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

BEFORE SHRI R.C. SHARMA (AM) AND SHRI RAM LAL NEGI (JM)

ITA No. 1182/MUM/2017
Assessment Year: 2012-13

M/s CLSA India Private Limited, 8/F Dalamal House, Nariman Point, Mumbai - 400021 PAN: AAACC2262K	**Vs.**	The Deputy Commissioner of Income-Tax, Circle 4(1)(1), 6th Floor, Room No. 640/678, Aayakar Bhavan, M.K. Road, Mumbai - 400020
(Appellant)		**(Respondent)**

Assessee by : Shri Mukesh Butani Shreyash Shah, Karishma Phatarphekar & Harsh Shah (ARs)

Revenue by : Shri Jayant Kumar (CIT) DR.
Pavan Kumar Beerla (DR)

Date of Hearing: 30/11/2018
Date of Pronouncement: 16/01/2019

O R D E R

PER RAM LAL NEGI, JM

This appeal has been filed by the assessee against the direction dated 26.12.2016 passed by the Ld. Dispute Resolution Panel-I (DRP) (WZ), Mumbai, u/s 144C (5) of the Income Tax Act, 1961 (for short 'the Act'), pertaining to the assessment year 2012-13 vide which the Ld. DRP has upheld the order passed by the Ld. TPO u/s 92CA(3) of the Act.

2. The assessee company CLSA incorporated in India is a subsidiary of Credit Lyonnais Securities Asia (CLSA) incorporated in Netherlands. The assessee filed its return of income for the assessment year under consideration

declaring the total income of Rs. 1,29,91,09,122/-. The return was processed u/s 143 (1) of the Act. Since, the case was selected for scrutiny, notice u/s 143 (2) and 142 (1) were issued and served upon the assessee. In response to the said notices, the authorized representative of the assessee appeared before the AO and submitted the details called for and discussed the case.

3. Since the assessee company had entered into international transactions with its associated enterprises (AEs), the Assessing Officer (AO) referred the matter to the Transfer Pricing Officer (TPO) for determining arm's length price of these transactions. The Ld. TPO vide order dated 27.01.2016 determined the arm's length price making upward adjustment of Rs. 143,67,42,784/-. Accordingly, the AO computed the total income of the assessee *inter alia* making addition of the arm's length price determined by the TPO u/s 92CA (3) of the Act as per the provisions of section 92CA (4) of the Act and passed draft assessment order u/s 143 (3) read with section 144C of the Act on 07.03.2016. The assessee filed objections against the said draft assessment order before the Ld. Dispute Resolution Penal (DRP) and the Ld. DRP after hearing the assessee dismissed the objections and passed directions u/s 144C (5) of the Act. Accordingly, the AO made an addition on account of Transfer pricing adjustment amounting to Rs. 143,67,42,784/- to the total income of the assessee and determined the total income of the assessee at Rs. 273,52,15,790/- as against the returned income of Rs. 129,91,09,122/-.

4. Aggrieved by the directions of Ld. DRP, the assessee has preferred this appeal before the Tribunal on the following effective grounds:-

1. *"On the facts and circumstances of the case and in law, the learned Transfer Pricing Officer (TPO)/the learned AO/Hon'ble DRP erred in assessing the total income of the appellant at Rs. 273,52,15,790.*

2. *"On the facts and circumstances of the case and in law, the learned TPO/ learned AO/Hon'ble DRP erred in rejecting the Transfer Pricing ('TP') analysis undertaken by the Appellant.*

3. *On the facts and circumstances of the case and in law, the learned TPO/ learned AO/Hon'ble DRP has erred in proposing/upholding an adjustment to the Arm's Length Price (ALP) determined by the Appellant in respect of the international transactions in connection with availing of intra-group services by the Appellant from its Associated Enterprises ('AE's). In doing so, the learned TPO/learned AO/Hon'ble DRP has erred in law and in facts by:*

3.1 Rejecting Transactional Net Method ('TNMM) as the Most Appropriate Method ('MAM) for the determination of the ALP.

3.2 Not appropriately applying any of the prescribed methods as per section 92C(1) of the Act.

3.3 Not appreciating the voluminous documentary evidence, details of cost incurred by the AEs, details of allocation keys used by the AEs etc. filed by the Appellant and

3.4 Not considering the benefits derived by the Appellant and also disregarding the commercial expediency of the Appellant.

The Appellant claims relief on the above grounds and thereby deleting the adjustments made by the learned AO in the final assessment order."

