

IN THE HIGH COURT OF KARNATAKA, BENGALURU

DATED THIS THE 06th DAY OF AUGUST 2018

PRESENT

THE HON'BLE Dr.JUSTICE VINEET KOTHARI

AND

THE HON'BLE Mrs.JUSTICE S.SUJATHA

I.T.A.No.58/2017

BETWEEN:

M/S. TOYOTA KIRLOSKAR MOTOR (P) LTD.
A LIMITED COMPANY REGISTERED
UNDER THE PROVISIONS OF COMPANIES
ACT, 1956, HAVING ITS OFFICE AT
PLOT No.1, BIDADI IND. AREA,
RAMNAGARA DISTRICT, KARNATAKA-562109
REPRESENTED HEREIN BY ITS
AUTHORISED SIGNATORY
PAN: AAAC5415B.

...APPELLANT

(By Mr. S.S. NAGANAND, SR. COUNSEL A/W
Mr. U.R. VIKRAM, ADV.)

AND:

1. THE COMMISSIONER OF INCOME TAX
LTU, JSS TOWERS, BSK III STAGE
BANGALORE-560095.
2. THE ASSISTANT COMMISSIONER OF INCOME TAX
LTU, JSS TOWERS, BKS III STAGE
BANGALORE-560085.

...RESPONDENTS

(By Mr. K.V. ARAVIND, ADV.)

THIS I.T.A. IS FILED UNDER SECTION 260-A OF THE IT
ACT, PRAYING TO FORMULATE THE SUBSTANTIAL QUESTION
OF LAW. SET ASIDE THE ORDER DATED 14/08/2014 IN
IT(TP)A No.1595/BANG/2012 PASSED BY THE ITAT (ANNEXURE-

E) INSOFAR AS IT REMITS THE MATTER TO THE AO/TPO, AND
ALLOW THE SAID APPEAL & ETC.

THIS I.T.A. COMING ON FOR HEARING THIS DAY,
Dr. VINEET KOTHARI J. DELIVERED THE FOLLOWING:-

JUDGMENT

Mr. S.S. Naganand, Sr. Counsel, A/W
Mr. U.R. Vikram, Adv. for Appellant- **Assessee**
Mr. K.V. Aravind, Adv. for Respondents - **Revenue**

1. This appeal has been filed by the Appellant-Assessee - M/s.Toyota Kirloskar Motor Pvt. Ltd., **u/s.260A** of the Income Tax Act, 1961, raising purportedly certain substantial questions of law arising from the order of the **ITAT, Bangalore Bench 'A', Bangalore**, dated **14.08.2014** passed in **IT(TP)A No.1595 (Bang) 2012** for **A.Y.2008-09**.

2. The Assessee is aggrieved only by the directions of the learned Tribunal for remanding the case back to the TPO/AO for undertaking the Transfer Pricing Analysis with regard to Royalty payments made by the Assessee-Indian company to its Associated Enterprise **M/s.Toyota Motors Corporation, Japan** and other

associated companies. The relevant portion of the learned Tribunal remanding the case back to the TPO/AO is quoted below for ready reference:-

*“ The total revenue if both segments are considered together would come to Rs.4 843.97 Crores and operating profit 202.15 Crores. Profit on sales which is the PLI adopted, would be 4.878%. Learned TPO, himself at Annexure-A of his order has given a finding that arithmetic mean of the PLI of the comparables considered by him for manufacturing segment after adjustment was 7.73% At Annexure-F, he has given a finding that PLI of the trading segment of the comparables was 6.42%. Learned TPO has also given a finding that both these were within the +/- 5% range allowable under the Act. **It is also not disputed that while computing the manufacturing segment results the TPO himself had accepted royalty as a part of cost.** This is clear from the segmental result given by the TPO at para-3 of his order which is not reproduced here for brevity. Going by the methodology adopted by the learned TPO, the combined results as mentioned by us above, gave the assessee a PLI of 4.878% for international transactions. **In such a scenario, considering the argument***

of learned DR, that ALP of the royalty payments though not 'nil' had a value which required to be properly fixed, a fresh look by the TPO/AO is required. AO/TPO has to see whether in a case where there is no ALP adjustment required for manufacturing/trading segment or combining both of them, a separate consideration of 'Royalty' for ALP adjustments is required and if so what could be the ALP assigned for it and the result thereof. Order of the AO with regard to ALP adjustment on Royalty is set aside and matter remitted back to him for fresh consideration as per law. Needless to say he can obtain required reports from the TPO for this purpose. Ground 7.8 to 7.12 of the assessee are treated as allowed for statistical purposes".

