

IN THE INCOME TAX APPELLATE TRIBUNAL
PUNE BENCH “C”, PUNE – VIRTUAL COURT

BEFORE SHRI R.S. SYAL, VICE PRESIDENT AND
SHRI S.S. VISWANETHRA RAVI, JUDICIAL MEMBER

ITA No.2986/PUN/2017

निर्धारण वर्ष / Assessment Year : 2013-14

Adient India Private Limited Plot No.1, S No.235 & 245, Hinjewadi, Tal-Mulshi, Pune - 411057 PAN : AAAC6342D	Vs.	DCIT, Circle-1(1), Pune
Appellant		Respondent

Assessee by

Shri Dhanesh Bafna

Revenue by

S/Shri Kalika Singh &
Madhavan A.M. Krishnan

Date of hearing

27-05-2021

Date of pronouncement

31-05-2021

आदेश / ORDER

PER R.S.SYAL, VP :

This appeal by the assessee is directed against the final assessment order dated 27-10-2017 passed by the Assessing Officer (AO) u/s.143(3) read with section 144C(13) of the Income-tax Act, 1961 (hereinafter also called ‘the Act’) in relation to the assessment year 2013-14.

2. The only issue raised in this appeal is against transfer pricing addition of Rs.5,95,39,429. Succinctly, the factual matrix of the case is that the assessee was earlier a 50:50 joint

venture between Johnson Controls International B.V. Netherlands and Tata Automotive Components Systems Limited (TACO). With effect from 25-03-2013, 50% of TACO's stake was purchased by Johnson Control Auto India Limited, thereby making it a 100% subsidiary of Johnson Controls Group. The assessee has been engaged in manufacture & sale and trading of automotive seating systems. The return was filed declaring total income of Rs.60.60 crores. The assessee reported certain international transactions and Specified Domestic Transactions (SDTs). The AO made a reference to the Transfer Pricing Officer (TPO) for determining the Arm's Length Price (ALP) of such transactions. In this appeal, we are concerned only with the SDT of "Service charges paid" to TACO amounting to Rs.5,95,39,429. The assessee applied the Comparable Uncontrolled Price (CUP) method for demonstrating this transaction to be at ALP. In doing so, the assessee chose 13 agreements from Royaltstat and Ktmine database of Buying & sales agent, Distribution, Sales representative, Marketing & advertising with the average fee paid at 5.43% as against its payment for the services at 1% only. The TPO required the

assessee to tender evidence of availing the services from TACO. After entertaining the evidence submitted by the assessee, the TPO held that there was no worthwhile evidence of receipt of the services and even if some services were availed, those were only either general or in the nature of the shareholders' activities. He further held that the assessee failed to exhibit any benefit derived from such services. In the hue of such factual panorama, the TPO refused to accept the CUP method originally applied by the assessee, which was based on the comparables chosen that were rendering Marketing services only as against the assessee availing services in Human resource and training, Group policies/Databases, Marketing and sales, Finance, Legal and taxation advisory and other strategic services. During the course of the proceedings before the TPO, the assessee came forward with an alternate benchmarking analysis under Transactional Net Marginal Method (TNMM) by aggregating the transaction of receipt of Administrative services along with others, which the TPO refused to accept on the ground of aggregation. He took recourse to 'any other method' under rule 10AB of the Income-tax Rules, 1962 (hereinafter referred

to as 'the Rules') and observed that this method also recognizes 'the price which would have been paid' as a valid base for determining the ALP. The TPO opined that since no services requiring payment of any consideration were availed by the assessee, no independent party would have paid anything for such services. This is how, the TPO determined nil ALP of the transaction of service charges paid. This resulted in proposing a transfer pricing adjustment of Rs.5.95 crores. The AO notified the transfer pricing addition of the equal amount in the draft order. The Dispute Resolution Panel (DRP) did not find anything amiss in the view taken by the AO/TPO and countenanced the addition, against which the assessee has come up in appeal before the Tribunal.

3. We have cogitated over the rival submissions through Virtual Court and scanned the relevant material on record. The TPO determined Nil ALP of the SDT of 'Service charges paid' to TACO on the premise that the assessee did not avail any services for which any compensation could have been paid. The issue under consideration can be decided by answering the following two questions:

I. Whether any services requiring payment were availed by the assessee? and

II. If yes, what is its ALP?

We espouse these two questions *ad seriatim*.