5. Ground No. 1 and 2 of the appeal are of general nature, therefore the same do not require separate adjudication.

6. Vide Ground No. 3, 3.1, 3.2, 3.3 and 3.4 the assessee has challenged the order passed by the AO on the ground that the Ld. TPO has wrongly made adjustment of Rs. 143,67,42,784/- by rejecting transactional net margin method (TNMM) adopted by the assessee as the most appropriate method (MAM) and that the Ld DRP has wrongly upheld the transfer pricing adjustments made by the Ld TPO. The assessee has further alleged that the Ld. TPO has determined the ALP, without applying any of the prescribed methods under section 92C(1) of the Act and rejecting the transfer pricing analysis of the assessee based on the TNMM, without appreciating the documentary evidence including details of cost incurred by the AEs , details of allocation keys used by the AEs etc., filed by the assessee and without considering the benefits derived by the assessee and without taking into consideration the commercial expediency of the assessee.

7. Before us, the Ld. counsel for the assessee submitted that the TP analysis submitted by the assessee is at arm's length based on TNMM by considering the assessee as the tested party. The Ld. counsel invited our attention to the profit and loss account of the assessee in which two major costs have been mentioned as employee cost and management fees recharge (intra group services). The intra group services are closely linked to the business of the assessee and the assessee's benchmarking approach based on TNMM by considering the assessee as the tested party may be upheld. The Ld. counsel further contended that without prejudice to the above, the assessee has also carried out a benchmarking on the transaction by considering the AEs as the tested party. Based on this approach also the assessee's transaction is arms length whereas the conclusion of Ld. TPO that the AEs have rendered 10000 hours of service and the assessee has paid @ Rs 3000/- per hour is not based on any comparable uncontrolled transaction. The Ld. counsel further contended that in fact the Ld. TPO has not followed any of the prescribed methods to benchmark the transaction and as per the settled law any addition

made under chapter X of the Act has to be based on the method prescribed under it, failing which such additions are liable to deleted. The Ld. counsel relied on the following cases to substantiate the said arguments:-

1. *Knorr-Bremese India (P.) Ltd. v. ACIT [2017] 77 taxmann.com 101 (Delhi – Trib).*
2. *AWB India Pvt. Ltd. v. ACIT [ITA No. 4454/Del/11)*
3. *AWB India Pvt. Ltd. v. DCIT [2014] 50 taxmann.com 323 (Del-Trib).*
4. *DCIT v. Danisco (I) P. Ltd. [2015] 63 taxmann.com 174 (Del-Trib)*
5. *Ingersoll Rand (India) Ltd. v. DCIT [2016] 67 taxmann.com 328 (Bang-Trib).*
6. *BG Exploration and Production India Ltd. v. JCIT [2017] (4) TMI 1145-ITAT Delhi]*
7. *DDIT v. BG Exploration & Production India Ltd. [2017] 80 taxmann.com 393 (Delhi-Trib).*
8. *Sabic Innovative Plastics India Pvt. Ltd. v. ACIT [ITA No. 1125/Ahd-2014 & ITA No. 427/Ahd-16]*
9. *AXA Technologies Shared Services (P.) Ltd. v. DCIT [2016] 76 taxmann.com 102 (Bangalore Trib).*

8. The Ld. counsel further submitted that u/s 92C of the Act read with rule 10B of the Income Tax Rules, the TPO is bound to determine the ALP by following one of the prescribed methods and since the Ld. TPO has not followed any prescribed methods in the present case, the transfer pricing adjustment made is unsustainable in law. The Ld. counsel further submitted that ad-hoc disallowance is not permissible even u/s 37 of the Act. Therefore, any ad-hoc determination of arms length price by the Ld TPO section 92 de-hors section 92C(1) of the Act cannot be sustained. To substantiate the aforesaid arguments the Ld counsel relied on the following cases:

1. *CIT v. Merck Limited [2016] 389 ITR 70 (Bombay).*
2. *CIT v. Lever India Exports Limited [2017] 78 taxmann.com 88 (Bombay)*
3. *CIT v. Johnson & Johnson Ltd. [2017] 80 taxmann.com 337 (Bombay)*

4. *CIT v. Kodak India (P) Ltd. [2017] 79 taxmann.362 (Bombay).*
5. *Kodak India (P) Ltd. v. ACIT [2013] 37 taxmann.com 233 (Mumbai-Trib).*
6. *Watson Pharma (P) Ltd. v. DCIT [2015] 54 taxmann.com 88 (Mumbai-Trib).*
7. *ITO v. Intertoll ICS India (P) Ltd. v. DCIT [2015] 71 taxmann.com 353(Mumbai-Trib).*
8. *ACIT v. Koch Chemical Technology Group (India) Ltd. [2015] 64 taxmann.com 464 (Mumbai-Trib).*
9. *CIT v. Diebold Software Services (P) Ltd. [2014], 48 taxmann.com 26 (Mumbai-Trib).*