3. The need to remand the matter back to the TPO/AO arose in view of the fact that for the earlier Assessment Year, the TPO had originally made the Transfer Pricing Analysis separately for manufacturing segment and trading segment of the Assessee, but the Tribunal vide para-11 of the same order took a view that

on a comprehensive view of the matter, since the trading activity was integrally connected with the manufacturing activity of the Assessee-company, trading the spare parts also to be imported from out of India from its Associated Enterprise, instead of taking separate T.P. Analysis for two different segments of the company, the '**Combined Transaction Approach**' was more appropriate to be adopted. The said reasons as discussed by the learned Tribunal are also quoted below for ready reference for giving background, in which, the aforesaid remand directions become necessary.

*“ 11. We have perused the orders and heard the rival contentions. There is no dispute that in the impugned assessment year, the TPO had not disturbed the values of the international transactions with regard to the trading segment and manufacturing segment. After making his own analysis TPO came to the conclusion that the segmental results were within the +/- 5% of the mean arithmetical margin of comparables. Only adjustment that he carried out was **with respect to royalty payments** effected by the assessee.*

*In the first place what we find is that the Coordinate Bench of this Tribunal in its decision in assessee's own case for the assessment year 2007-08 referred supra, had clearly held that **segmented approach was not warranted in assessee's case, since the trading and manufacturing transactions undertaken by the assessee were so interlinked and interconnected, requiring it to be evaluated together.** We find that there was no change in the business model of the assessee for the impugned assessment year. Hence, the order of the Tribunal for assessment year **2007-08** would be very relevant portion. Paras.41 to 47 of the order of the Tribunal is re-produced here under;*

*“ 2. We have given a very careful consideration to the rival submissions. On the issue as to whether the international transactions have to be **considered separately or independently without aggregating them** as part of the segment to which they relate, we find that the term **‘international transaction’** has been defined in section 92B of the Act to mean and include transactions between two or more AEs, either or both of whom are nonresidents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money or any other transaction having bearing on the profits, income, losses or assets of such*

enterprise. Section 92 of the Act provides that income from international transactions between AEs shall be computed having regard to ALP. Section 92-C of the Act prescribes the methods of determining ALP, having regard to the most appropriate method which will be decided in accordance with the rules prescribed. Rule 10A(d) of the Income-tax Rules 1962 [‘the Rules’] provides that ‘transaction’ **would include a number of closely linked transactions.** Rule 10B(1)(d) of the Rules advocate profit split method of determining ALP where international transactions involve transfer of unique intangible or in multiple international transactions which are so inter-related that they cannot be evaluated separately for the purpose of determining ALP of any one transaction. It thus appears that the Act and the Rules contemplate determining ALP by aggregating international transactions which are multiple, interlinked or inter-related to each other and cannot be evaluated separately. To this extent the conclusions of the TPO regarding determination of ALP by taking segmental results without looking into as to **whether the two segments are interlinked or inter-related cannot be sustained.** As to what would be the most appropriate method in such cases is again dependent on Rules 10B(2) and (3) of the Rules.

2. The OECD guidelines as well as the Australian Tax Officer (ATO) Taxation Rule 97/20 on International Transfer Pricing para.2.74(1)

referred to by the assessee before the Revenue authorities which have been set out in the earlier part of this order seems to support '**combined transaction approach**' where the transactions are closely linked or continuous that they cannot be evaluated adequately on an individual basis. In such a situation, rather than assessing the ALP of the transactions individually, the transactions could be evaluated together using the most appropriate method.