I. Whether any services requiring payment were availed by the assessee?

4.1. The assessee entered into Administrative Service Agreement (ASA) on 02-02-2005 with TACO for receipt of services comprising of Human resource, Group policies/Databases, Marketing and sales, Finance and Legal & taxation advisory services. A detailed chart has been placed at pages 434 onwards of paper book indicating the description of various services under the above referred broad categories of services availed. Under Marketing and sales support services, the assessee has referred to the services received from TACO team whose details have been provided at pages 449 to 527 of paper book. The first document at page 449 onwards is recommendation of the price strategies and other commercial terms by TACO team which provided assistance to the assessee by circulating “SIAM Monthly Monitor-Commodity Prices”, a guideline on price trends of various commodities

which may influence the automobile industry. The next document is the TACO team assisting the assessee in evaluating various production and sales report on yearly basis of General Motors with production schedule of the relevant models. The next document is sharing of cumulative details of production of passenger vehicles, commercial vehicles, two wheelers and three wheelers in the market with a view to help the assessee in analyzing the overall market trend and planning the production based on the projected trend. Under the next broader head of Group policies/Databases, TACO provided services which have been detailed at pages 542 to 606 of paper book. The first document is of TACO providing access to the assessee to its operating system in order to ensure that the policies are accessible to all the employees at a single stop. There is another document giving the mobile phone and accessories policy laying down the eligibility of the employees who shall be entitled to receive a mobile phone and other related accessories. All the relevant e-mails on such services have been placed in the paper book. The next broader head of the services is 'Human Resource and Training'. The details of such services along with e-mails are available at pages 608 to

681 of paper book. Through such documents and e-mails, TACO recruited the assessee's personnel, sales managers, engineers and operators, etc. and also took HR reviews. It also circulated a standard format of increment letter and promotion letter, etc. The next broader head of the services is 'Finance'. The details of such services have been set out at pages 698 to 772 of paper book. The services availed by the assessee under this head relate to guidelines of budgeting, monitoring the entire process of preparing of budgets; internal auditing and relevant registers / records to be maintained. Similar is the position under the head of Legal and taxation advisory services. The details of such services have been given at pages 774 to 901 of paper book, which deal with the circulation of relevant case laws on allowability of interest, circulation of income-tax instructions with respect to standard operating procedure for filing of appeals to High Court, etc., updation of TDS certificates, case laws on admissibility of input service tax credit to the assessee, advance tax template, differential custom duty and case law under relevant tax provisions. From the above cumulative details of all the services running into more than 450 pages, it

is more than evident that TACO provided specific and also exclusive services under the Agreement to the assessee along with certain other group entities, which are not general in nature but precise, detailed and specific.

4.2. The TPO determined Nil ALP by assigning another *raison d'être* that the assessee failed to show any benefit received by it from the services. In our considered opinion, what is relevant is to consider the availing of the services and not the resultant benefit arising there from. Every expenditure incurred by a businessman cannot necessarily lead to swelling the profit. If the proposition of the TPO is taken to a logical conclusion, then it would mean that no business would ever incur loss, which is not a reality. The important consideration is the incurring of *bona fide* expenditure and availing of service, which may or may not lead to the increased income. Application of the benefit test is not warranted. Enquiry in this regard should come to an end as soon as the factum of availing the services for the business purpose is established. We have noticed above that the assessee did avail the services from TACO for running its business operations. As such, there was no need to look beyond that and search for some

benefit accruing to the assessee as a pre-condition for allowing the deduction.

4.3. The TPO also held that the services, if any, availed by the assessee were in the nature of shareholders services, not requiring payment of any consideration. Suffice to say, shareholder or stewardship services take place when some act or service is done by a shareholder to the company in order to ensure that his investment in the shares is safe and further such an act or service does not produce any effect to the company receiving it. From the detailed narration of services above, it is overt that the services did produce effect to the assessee company. As such, they go outside the ambit of the shareholder services as branded by the TPO. It is, therefore, held that TACO rendered specific and also exclusive services to the assessee, which are not in the nature of shareholder services, and hence require payment of consideration as a *quid pro quo* in an uncontrolled situation.

