

**IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH 'I-2', NEW DELHI**

Before Ms. Suchitra Kamble, Judicial Member

Dr. B. R. R. Kumar, Accountant Member

ITA No. 9374/Del/2019 : Asstt. Year : 2015-16

Nissin Brake India Pvt. Ltd., SP-1-33-35, New Industrial Area, Phase-III, Neemrana, Alwar Rajasthan-301705	Vs	Deputy Commissioner of Income Tax, Circle-3(1), Gurugram
(APPELLANT)		(RESPONDENT)
PAN No. AACCN3633K		

Assessee by : Sh. Vishal Kalra, Adv.

Revenue by : M. Bernwal, Sr. DR

Date of Hearing: 28.02.2020	Date of Pronouncement: 05.05.2020
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ORDER

Per Dr. B.R.R. Kumar, Accountant Member:

The present appeal has been filed by the assessee against the order dated 11.10.2019 passed by the AO u/s 143(3) r.w.s. 144C of the Income Tax Act, 1961.

2. Following grounds have been raised by the assessee:

"1. That on the facts and circumstances of the case and in law, the AO has erred in assessing the total income of the Appellant for the relevant AY at INR 19,52,28,784 as against the Nil returned income.

2. That on the facts and circumstances of the case and in law, the AO / Honorable Dispute Resolution Panel ("Hon'ble DRP") / Transfer Pricing Officer ("TPO") erred in making a transfer pricing adjustment of INR 7,21,09,339 on substantive basis and of INR 1,86,28,342 on protective basis.

Adjustment made on substantive basis and (Payment of royalty and product development fees)

3. *That on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in arbitrarily applying benefit test and Comparable Uncontrolled Price ("CUP") method to benchmark the ALP of royalty and product development payments as Nil, without appreciating that the Hon'ble Tribunal in Appellant's own case for AY 2013-14 and AY 2014-15, has rejected the said approach.*

4. *That on the facts and circumstances of the case and in law the AO / DRP / TPO erred in arbitrarily holding that the Appellant has not demonstrated any benefit received on account of royalty and product development services fees paid to Associated enterprises ("AE").*

5. *That on the facts and circumstances of the case and in law, the AO / DRP / TPO while determining the ALP of royalty and product development payments as Nil, alleged that the effective royalty payments to the AEs amounted to 7.2% by taking into consideration certain irrelevant expenses without appreciating that the below mentioned expenses had no nexus to the royalty / product development payments made by the Appellant:*

- a. License to use trademark and to manufacture, use and sell the products manufactured by Nissin India which is only 3%*
- b. Payment for technical services*
- c. Payment for product development services*

6. *That on the facts and circumstances of the case and in law the AO / DRP / TPO erred in questioning the commercial expediency for incurring royalty and product development expenditure without providing any cogent reasons, especially, when the said amount was incurred wholly and exclusive for the purposes of business.*

7. That on the facts and circumstances of the case and in law, the AO / TPO erred in rejecting the supplementary benchmarking exercise for payment of royalty wherein this transaction was compared with the companies operating in automotive industry. Further, the DRP erred in summarily rejecting the alternate benchmarking.

8. That on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in not considering the benchmarking submitted by the Appellant wherein it has been shown that third party is also paying royalty to Nissin Kogyo Co. Ltd. ("Nissin Kogyo") at similar rate.

9. That on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in not considering that other group companies in the Nissin Group are also paying royalty and product development fees to Nissin Kogyo.

10. That on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in not considering the detailed evidences furnished in relation to product development fees wherein the detailed functions being performed by the Appellant and Nissin Kogyo had been submitted.

11. That on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in relying on prior year's order irrespective of the fact that sufficient information / documentation were furnished for the captioned year.

12. That on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in disregarding its own approach in the case of the Appellant for AY 2009-10, AY 2010-11 and AY 2012-13, wherein the similar approach adopted by the Appellant was accepted, i.e., TNMIM as the most appropriate method for benchmarking the international transaction in relation to payment of royalty and product development service fees.