9. On the other hand, the Ld. departmental representative (DR) relying on the directions issued by the Ld DRP, submitted that the TNMM method adopted by the assessee is not an appropriate method as the intra-group services received by the assessee is a separate class of transaction which could not be aggregated with other international transactions of receipt of brokerage services, sub-advisory services, research support services etc. The Ld. DR placed reliance on the judgment of the Hon'ble Punjab and Haryana High Court in *Knorr Bremse India Pvt. Ltd. vs. ACIT*, [2015] 63 taxmann.com186 (P&H). The Ld DR further submitted that the assessee has failed to establish that the intra group services were inextricably linked to other international transactions. Moreover, the TP study of the assessee do not reflect as to whether the similar level of cost of payment of intra group services had been incurred by the companies taken as comparables by the assessee. Hence, the Ld. DRP has rightly rejected the objection of the assessee and upheld the findings of Ld. TPO. The Ld. DR further submitted that the services rendered by the AEs are general and the assessee has failed to adduce any reliable evidence to substantiate that the AEs incurred a particular cost in rendering services to the assessee. In respect of international sales trading and support, the foreign institutional Investors are client of the assessee and if some revenue is generated, the same is on account of membership of the group and the same would not result in payment for such services in a third party uncontrolled situation. The communication received on day today basis from AEs would be

in the nature of shareholder activity for effective management of the group entities. Emails in respect of group services were found to be day today correspondence in which the legal work was prepared by the assessee company and it was sent to the AE for a review, which again is in the nature of share holder service. Moreover, the assessee has not provided details of actual cost of service in respect of the services received by the assessee. The assessee has also failed to provide details of number of hours devoted by each employee in respect of services provided to the assessee and per hour cost of the services availed. The Ld. DR further submitted that in the light of the aforesaid facts, the Ld. DRP has rightly upheld the best judgment arms length price determined by the Ld. TPO.

10. We have heard the rival submissions and also perused the material on record including the cases relied upon the parties. The first issue pertains to the assessee's objection raised before the Ld. DRP on the ground that the Ld. TPO has wrongly rejected the TNMM followed by the assessee in its transfer pricing analysis. Brief facts and material which need necessary mention for the purpose of deciding the issues involved are that the assessee company incorporated under the companies Act 1956, is primarily engaged in the business of equity broking and has membership of Bombay stock exchange and the National stock exchange. The assessee's customers comprise of foreign institutional investors (FIIs) and domestic institutional investors (DIIs). As contended by the Ld. counsel for the assessee, since the assessee had no international sales presence or capability to maintain client relationship with FIIs on global basis or internal resources to undertake various activities like regional research or perform various back-office functions, it entered into agreements with CLSA Ltd. Hong Kong and CLSA Singapore private Ltd., which had the capacity to maintain the client relationship on global basis for providing services in the nature of international equity sales and sales trading support, dealing sport and regional research as well as a range of back-office support services. In the year relevant to the assessment year under

consideration, the assessee made payment of Rs. 146,67,42,784/-for availing these intra group services. The assessee benchmarked the said international transaction using TNMM as the most appropriate method considering itself as the tested party and adopted operating profit (OP)/operating cost (OC) as the profit level indicator (PLI). Since the assessee's margin of 26.09% was better than the comparable companies margin of 10.14% the assessee claimed the transition to be at arm's length. Alternatively, the assessee also benchmarked the said transaction by considering the AEs as the tested party and based on comparable companies margin justified that the markup charged by the AE's are at arm's length.

11. Since, CLSA India had paid Rs. 129,30,35,428/- to CLSA Hong Kong and Rs. 17,37,07,356/- to CLSA Singapore for providing operational support to CLSA affiliates including the assessee during the year relevant to the assessment year under consideration, the Ld. TPO asked the assessee to submit the details of Intra Group Services and substantiate the ALP for the same along with the relevant supporting documents. The assessee was further asked to show cause as to why similar adjustment should not be made particularly in the light of the fact that similar adjustment on Intra Group payments was confirmed by the Ld. DRP in the A.Y. 2011-12 under the similar set of facts.