II. If yes, what is its ALP?

5.1. Having found that the assessee availed services from TACO requiring payment of consideration, the next question

is determination of its ALP. It is seen that the assessee entered into 16 international transactions and 10 SDTs in total. The SDT under consideration was benchmarked by the assessee under the CUP method. The assessee, in alternative and without prejudice to the CUP as the most appropriate method, also put forth the ALP determination under the TNMM before the TPO, who rejected both of them and applied the 'Other method' under rule 10AB to determine Nil ALP. Now the case of the assessee before the Tribunal is that the CUP method was correctly applied by it and further that if this method is not acceptable, then the TNMM, as applied by it, should be accepted. The last alternative contention in this regard is that in any case, the 'Other method' can be applied based on the 'reasonableness' of the amount paid. We will examine these contentions, one by one.

A. CUP method

6.1. While applying the CUP method, the assessee selected 13 agreements from Royaltstat and Ktmind databases for Buying & sales agent, Distribution, Sales representative, Marketing & advertising. The TPO did not accept the determination of the ALP under this method mainly because of

the functional difference in the nature of services availed by the assessee and those selected under the external CUP method. In this regard, it is observed from the ASA that the assessee availed a bouquet of services from TACO comprising of Human resource, Group policies/Databases, Marketing and sales, Finance and Legal & taxation advisory services. As against that the assessee chose certain 13 comparables agreements from foreign databases which were in the field of Marketing only. Rule 10B(2) provides that for the purposes of sub-rule (1), 'the comparability of an international transaction or a specified domestic transaction with an uncontrolled transaction shall be judged with reference to the following, namely:— (a) the *specific characteristics of the property transferred or services provided* in either transaction; (b) the *functions performed*, taking into account assets employed or to be employed and the risks assumed, by the respective parties to the transactions;.....'. Thus it is evident that the specific characteristics of the services provided must be similar while benchmarking a SDT. Since the CUP method seeks comparison on the basis of price charged or paid, as opposed to profit rate in most other methods, the functional similarity

between the transaction under consideration and that of the comparables assumes fundamental importance. The nature of services/properties received/ transferred must be quite similar, if not identical with the transaction under consideration. The level of similarity between the comparable transaction(s) and the transaction to be benchmarked needs to be of the highest order under the CUP method. It is wholly impermissible to pick up any service and then compare it with service to be benchmarked. If the functional comparability lacks, as is the case under consideration, then the CUP method cannot be applied with such a truncated data. As the assessee in the instant case availed a bunch of services consisting of Finance, Human resources, Legal, Marketing and Group policies/databases, it cannot be logically compared with companies rendering only marketing services.

6.2. Another factor which is of quite significance in the case under consideration is that the assessee chose 13 comparable agreements from Royaltstat and Ktmind databases that record transactions of foreign countries only. Rule 10B(2) also adds that for the purposes of sub-rule (1), 'the comparability of an international transaction or a specified domestic transaction

with an uncontrolled transaction shall be judged with reference to....(d) *conditions prevailing in the markets in which the respective parties to the transactions operate*, including the *geographical location* and size of the markets, the laws and Government orders in force, costs of labour and capital in the markets, overall economic development and level of competition and whether the markets are wholesale or retail.’ As the assessee is an Indian entity and has paid to TACO, another Indian entity for the services availed in India, comparison has to be necessarily made with the parties availing similar services in India only.

6.3. The above analysis delineates and deciphers that neither the comparables chosen by the assessee rendered similar services nor were they located in India. In our considered opinion, the authorities below were justified in rejecting the CUP method applied by the assessee in such a manner.

B. Any other method

7.1. The TPO, after rejecting the assessee’s benchmarking under the CUP method, proceeded to determine the ALP of the transaction under ‘other method’ as per rule 10AB of the Rules. He found this method contemplating the ALP

determination not only on the basis of the price charged or paid for the same or similar transactions but also the price that *would have* been charged or paid. Since he came to the conclusion that the assessee did not avail any services requiring the payment, he held that no independent party *would have* paid for similar services and thus determined nil ALP under this method.