**Adjustment made on protective basis
(Comparability analysis)**

13. That on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in arbitrarily rejecting 1 comparable company selected by the Appellant in its transfer pricing documentation for benchmarking the manufacturing segment without any valid and cogent reasons.

14. That on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in arbitrarily selecting certain additional comparable companies for determining arm's length price of the manufacturing segment.

15. That on the facts and circumstances of the case and in law, the AO / TPO erred in rejecting the alternative approach to consider PBDIT / Sales as the Profit Level Indicator. Further, the DRP erred in summarily rejecting the alternate the alternate approach.

16. That on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in rejecting adjustment sought on under-utilization of capacity without taking cognizance of the fact that the Appellant was operating at different level of capacity as compared to comparables and hence economic adjustment for the difference in capacity levels was warranted.

17. That on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in disregarding their own approach adopted for the AY 2009-10 and AY 2010-11, where Appellant has been granted capacity utilization adjustment.

18. That on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in disregarding the approach adopted by Hon'ble Tribunal in the case of Appellant for AY 2010-11, AY 2012-13 and AY 2013-14, wherein the Hon'ble Tribunal has granted capacity utilization adjustment to the Appellant.

19. Notwithstanding and without prejudice to grounds of Appeal Nos. 3 to 10, that on the facts and circumstances of the case and in law, the AO / DRP / TPO erred in including the payment of royalty and product development fees while calculating the total value of international transactions for the purpose of granting proportionate adjustment.

20. That on the facts and circumstance on the case and in law, the AO failed to provide the relief on account of brought forward losses in the income tax return.

21. That on the facts and circumstances of the case and in law, the AO erred in proposing to charge interest under section 234B and 234C of the Act.

22. That on the facts and circumstances of the case and in law the AO erred in initiating penalty proceedings u/s 271(1)(c) of the Act."

3. The assessee is a subsidiary of Nissin Kogyo Co. Ltd., Japan ("Nissin Kogyo") and is engaged in manufacturing, altering, conversion, procurement, sale and trading of various automotive and aluminium and / or non-automotive brake and aluminium components, spare parts and other related accessories.

4. During the year, the assessee entered into various international transactions with its associated enterprises ("AEs") which was a subject matter of Transfer Pricing study leading to change in the transfer pricing method of TNMM to CUP and consequently inclusion of five entities as comparables which ultimately led to adjustment of 1.72% of profit against the 3.14% shown by the assessee in the TP documentation. The TPO made adjustments substantially on account of royalty and product development fees and protective adjustment has

been made in the manufacturing segment by selecting comparables which are purportedly in the similar line of business as that of the assessee. The Id. DRP vide order dated 27.08.2019 has not interfered on the issue of **royalty and product development fees** and directed that adjustments should be computed on the transactions carried with AE only. Thus, after restricting the transactions carried with the AE, the adjustment in the **manufacturing segment** on protective basis has been tapered down to Rs.186,28,342/- from Rs.746,67,093/-.

5. The assessee is in appeal before us on the issue of royalty payment as well as the adjustment in the manufacturing segment.

Royalty Payment:

6. The assessee entered into holding company for grant of rights to use the trademarks and to manufacture products which are under ITR. The assessee's contention is that the agreement is not limited to the drawings but also applicable to designs, product standards, quality control and engineering & testing data too. It was contended that it is a running royalty paid by the assessee to Nissin Kogyo for the products manufactured, procured and sold by the assessee @ 3% of the value added. The basic issue of payment of royalty at the rate of 3% was objected by the revenue on the grounds that it is only an arrangement to transfer the profits without any economic substance whereas the assessee strongly relied on the fact that the other group companies based at Philippines and Ohio Inc. also pay royalty at the rate of 3%. The assessee

also relied on the fact that even the third parties which are unrelated to the holding company namely, Hengtong also paid royalty at the rate of 3% and contended that there was no need to adjustment of the royalty paid.

7. Further, the revenue has made the adjustment under the CUP method against the TNMM as the most appropriate method resorted by the assessee.