12. In response to the said query, the assessee submitted that it has entered into separate service level agreements with the CLSA service providers, pursuant to which the following services were rendered by them during the year relevant to the assessment year under consideration:-

Broking Management,

Client Management,

CLSA U,

Communications,

Compliance,

Credit Risk Management,

Development Squad,
Event Marketing,
Finance and Accounting,
Future & Options Management Support Services,
Human Resources,
Information Technology,
Internal Audit,
International Sales and Sales Trading Support,
Legal,
Management,
Market Risk Management,
Operational Risk Management,
Regional Algorithm Business Support,
Regional Research, Tax Planning and Management.

13. To substantiate its claim, the assessee *inter alia* submitted transfer pricing study report, copy of audited financials, copies of service level agreement entered into with CLSA, Hong Kong and CLSA, Singapore, description of services and summary of benefits, supplementary analysis KPMG benchmarks, documentary evidence to prove services rendered by the intra group under the heads administration, broking management, client management, communications, compliance, credit risk management, developed squad, events marketing, finance, Human Resources, Information Technology, internal audit, internal sales and sales trading support, legal, Management, Operational Risk Management and Regional Research. The assessee also submitted description of the various services, head-wise breakup of the payments and cost allocation as per keys provided in agreement.

14. As pointed out by the Ld. counsel, the assessee has benchmarked the transaction with entry-level TNMM. It has benchmarked the transaction separately by adopting AE as tested party and using foreign data base. We

notice that the arithmetic mean of the comparable companies was 10.14% and the assessee had earned net profit margin of 26.09%. As pointed out by the Ld. counsel, the margin earned by the assessee company at an entry level is in accordance with the provisions of section 92C(2) of the Act. But the Ld. TPO did not accept the entry level benchmarking of the cost contribution holding that the cost contribution constitutes a small part of the total transactions at the entry level, therefore, the profit margin at the entry level cannot be the basis for determining the ALP of the cost contribution. The profit at entry level is affected by various other factors therefore the TNMM is not the most appropriate method to benchmark the transaction of cost contribution. Secondly, the Ld. TPO held that under the transfer pricing provisions, each international transaction has to be benchmarked separately.

15. We further notice that the assessee has benchmarked the transaction by using foreign comparable companies i.e., by using AE as tested party. As pointed out by the Ld. counsel for the assessee, the assessee has separately benchmarked its various international transactions including the transaction of payment of intra group services. The assessee has submitted transfer pricing study report which is available at page 43 to 74 of the paper book submitted by the assessee. The transfer pricing study report reveals that the net profit margins of the identified comparable companies range between -2.88 and 25.13% and the arithmetic mean of the NPMs of comparable companies is 10.40%. On the other hand, the net profit margin of the assessee company for the financial year ended March 31, 2011 at entry level was 26.09%. In the light of the aforesaid facts, there is no merit in the findings of the Ld. TPO that the margin earned by the assessee at an entry level is not in accordance with the provisions of section 92C(2) of the Act. Under these circumstances, the action of the Ld. DRP in confirming the transfer pricing adjustment done by the Ld. TPO is not justified. The assessee has also submitted a supplementary analysis i.e. AUP report from Price Waterhouse Coopers (PWC) which certifies the cost

and markup charged by AEs and KPMG benchmarking report, which determines arm's length markup for services availed. So, there is merit in the contention of the Ld. counsel that the assessee has complied with all requirements as prescribed under the Act and the Rules and the TP analysis has been carried out as per the provisions of law. We are therefore of the considered view that the assessee has discharged its onus by demonstrating that the transaction is at the arms length in accordance with the provisions of section 92C of the Act and has maintained the prescribed documentation in support of such compliance.

16. On the other hand the Ld. DRP has upheld the findings of the Ld. TPO rejecting the objections filed by the appellant/assessee. The operative part of the findings of the Ld. DRP read as under:

> *"3.3.1 We have considered the facts of the case and submissions made by the assessee. We find that the issues at hand are squarely covered against the assessee in its own case for A.Y. 2011-12, by the decision of DRP-I (WZ), Mumbai holding as under:-*
>
> *"We have considered the facts of the case and the submissions made. As per the provisions of section 92C of the Act, the arm's length price in relation to an international transaction shall be determined by adopting any of the prescribed five methods, being the most appropriate method '(MAM) having regard to the nature of transaction or class of transactions or class of associated persons or functions performed by such persons or such other relevant factors as may be prescribed. Each transaction is to be examined separately and independently. Different transactions cannot be bundled up together. Only those transactions which are closely interlinked, interrelated, interlaced, inter-wined, inter-connected, inter-dependent and continuous can be grouped and bundled together for bench marking provided the said transactions can be evaluated and adequately compared an aggregate basis. Otherwise the bunching of independent and different transactions is not permitted. P&H High Court also in the case of Knorr Bremse India Pvt. Ltd. in ITA Nos. 182 and 172 of 2013 in their order dated 06.11.2015 have held as under:-*