7.2. Rule 10AB provides that: “For the purposes of clause (f) of sub-section (1) of section 92C, the other method for determination of the arm's length price in relation to an international transaction or a specified domestic transaction shall be any method which takes into account the *price which has been charged or paid, or would have been charged or paid*, for the same or similar uncontrolled transaction, with or between non-associated enterprises, under similar circumstances, considering all the relevant facts.” A bare perusal of the rule makes it graphically clear that the ‘other method’ is the one which not only encompasses the price actually charged or paid for benchmarking but also the price which *would have been charged or paid* in a comparable uncontrolled transaction. Any potential price which could be

charged or paid for similar goods/services, even though not actually transacted, can also be accepted for benchmarking the SDT under consideration. In principle, no fault can be found with the TPO in interpreting the rule in the way he did. However, the steps following such an interpretation went awry as he determined the Nil ALP on the bedrock that no services were actually availed by the assessee requiring payment of any consideration, which has been overturned *supra*. Thus, the application of this method by the TPO in this way is rendered nugatory.

7.3. The Ld. AR urged for the application of the 'other method' in the instant case and harped on reasonableness of the expenditure as a yardstick for deeming the transaction to be at ALP. To buttress his point of view, he relied on the Tribunal order passed in certain group companies, in which similar issue was involved about payment to TACO for availing similar services. Our attention was drawn towards the Tribunal order in Yazaki India Private Limited Vs. DCIT for the A.Y. 2009-10 deleting the disallowance, paid at 1.31% of the sales, u/s 40A(2) for availing similar services from TACO. In this order dated 11-07-2019 in ITA No.621/PUN/2014, the

Tribunal observed that in the case of Tata Johnson Controls Automotive Ltd. Vs. DCIT, the Pune Benches of Tribunal accepted the payment to TACO at 1% of turnover as reasonable. Similar view was taken in another group company, Tata Ficosa Automotive Systems Ltd. Vs. DCIT, in which payment was made to TACO for similar services at 2% of net sales, which was disallowed by the AO u/s 40A(2) and the Pune Tribunal deleted the same. The Ld. AR further referred to the decision of the Tribunal in the assessee's own case for the A.Y. 2008-09 in which disallowance u/s 40A(2) for such services came to be deleted. It is on the strength of the acceptability by the Tribunal of the payments made by the group concerns to TACO for similar services as reasonable, which were disallowed by the AO u/s 40A(2), that the Ld. AR submitted that the same 'reasonableness criteria' should be applied in determining the ALP under rule 10AB also. The Id. DR took strong exception to the view canvassed by the Id. AR in this regard.

7.4. The Finance Act, 2012 brought SDTs within purview of transfer pricing provisions under Chapter X of the Act w.e.f. 1.4.2013. The term 'SDT' has been defined u/s 92BA to

include, *inter alia*, any expenditure in respect of which payment has been made or is to be made to a person referred to in section 40A(2)(b). Prior to that, the disallowance was governed by section 40A(2) only. Clause (i) containing the above mandate remained on the statute till 1.4.2017 before its omission by the Finance Act, 2017. The assessment year under consideration is 2013-14 and accordingly clause (i) is applicable, which requires determining the ALP of the SDT of payment to TACO for availing the services. It goes without saying that the criteria for determining the ALP under Chapter X is entirely different from examining the reasonableness of expenditure u/s 40A(2). Had the position been similar, there was no need to include section 40A(2) disallowance cases within the purview of the transfer pricing provisions. Section 40A(2) simply provides for making disallowance of any expenditure which is excessive or unreasonable having regard to the fair market value of the goods or services, etc. On the other hand, Chapter X contemplates determining the ALP strictly as per one of the methods prescribed in Income-tax rules. Further, primary responsibility of demonstrating that the specified domestic transactions is at ALP is that of the

assessee as against the responsibility of the AO to prove that the expenditure was excessive u/s 40A(2). The concept of 'reasonableness' u/s 40A(2) is alien to Chapter X that simply requires determination of the ALP under one of the methods prescribed as per section 92C. All the decisions relied by the Id. AR have been delivered in the context of disallowance made u/s 40A(2) for the assessment years 2009-10 or prior thereto. The conclusion arrived at by the Tribunal in such orders deleting the disallowance u/s 40A(2) is of no avail in determining the ALP of SDTs under the transfer pricing provisions. Once the ALP is to be determined under Chapter X, one needs to strictly adhere to the mechanism set out in the respective methods and not go arbitrarily by any non-prescribed mode or method. Vindicating the assessee's contention of applying the test of 'reasonableness' in the context of transfer pricing provisions would be too simplistic an approach leading to laying down a preposterous interpretation of the Chapter-X.