8. The similar issue in the case of the assessee has come up before the ITAT for the assessment years 2013-14 (ITA 6366/Del/2017) and 20014-15 (ITA 6962/Del/2018) wherein it was held that royalty is intrinsically linked with the production and sales. The Tribunal also set aside the impugned order and remanded the issue back to the Id. TPO to decide it afresh after providing an opportunity to the assessee. Aggrieved with the order of the Tribunal for the assessment year 2013-14, the revenue preferred before the jurisdictional High Court

9. The Hon'ble Jurisdictional High Court of Punjab & Haryana vide order dated 10.01.2020 held that there is no need to deviate from TNMM followed by the assessee to CUP method followed by the revenue.

10. Hence, keeping in view the judgment of the Hon'ble Jurisdictional High Court, we hereby direct the revenue to determine adjustments considering the TNMM as the most appropriate method. The appeal of the assessee on this ground is treated as allowed.

Product Development Cost:

11. During the year, the assessee received product development services from the parent company and has paid fees for the same on cost-to-cost basis. The revenue contended that the assessee has carried out R&D activities during the year based on the correspondence between the assessee and the holding company. The revenue contended that the assessee is paying unreasonable amount of royalty to the parent company on this head. The assessee submitted that they do not have any R&D centre in India and all product development activities are done by the parent company and product development cost consists of R&D services for existing and new products. The assessee contended that all the customer specific request for R&D and modification are being carried out by the parent company on behalf of the assessee company. The agreement, calculation of product development fees and the invoices raised by the AE have been a part of the paper book which have been duly perused.

12. The facts reveal that the revenue has accepted the assessee's contention for the assessment years 2009-10 and 2010-11. The Tribunal and the Hon'ble Jurisdictional High Court held that TNMM be the most appropriate method for benchmarking the transaction.

13. Hence, keeping in view the judgment of the Hon'ble Jurisdictional High Court, we hereby direct the revenue to determine adjustments considering the TNMM as the most appropriate method. The appeal of the assessee on this ground is treated as allowed.

Adjustment on Protective Basis:

14. At the outset, we hold that protective adjustment and substantive adjustment for the same assessee are not required to be done by the revenue. Protective and substantive adjustments are resorted when there is lack of clarity owing to peculiar circumstances which are equal applicable to two different assesseees pertaining to the same taxable income and the matter needs to be put at rest at level of revenue authorities.

15. Since, this issue is inter related with the TNMM as the most appropriate method, we hereby adjudicate on the suitability of the comparables.

16. The issues raised before us pertains to rejection of one comparable selected by the assessee in their TP documentation and selection of five comparables by the revenue in their TP study.

17. The submissions of the Id. DR on the comparables is as under:

"Issues pertaining to Transfer Pricing Adjustments on alternate argument with respect to addition on protective basis following TNMM subject to the departments stand for the substantive addition following CUP method :

1. The assessee has mainly challenged the inclusion of following comparables on functional dissimilarity:

- (i) Admach Auto India Ltd.*
- (ii) ASK Automotive Pvt. Ltd.*
- (iii) Gabriel India Ltd.*
- (iv) Brakes India Pvt. Ltd.*
- (v) Munjal Showa Ltd.*

Printout of screen shot of website of these comparable companies are enclosed showing their respective business profile/manufacturing activity.

2. All the above comparable companies are in the manufacturing business of either braking systems or shock absorbers or both which are essentially connected with automobile sector and are very much identical to the line of business profile/manufacturing activity undertaken by the assessee. For the purpose of comparability under TNMM, all these companies have been identified by the TPO after applying appropriate filters as elaborately discussed in his order and the same has also been upheld by Ld. DRP.

3. The functional comparability with respect to these comparable companies with the appellant company is also supported by the meaning of 'Core Auto components' given

It has been held that "In our considered opinion, no two comparable companies can be replicas of each other. The application of Rule 10B should be carried out and judged not with technical rigor, but on a broader prospective."

[Para 36, P/38 of the order dated 22.07.2011.]

6. Accordingly, it is requested that the above comparables may kindly be considered to be retained for comparability under TNMM.