"43 It follows, therefore, that if the TPO had correctly come to the conclusion that the said five items were not connected to the rest, he was justified in determining the arm's length price thereof separately from and independent of the others. It would be neither logical nor rational in that event to club several independent and unconnected transactions for the purpose of determining the arm's length price. If, on the other hand, it is established that the sale of various goods and/or the provision of services formed one composite indivisible transaction, TNM method cannot be applied selectively to some of the component and the CUP or any other method to the remaining component.

44 in the present case, all the items tabulated above were not provided by the same entity. They were provided by different entities. That these entities were all part of the same group is not determinative of the issue whether they were part of a single international transaction. Each party to the group is a separate legal entity. We do not rule out the possibility of these being a single international transaction where goods are sold and/or services are supplied by various entities within a group under a single transaction. That, however, would depend upon the facts of each case. The onus would be on the assessee to establish that though the goods were supplied and/ or the services were rendered by different legal entities they were part of an international transaction pursuant to an understanding between the various members of the group. This would be an issue of fact for the determination of the authorities under the Act."

1.1. *The various international transactions of the assessee are: (i) Brokerage (ii) IT support services, (iii) Fees for sub-advisory services, (iv) Payment for intra-groups services (v) Interest (vi) Reimbursement of expenses and (vii) Bank charges. These transactions cannot be said to be closely inter-linked, interrelated, interlaced, inter-wind, inter-connected and inter-dependent and also they cannot be evaluated and adequately compared on aggregate basis. All these*

transactions are different and independent of each other. They are also provided to different entities. Therefore, they cannot be bunched together for benchmarking by applying TNMM at entity level. Therefore the benchmarking of the assessee is neither scientific nor permitted as per law. Hence, the TPO has rightly rejected the entity level TNMM. The same is hereby upheld.

1.2. *All these transactions can be independently examined and benchmarked applying CUP. Hence, the TPO has rightly applied CUP in respect of these transactions. ITAT Mumbai in the case of Goldman Sachs (India_) Securities Private Limited v ACIT (ITA No. 7724/Mum/2011) has upheld the application of CUP in the case of brokerage transactions similar to those of the assessee. Further, ITAT Bangalore in the case of M/s Fosroc Chemicals India Private Limited in IT (TP) A No. 148/Bang/2014 for AY 2009-10 in their order dated 10.04.2015 has upheld application of CUP as MAM for benchmarking of payment for technical and management services.*

1.3. *ITAT Bangalore in Fosroc Chemicals India case supra has also held that aggregation of different international transactions would depend on the nature of services received by the assessee and how the different segment of the assessee benefited from the services received. The test whether to adopt a combined transaction approach or to evaluate the international transaction on a transaction-by-transaction basis is to see whether the transaction can be evaluated adequately on a separate basis. Though the ITAT has not answered the question aggregation of transactions in this case but emphasis has been laid on preference for separate benchmarking.*

1.4. *Further, Delhi High Court in Sony Ericsson's case in ITA No. 16/2014 in the order dated 16.03.2015 has clearly laid down the criteria for aggregation of the different transactions. P&H High Court also in their order dated 06.11.2015 in the case Knorr-Bremse India Pvt. Ltd. ITA No. 172 & 182 of 2013 have clearly laid down the criteria for aggregation of different transaction and also for bench marking of intra-group services. It has been held in this case, that intra group services cannot be benchmarked applying entity level TNMM but it has to be benchmarked applying CUP. Therefore, on facts of this case*

the transactions cannot be aggregated. Hence, objections regarding rejection of entity level TNMM and application of CUP are rejected."