7.5. There is another reason for not accepting the assessee's contention of accepting the SDT at ALP on the basis of reasonableness of the expenditure. All the cases relied by the

ld. AR are the transactions between TACO and other group companies, such as, Tata Johnson Controls Automotive Ltd., Tata Ficosa Automotive Systems Ltd. and the assessee itself. Relevant part of rule 10AB provides for considering the price which has been charged or paid, or would have been charged or paid, for the same or *similar uncontrolled transaction, with or between non-associated enterprises...*. It is overt from the language of rule 10AB that the rule making authority has envisaged comparison of the SDT with the price charged or paid or would have been charged or paid for the same or “similar uncontrolled transaction with or between non-associated enterprises”. Two expressions have been simultaneously used in the rule, namely, ‘uncontrolled transaction’ and ‘between non-associated enterprises’. Rule 10A(ab) defines ‘uncontrolled transaction’ to mean: ‘a transaction *between enterprises other than associated enterprises, whether resident or non-resident*’. It is thus manifest that the prohibition to use transactions between the associated enterprises for the ALP determination under the ‘other method’ has been doubly ensured, firstly, by stating that there should be an ‘uncontrolled transaction’ and then further

qualifying it by 'with or between non-associated enterprises'.

A *fortiori*, if the transactions for comparison are between associated enterprises or in other words, controlled transactions, the same cannot be considered for the benchmarking exercise.

7.6. Indisputably, all the transactions cited as evidence of 'reasonableness' are between the associated enterprises and hence controlled transactions. When the legislature specifically provided for considering transactions only between non-associated enterprises, it is absolutely unwarranted to consider any transaction between two associated enterprises for determining the ALP under rule 10AB. We, therefore, jettison the contention advanced on behalf of the assessee in this regard and hold that the transactions between two related enterprises cannot be construed at ALP on the basis of reasonableness of the amount *per se*.

C. TNM Method

8.1. During the course of the hearing before the TPO, the assessee put forth a without prejudice argument of adopting the TNMM as most appropriate method for showing the SDT

at ALP. The assessee did this exercise by aggregating the SDT with other international / specified transactions, which approach came to be abrogated by the TPO by holding that the payment for the 'Administrative service charges' could not be aggregated with all other transactions. The ld. AR re-emphasized the same argument before the Tribunal.

8.2. Section 92(1) of the Act provides that any income arising from 'an international transaction' shall be computed having regard to the arm's length price. Section 92C(1) provides for the computation of the ALP and mandates to follow one of the prescribed methods as the most appropriate method, which, *inter alia*, include the TNM method, as has been applied by the assessee on without prejudice basis on aggregate basis and got snubbed at the hands of the TPO. The mechanism for determination of the ALP under the TNMM has been provided in Rule 10B(1)(e) of the Rules. The term 'transaction' has been defined in Rule 10A(d) as including '*a number of closely linked transactions*'. It, therefore, boils down that the term 'transaction' also includes a plural of transactions. However, the caveat is that in order to cover plural of transactions within the term 'transaction' under Rule 10A(d), it is *sine qua non*

that such number of transactions must be closely linked. If they are not closely linked, then there can be no question of their aggregation for the purpose of determining the ALP under the Rules.

8.3. In one sense, closely linked transactions mean similar or alike transactions of purchase or sale etc. of goods or services. To put it simply, if there are several transactions of, say, purchase of similar goods or goods with minor variations, then instead of finding the ALP of such transactions individually, it satisfies the prescription of closely linked transactions if these are combined and benchmarked in an aggregate manner. However, where the transactions are of diverse nature, they would justify aggregation only if inter-related. The Hon'ble Punjab & Haryana High Court in *Knorr-Bremse India P. Ltd. VS. ACIT (2016) 380 ITR 307 (P&H)* has dealt with three circumstances in which the aggregation is permissible. First, in case of a package deal where each item is not separately valued but all are given a composite price, these are to be taken as one international transaction. Two, where a number of transactions are priced differently but on the understanding that the pricing was dependent upon the assessee accepting all

