 3,72,560/- was disallowed and added to the total income of the assessee in the draft assessment order.

33. On this issue the DRP's directed the Assessing Officer to verify whether the department has filed any appeal against the order of the Ld. Commissioner of Income Tax (A) for the assessment year 2006-07. If no appeal is filed, then only the Assessing Officer is directed to delete the addition. On the above directions, the Assessing Officer noted that in the assessment year 2006-07 department has not accepted the decision of the Ld. Commissioner of Income Tax (A) and an appeal was filed before the Tribunal on this issue. In view of this the disallowance of ₹ 3,72,560/- on account of legal and professional charges was added to the income of the assessee.

34. Against the above order the Assessee is in appeal before us.

35. We have heard the rival contentions in light of the material produced and precedent relied upon. Ld. Counsel of the assessee submitted that the assessee company employs foreign nationals for the purpose of its business, as they have requisite expert knowledge of the markets outside India. Assessee company has many of the foreign nationals, on its rolls, working at various managerial positions. As per the general policy of the assessee company and the market wide practice, the company at the time of the departure of such foreign assignees, after completion of their assignments, bears the

cost of their return journey to their respective home countries. In accordance with such an obligation, it had incurred the following expenditure which expenditure had been debited under the head legal and professional though such expenses are miscellaneous business expenditure. The details in this regard are as under:-

S.No.	Name of the payee	Remarks	Date	Amount	Page of PB
1	Writer Relocations	Charges of unaccompanied passenger baggage clearing New Delhi to Tokyo, Japan Mrs. Keiko Mugikura	21.6.2006	₹ 1,33,000/-	605-607
2	-do-	Charges of unaccompanied passenger baggage clearing New Delhi to Kobe, Japan Mrs. Chizuko Haruna	21.6.2006	₹ 34,000/-	608-610
3	-do-	Charges of unaccompanied passenger baggage clearing New Delhi to Japan Mrs. Rie Nagashima	30.3.2007	₹ 70,000/-	611-613
4	-do-	Charges of unaccompanied passenger baggage clearing New Delhi to Tokyo, Japan Mrs. Rie Nagashima	31.3.2007	₹ 47,500/-	614-617
		Charges of unaccompanied passenger baggage clearing Mumbai to New	02.8.2006	₹ 23,200/-	618-619

		Delhi Mrs. K. Nagashima			
5	-do-	Charges of unaccompanied passenger baggage clearing New Delhi to Chiba, Japan Mrs. K. Nagashima	23.11.2006	₹ 61,360/-	620-622
Total				₹3,69,060/-	

36. Ld. Counsel of the assessee further submitted that during the course of assessment, assessee duly provided the details of such expenditure. However, the Assessing Officer held that the said expenditure is personal in nature. It is further submitted that for assessment year 2006-07, the Ld. Commissioner of Income Tax (A) had deleted the above disallowance by holding that such expenditure is not personal expenditure. Furthermore, for assessment 2008-09 the Assessing Officer disallowed similar expenditure, he was directed to delete the same by the DRP. Accordingly, Id. Counsel of the assessee prayed that this addition may be deleted.

37. Ld. Departmental Representative on the other hand, relied upon the order of the Assessing Officer.

38. We have carefully considered the submissions. We find that these expenditures were incurred by the assessee on its employees who were returning to their home countries, after completion of the assignments. The expenditures were charges in connection with passenger baggage clearing. Similar expense was also allowed by the Ld. Commissioner of Income Tax (A) in the assessment year 2006-07.

DRP has also allowed expenditure in assessment year 2008-09. Under the circumstances, we hold that assessee has cogent submissions, the addition in this regard cannot be sustained. Accordingly, we delete the addition.

39. The ground no. 9 reads as under:-

“That the Id AO/DRP has further erred both in law and on facts in making a disallowance claim of deduction of deposits written off of Rs. 2,56,257/- on factually incorrect and, legally erroneous considerations and thus, the same is not tenable.”

40. On this issue Assessing Officer noted that as per the details filed by the assessee, it was observed that assessee has debited an amount of ₹ 2,56,257/- to profit and loss account under head ‘deposits written off’. The assessee was asked to furnish the details of these expenses and also to explain as to why the same may not be disallowed and added to total income. Assessee did not offer any explanation in this regard. Hence, an amount of ₹ 2,56,257/- was added to the total income in the draft assessment order. Assessing Officer noted that the objections filed by the assessee, the DRP has not made any interference. Hence, the addition of ₹ 2,56,257/- on account of deposits written off was added to the income of the assessee.

41. Against the above order the Assessee is in appeal before us.

42. Ld. Counsel of the assessee submitted that from the perusal of the schedule forming part of the profit and loss account on page 65 of the Paper Book, it would be seen that assessee has not written off any such deposits amounting to ₹ 2,56,257/- in the instant year, but in fact the same had been debited in the A.Y. 2006-07 and claimed in the A.Y. 2006-07. Hence, it has been submitted that Assessing Officer misread the profit and loss account and amount claimed in the A.Y. 2006-07 was understood by him as the amount claimed in the A.Y. 2007-08, and on this misconception Assessing Officer made the aforesaid addition.

43. Ld. Departmental Representative relied upon the order of the Assessing Officer.

44. We have carefully considered the submissions and perused the records. We find that there is considerable cogency in the assessee's submissions. On perusal of the profit and loss account as referred by him clearly shows that the such write off was claimed in assessment year 2006-07 and by misreading, the Assessing Officer has taken it as pertain to assessment year 2007-08. Under the circumstances, we find considerable cogency in the submissions of the assessee.

Accordingly, we set aside the order of the Assessing Officer and decide the issue in favour of the assessee.

45. In the result, the appeal filed by the assessee stands partly allowed.

Order pronounced in the open court on 31/1/2013.

Sd/-

**[I.C. SUDHIR]
JUDICIAL MEMBER**

Sd/-

**[SHAMIM YAHYA]
ACCOUNTANT MEMBER**

Date 31/1/2013

"SRBHATNAGAR"

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|--------------|---------------|--------|------------|
| 1. Appellant | 2. Respondent | 3. CIT | 4. CIT (A) |
| 5. DR, ITAT | | | |

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By Order,

Assistant Registrar,
ITAT, Delhi Benches