7. As regards exclusion of Foundation Brake Manufacturing Pvt. Ltd. the TPO has excluded this company from the final set of comparables on the ground of continuous losses being shown by this company for last 3 years. Before DRP the assessee did not object to this filter and accordingly Hon'ble DRP held that the same has been rightly rejected. Accordingly, it is requested that this comparable may kindly not be considered for inclusion under TNMM."

18. The entities are examined as to their relevance and comparability.

1. Admach Auto India Ltd.: The comparable manufactures sheet metal components against the brake system manufactured by the assessee company. As per Rule 10TA(b) and Rule 10TA(h) of the Income Tax Rules, 1962, a separate definitions have been laid down for core auto components and non-core auto components. As per Rule 10TA(b)(3), the core auto components means, suspension breaking parts including brake and brake assemblies, brake lining, shock absorbers and leaf springs and Rules 10TA(h) defines "non-core components" means auto components other than core auto components.

Since, the business of the assessee is "core auto components", we hold that it cannot be compared with an entity which is in the business of "non-core auto components". This comparable cannot be considered for the study.

2. ASK Automotive Pvt. Ltd.: The turnover of the company is Rs.937 crores compare to the turnover of Rs.220 crores of the assessee company. Hence, it was argued that it cannot be a right comparable. Further, the comparable incurred expenditure on R&D activities whereas the assessee company doesn't have any R&D centre in India. We find that the brake shoes manufacturing which is a core auto components consists of 28.97% of the total turnover of the company which is approximately Rs.270 crores. Hence, the turnover is not an impediment for comparative study. We also find that the R&D expenditure incurred by the ASK Automotive Pvt. Ltd. is very minimal which would not alter the comparison to a considerable extent. Hence, we hold that ASKAPL may be considered as a correct comparable.

3. Gabriel India Ltd.: This company is primarily into manufacturing of front forks and shock absorbers. Since, they are non-core auto components owing to the difference in the products manufacturing it cannot be treated as a right comparable.

4. Brakes India Pvt. Ltd.: The product line is similar to that of the assessee. However, the turnover of this comparable is 16 times to that of the assessee's turnover. In general that the turnover filter is adopted to avoid selection of high-end companies with that of minnows in a similar line of business. The range cannot be fixed and how to adopt the filter depends on the facts of each case. High turnovers cannot be rejected *prima facie* while low turnovers are accepted when it suits to the parties without objections from either of the sides. An acceptable range would be the turnover of the taxpayer and the range of the upper limit at ten times as well as the lower limit at ten times (1/10) with a margin of variation may be considered as a right comparable. Since, in this case the turnover is 16 times which is well beyond the margins for a right comparison and eliciting correct results. Hence, we hold that BIPL may not be considered as a comparable in the instant case.

5. Munjal Showa Ltd.: The company is engaged in the manufacturing of shock absorbers, struts and rear cushions. Since, the product line is different the profits cannot be comparable and hence cannot be considered as a right comparable.

6. Foundation Brake Manufacturing Pvt. Ltd.: The company has been showing losses continuously for the last three years and doesn't cross the proposed filter, hence cannot be considered as a right comparable.

Ground No. 16: Capacity Utilization Adjustment

19. We have gone through the record and the orders of the Tribunal for the earlier three assessment years i.e. assessment years 2010-11, 2012-13 and 2013-14 wherein the capacity utilization adjustment has been duly granted. Keeping in view the industrial standing of the comparable, we hereby direct that the same benefit may be accorded in the instant year.

Ground No. 20: Brought forward losses

20. The AO is directed to consider relief on account of brought forward losses as per the Income Tax Act after taking into consideration the business losses and unabsorbed depreciation as per the earlier returns filed by the assessee.

21. In the result, the appeal of the assessee is allowed.

Order Pronounced in the Open Court on 05/05/2020.

Sd/-

(Suchitra Kamble)
JUDICIAL MEMBER

Sd/-

(Dr. B.R.R. Kumar)
ACCOUNTANT MEMBER

Dated: 05/05/2020

Subodh

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

ASSISTANT REGISTRAR