of them together (i.e. either take all or leave all), then also they should be viewed as one transaction. But it will be on the assessee to prove that although each is priced separately, but they were provided under one composite agreement. Three, where each component was priced differently, but they are inextricably linked in such a way that one cannot survive without the other. The Hon'ble High Court held that merely because purchase of goods and acceptance of services leads to manufacture of final product, it does not follow that they are dependent transactions requiring aggregation. We find that the extant case is not covered any of the three situations. The Hon'ble Delhi High Court in *Magneti Marelli Powertrain India Pvt. Ltd. vs. DCIT (2016) 389 ITR 469 (Delhi)* held that Royalty and technical assistance fee did not form part of a composite transaction and have to be treated as two separate transactions for computing arm's length price.

8.4. On an examination of the nature of the SDT of payment of service charges by assessee to TACO, it turns out that the same is entirely different and not at all inter-related with other transactions that the assessee aggregated with. It is just elementary that intra-group services cannot be clubbed with

the manufacturing or trading transactions undertaken by the assessee justifying aggregation. We, therefore, hold that the TPO was justified in repelling the assessee's aggregation approach under the TNMM.

9. Having found that the mechanism applied either by the assessee or the TPO under all the three methods is improper, we are left with nothing to adjudicate upon. The Tribunal, being an adjudicating and not an original authority, cannot usurp the power of the AO/TPO and itself undertake the ALP determination in the peculiar circumstances as are instantly obtaining. In such a case, we are left with no option but to set aside the impugned order and remit the matter to the file of the AO/TPO for re-determining the ALP of the SDT afresh as per law after affording opportunity of hearing to the assessee. We order accordingly. It is made patent that in the fresh determination, it would be open to the TPO to choose any of the prescribed methods as the most appropriate method to be applied in the prevailing circumstances for re-determining the ALP. It is hereby clarified that we have not totally ruled out the application of the CUP under rule 10B(1)(a) or other method under rule 10AB or the TNMM under rule 10B(1)(e)

but rejected the application - of the CUP method only because the assessee wrongly applied it by choosing functionally different companies and that too from foreign jurisdictions; of 'any other method' because the TPO wrongly held that no services were availed and the assessee also wrongly contented for accepting the transaction at ALP only on the strength of 'reasonableness' of expenditure as per the mandate of section 40A(2) of the Act; and of the TNMM because of the aggregation approach adopted by the assessee. To put it simply, such three methods, *inter alia*, are also open before the TPO in the fresh proceedings to choose from provided the flaws in their application, as discussed above, are removed and they are correctly applied as per their respective prescriptions. Needless to say, the assessee will be at liberty to lead any fresh evidence in support of its case in such fresh proceedings.

10. In the result, the appeal is allowed for statistical purposes.

Order pronounced in the Open Court on 31st May, 2021.

Sd/-
(S.S. VISWANETHRA RAVI)
JUDICIAL MEMBER

Sd/-
(R.S.SYAL)
VICE PRESIDENT

पुणे Pune; दिनांक Dated : 31st May, 2021
GCVSR

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

1. अपीलार्थी / The Appellant;
2. प्रत्यर्थी / The Respondent;
3. The DRP-3, Mumbai
4. The CIT (IT/TP), Pune
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, पुणे
“सी” / DR ‘C’, ITAT, Pune
6. गार्ड फाईल / Guard file

आदेशानुसार/ BY ORDER,**// True Copy //**

Senior Private Secretary
आयकर अपीलीय अधिकरण ,पुणे / ITAT, Pune

		Date	
1.	Draft dictated on	27-05-2021	Sr.PS
2.	Draft placed before author	31-05-2021	Sr.PS
3.	Draft proposed & placed before the second member		JM
4.	Draft discussed/approved by Second Member.		JM
5.	Approved Draft comes to the Sr.PS/PS		Sr.PS
6.	Kept for pronouncement on		Sr.PS
7.	Date of uploading order		Sr.PS
8.	File sent to the Bench Clerk		Sr.PS
9.	Date on which file goes to the Head Clerk		
10.	Date on which file goes to the A.R.		
11.	Date of dispatch of Order.		

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