17. The Ld DRP has upheld the transfer pricing adjustment made by the Ld. TPO in the light of the judgments of the Hon'ble High Court of Delhi in *Sony Ericsson's case (supra)* and the P&H *High Court in the case Knorr-Bremse India Pvt. Ltd.(supra)* in which it has been held that the answer to the issue whether a transaction is at an arm's length is not dependent on whether the transaction results in the assessee's profit. But the only important aspect which is to be seen is whether the transaction entered into is *bona fide* or the same has been entered into for the purpose of diverting the profits. The Ld. DRP has further relied on the decision of the ITAT Mumbai in the case of *Goldman Sachs (India) Securities Private Limited v ACIT (ITA No. 7724/Mum/2011)* and ITAT Bangalore in the case of *M/s Fosroc Chemicals India Private Limited in IT (TP) A No. 148/Bang/2014 for AY 2009-10* in which the Tribunal has upheld the application of CUP as MAM for benchmarking of payment for technical and management services. In the light of the above findings of the Ld. DRP the following question arise:

(a) whether the Ld. TPO has determined the ALP in this case by following comparable uncontrolled price (CUP) method as the most appropriate method and (b) whether the Ld. DRP has rightly upheld the transfer pricing adjustment made by the Ld. TPO?

18. In order to determine the said questions, it is important to see as to whether the Ld. TPO has determined the arm's length price of the international transactions by following one of the prescribed methods which is the most appropriate in the light of the facts and the circumstances of the case? We notice that the Ld. TPO has estimated the man hours of services rendered by the AE to the assessee at 10000 hours and applying the rate of 3000 per hours determined the arms length compensation of the services rendered by the AE to

the assessee at Rs. 3,00,00,000/-. The relevant part of the order passed u/s 92CA(3) of the Act is reproduced as under:

"*5.8.2 Though no concrete evidence of receipt of service has been provided by the assessee as detailed above, on a without prejudice basis it is estimated that, at the very best, the AE could have devoted a maximum of the following man hours in respect of various services claimed to be availed by the assessee*

SI No.	*Department*	*Total*	*Share in %*	*Remarks of the TPO*
1.	*International sales and sale Trading Support*	*774477979*	*52.80*	*These three departments constitutes 80% of allocation, 8000 man hours are estimated*
2.	*Regional Research*	*248699719*	*16.96*	
3.	*Management*	*16213236*	*11.05*	
4.	*Information Technology*	*109448954*	*7.46*	*Rest of departments constitutes 20% allocation, so 2000 man hours are estimated.*
5.	*Broking Management*	*37815450*	*2.58*	
6.	*Legal*	*32086984.3*	*2.19*	
7.	*Events Marketing*	*18507639.4*	*1.26*	
8.	*Client Management*	*14499282.2*	*0.99*	
9.	*CLSA U*	*12405574.2*	*0.85*	
10.	*Futures & Options Management Support*	*11789552.8*	*0.80*	
11.	*Human Resources*	*10720135.2*	*0.73*	
12.	*Credit Risk Management*	*10106024.4*	*0.69*	
13.	*Regional Algorithm Business Support*	*9183280.17*	*0.63*	
14.	*Tax Planning and Management*	*8796597.54*	*0.60*	

15.	*Compliance*	*5334397.79*	*0.36*	
16.	*Operational Risk Management*	*4286031.08*	*0.29*	
17.	*Finance & Accounting*	*3741284.96*	*0.26*	
18.	*Internal Audit*	*1356363.47*	*0.09*	
19.	*Development Squad*	*1299073.45*	*0.09*	
20.	*Market Risk Management*	*1119912.22*	*0.08*	
21.	*Communications*	*-11063811*	*-0.75*	*This is negative, so man hours are not allocated.*
	Total	*1466742784*	*100*	*10000*

19. The Ld. TPO has justified the method of estimating the hours devoted by the AE in respect of various services claimed to be availed by the assessee holding as under:-

> *"5.11.2 In the absence of all these details regarding the number of employees working with the AE, the salaries paid to these employees, the educational qualification of these employees, the number of hours dedicated by these employees towards the services rendered to the assessee, the undersigned is constrained to go by estimation to the best judgment, to quantify the value of the services if at all any being rendered by the AE to the assessee. Without prejudice to the contention of the undersigned, regarding the services being rendered by the AE to the assessee. However after considering the evidence filed by the assessee, as a matter of abundant precaution, the undersigned proceeds to make a reasonable estimate, of whatever little services that can be said to have been rendered in the facts and circumstances of this case. Having regard to the nature of services which are claimed to have been rendered in the instant case, the undersigned estimates the salary for such an employer at Rs. 3000 per hour. To the best of my judgment, the number of man hours rendered by the employees towards rendering of these services to the assessee, is estimated earlier at 10,000 Hours at para 5.8.2"*

20. From the observations of the Ld. TPO, it is clear that TPO has made the transfer pricing adjustment purely on estimation basis without any supporting material. Though the Ld. TPO has mentioned that arms length price has determined by applying CUP method but in fact the Ld. TPO has not come up with any comparables to justify the application of cup method. The Ld. TPO has not brought on record any material to substantiate that the AE provided the similar services to an independent enterprise in comparable circumstances. The Ld. TPO has also not brought on record any instance where comparable services were provided to an independent enterprise in the recipient market. So in view of the fact that the Ld. TPO has, in fact, not applied the CUP method to determine the arm's length price of the transaction, there is no reason to reject the TNMM method applied by the assessee. The Hon'ble jurisdictional High Court in the case of *Johnson & Johnson Ltd. (supra)* while dealing with the issue of determination of arm's length price of royalty on estimation basis by the TPO held as under:-

> *"(d) We find that the impugned order of the Tribunal upholding the order of the CIT (A) in the present facts cannot be found fault with. The TPO is mandated by law to determine the ALP by following one of the methods prescribed in section 92C of the Act read with Rule 10B of the Income Tax Rules. However, the aforesaid exercise of determining the ALP in respect of the royalty payable for technical knowhow has not been carried out as required under the Act. Further, as held by the CIT (A) and upheld by the impugned order of the Tribunal, the TPO has given no reasons justifying the technical knowhow royalty paid by the Assessing Officer to its Associated Enterprise being restricted to 1% instead of 2%as as claimed by the respondent assessee. This determination of ALP of technical knowhow royalty by the TPO was ad-hoc and arbitrary as held by the CIT (A) and the Tribunal*".

21. Hence, from the plain reading of the relevant provisions and the ratio laid down by the Hon'ble jurisdictional High Court, it can be concluded that the law does not permit the TPO to determine the arm's length price on estimation

basis. We are therefore, of the considered view that the arms length determined by the Ld. TPO is not in accordance with the provisions of the Act and the ratio of law laid down by the Hon'ble jurisdictional High Court. On the other hand the intra group services are closely linked to the business of the assessee and the assessee's benchmarking approach is based on TNMM. Further as pointed out by the Ld. counsel, the Delhi Bench of the Tribunal in the case of *Knorr Bremse India P. Ltd. vs. AICT 77 taxmann.com 101 (Delhi Tri),* has held that payment of intra group services may be benchmarked using TNMM. The observations of the Tribunal are as under:-

> *"18. As regards to the application of method for determining the Arm's Length Price, we are of the view that the method to be used to determine arm's length price for intra-group services should be in accordance with the guidelines in Chapter- I, II & III ÖECD Transfer Pricing Guidelines" which provides the various methods to be applied and the CUP method is likely to be a most appropriate method where there is a comparable service provided between independent enterprises in the recipient's market or by the AEs providing the services to an independent enterprise in comparable circumstances. In the present case, the TPO although applied the CUP method but nothing was brought on record to substantiate that the AE provided the similar services to an independent enterprise in comparable circumstances. He also did not bring on record any instance where comparable services were provided to an independent enterprise in the recipient market. Therefore, in our opinion, in the assessee's case the CUP method was not the most appropriate method. On the contrary, the assessee rightly applied the TNMM method as most appropriate method because it was difficult to apply the CUP method or the cost plus method. Therefore, the TNMM was the most appropriate method in the absence of a CUP which is applicable where the nature of the activities involved, assets used, and risk assumed is comparable to those undertaken by an independent enterprise."*

22. Section 92C(1) of the Act, contemplates that the arms length price in relation to an international transaction shall be determined by comparable

uncontrolled price method; resale price method; cost plus method; profit split method; transactional net margin method or such other method as may be prescribed by the Board. Hence, the TPO is bound to determine the ALP by following one of the prescribed methods, however, we notice that in the present case the Ld. TPO has not followed any prescribed methods and made the transfer pricing adjustment by estimating the man hours and the cost of service per hour. We therefore, find merit in the contention of the Ld. counsel that any ad-hoc determination of arms length price by the Ld TPO u/s section 92 de-hors section 92C(1) of the Act cannot be sustained. The contention of the Ld. counsel is further supported by the judgment of the Hon'ble jurisdictional High Court in the case of *Commissioner of Income Tax vs. Merck Ltd. 389 ITR 70 (Mum*). In the said case the Hon'ble High Court decline to interfere with the findings of the Mumbai Bench of the Tribunal that the transfer pricing adjustment made by the TPO without following one of the prescribed methods makes the entire transfer pricing adjustment unsustainable in law. The grievance of the revenue was that the consideration paid to the AE is only attributable to the services received / availed.

23. In the light of the facts of the case, provisions of the Law and the cases discussed in the foregoing paras, we are of the considered view that the transfer pricing adjustment made by the Ld. TPO on *ad hoc* basis is not sustainable in law. Since, the order passed by the TPO u/s 92 CA(3) of the Act is not sustainable, the Ld. DRP ought to allowed the objection filed by the assessee. Hence, we decide both the questions mentioned in para No 17 (supra) in negative and further hold that the assessment order passed by the AO pursuant to the directions passed by the Ld DRP u/s 144(5) of the Act, is not sustainable in law.

24. Now the issue arises as to whether the legal infirmity in the impugned order can be cured by restoring the issue to the Ld. TPO? On the said issue the Ld. counsel for the assessee heavily relied on the judgment of the Hon'ble Jurisdictional High Court, delivered in *CIT vs. Kodak India Pvt. Ltd.,(supra)* in

which the coordinate Bench had declined to restore the issue similar to the present case to the file of TPO holding that the methods as prescribed by the legislature are mandatory and not directory and when the mandatory provision is either superseded or ignored it affects the jurisdiction. Since, the TPO did not adhered to the prescribed methods consciously, another innings to rectify the mistake cannot be allowed. The Hon'ble High court held that the Tribunal has rightly declined to restore the similar issue to Assessing Officer for re-determining ALP by adopting one of the methods as listed out in section 92C of the Act. The relevant paras of the order of the Hon'ble Court reads as under:-

> *"10. We must also record the fact that the ALP was arrived at by the Transfer Pricing Officer (TPO) by not adopting any of the methods prescribed under section 92C of the Act. The method to determine the ALP adopted was not one of the prescribed methods for computing the ALP. It was not even any method prescribed by the Board. At the relevant time, i.e. for A.Y. 2008-09 Section 92C of the Act did not provide for other method as provided in Section 92(c)(I)(f) of the Act. The impugned order of the Tribunal holds that the method adopted by the Revenue to determine the ALP was alien to the methods prescribed under Section 92C of the Act. In the above circumstances, the Tribunal declined to restore the issue to the Assessing Officer for re-determining the ALP by adopting one of the methods as listed out in Section 92C of the Act. This finding of the Tribunal has also not been challenged by the Revenue.*
>
> *11. In view of the fact that the Revenue has accepted the order of the Tribunal on its findings on facts on the two issues as pointed out hereinabove as well as the refusal of the Tribunal to restore the issue of determination of ALP to the TPO by following one of the methods prescribed under the issue of determination of ALP to the TPO by following one of the methods prescribed under Section 92C of the Act. Thus, the question as formulated for our consideration even if answered in favour of the Revenue would become academic in the present facts. Thus, we see no reason to*

entertain this appeal. However, we make it clear that the issues of law which has been raised in the present appeal are left open for consideration in an appropriate case."

25. In view of the judgment of the Hon'ble jurisdiction High Court, the issue cannot be restored to the file of the Ld. TPO to determine the arm's length price by applying most appropriate method out of the prescribed methods under the provisions of law.

26. Hence, in the light of the facts and circumstances of the case and the ratio laid down by the courts of law discussed above, we hold that since the TPO has not made the transfer pricing adjustment by following the mandatory provisions of the law and determined the same on estimation basis, action of the Ld. DRP in upholding the TP adjustment so made by the Ld. TPO is bad in law. So far as the cases relied upon by the Ld. DR is concerned, we are of the considered view that the facts of the said cases are different from the facts of the present case. Since, the Ld. TPO has not determined the arm's length price in accordance with the provisions of law, there is no reason to hold that the TNMM method applied by the assessee is not the most appropriate method within the meaning of section 92C of the Act.

27. We therefore, decide Ground No. 3 to 3.4 of the appeal in favour of the assessee and allow the appeal of the assessee and direct the AO to delete the upward adjustment of Rs. 143,67,42,784/- confirmed by the Ld. DRP.

In the result, appeal filed by the assessee for assessment year 2012-2013 is allowed.

Order pronounced in the open court on 16th January, 2019.

Sd/-	*Sd/-*
(R.C. SHARMA)	(RAM LAL NEGI)
ACCOUNTANT MEMBER	JUDICIAL MEMBER

मुंबई Mumbai; **दिनांक** Dated: 16/01/2019

Alindra, PS

आदेश प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1. **अपीलार्थी** / The Appellant
2. **प्रत्यर्थी** / The Respondent.
3. **आयकर आयुक्त(अपील)** / The CIT(A)-
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//

उप/सहायक पंजीकार (Dy./Asstt. Registrar)

आयकर अपीलीय अधिकरण, मुंबई / ITAT, Mumbai