43. The above being the legal position, it becomes necessary to examine the international transactions carried out by the assessee with its AE during the previous year which have been categorized into 2 segments by the TPO in his order and find out if they are interlinked or interconnected so that the transactions need to be evaluated together rather than individually. In this regard, **we find that the submissions made by the Assessee before TPO as well as before DRP have not been considered at all.** The TPO proceeded on the basis that **ALP of each transaction has to be examined independently/individually by placing reliance on the decisions of Tribunal in the case of Star India Ltd. (supra) and UKB(I) (P) Ltd. (supra).** We agree with the submissions of

*the learned counsel for the assessee that these decisions have in fact accepted in principle that aggregation of **transactions have to be done where they are interlinked but have on facts found that transactions were not interlinked and therefore held that ALP of transactions have to be determined individually.** The following decisions relied upon the learned counsel for the assessee also supports the plea of the learned counsel for the assessee. :*

i. M/s. Thyssen Krupp Industries vs. ACIT (ITA No.7032/Mum/2011),

ii. Hindustan Unilever Ltd. vs. ACIT (ITA No.7868/Mum/2010), and

iii. DCIT vs. CMA CGM Global India (P) Ltd. (ITA No.5979/Mum/2010)

*44. The DRP without examining the submissions on behalf of the assessee has simply endorsed the findings of the TPO. With regard to the conclusions of the DRP, upholding the order of the TPO that the trading and manufacturing segment of the assessee are distinct and not inter-related warranting combined transaction approach, the ld. counsel for the assessee drew our attention to the order of the Tribunal in assessee's own case for **A.Y. 2003-04** in ITA No.828/B/2010, wherein identical issue was*

considered and decided by this Tribunal as follows:-

*"14.5.2 Taking into consideration the submissions made and the facts and circumstances of the case, we agree with the submissions of the learned counsel for the assessee. While it is true that function, assets and risks of the trading and manufacturing segments generally differ, however circumstances may warrant combining both of them. It is only in the specific facts of the case that the combining of both segments is advisable. In the instant case of the assessee, the sale of spare parts is triggered as a result of the manufacturing activities, including warranty commitments. Therefore, we are of the view that it would not be in the **fitness of things for the sale of spare parts and components to be considered in isolation from the sale of manufactured vehicles. This view is supported by the OECD T.P. Guidelines, 2010, relied on by the assessee. This view is also buttressed by the fact that the comparable companies are also trading in spare***

parts and components. On a overall consideration, it can be concluded that trading in spare parts is closely inter-linked with the manufacturing segment of the assessee. We are of the view that no meaningful purpose would be served in segregating the trading and manufacturing segments, particularly when the assessee and the comparable companies are at par with regard to the nature and scale of combined activities. Needless to add that this finding / decision by its very nature has to be case-specific and year-specific as the decision is based on the facts and circumstances of this particular case and of this particular year and is not to be construed as laying down the principle in this regard. We, therefore, direct the Assessing Officer / TPO to compute the ALP at the entity / enterprise level by combining the trading and manufacturing segments."

*45. It is no doubt true that the Tribunal has observed that the ruling given in that year is based on the facts that prevailed in that year. We find that the facts in the present **assessment***

year are also identical and there has been no change whatsoever in the business model of the assessee. In these circumstances, we are of the view that the decision rendered by the Tribunal would be applicable for **this assessment year also.** Respectfully following the decision of the Tribunal, we hold that the trading and manufacturing segment of the assessee are not distinct and are inter-related warranting combined transaction approach.

46. We have already seen in para 9 of this order that the TPO has arrived at the bifurcation of the manufacturing and trading segmental operating results. In view of our conclusions that the trading and manufacturing segments are interlinked and therefore a combined transaction approach has to be adopted, we combine the results so arrived at by the TPO, which is given in para 9 of this order. If the segmental results are combined, the operating revenue of the assessee would be 3767.91 crores and the operating profit would be Rs.94.34 crores. Thus, the operating profit margin on sales would be 2.517.

47. Even assuming that the adjustment on account of operational efficiency made by the TPO is to be accepted, then the combined margin after

adjustment of the five comparables which is given in para-20 of this order, would be 7.10%. If the arithmetic mean of the five comparables as above is tested as against the operating profit margin on sales of the assessee at 2.517%, then the same would be within the (+)/(-) 5% range of the arithmetic mean and therefore no addition by way of adjustment to the ALP can be made. In this view of the matter, we are of the view that the addition sustained by the DRP deserves to be deleted and is hereby deleted. Gr.No.12 is accordingly allowed”.

4. The contention raised by the learned senior counsel for the Appellant-Assessee Mr.S.S.Naganand before us is that remand in these circumstances is only an academic because for the previous assessment years, the Tribunal's findings in this regard have already been upheld by this Court while dismissing the Revenue's appeals filed before this Court in **ITA No.172/2013** (*The Commissioner of Income Tax & Anr. Vs. M/s.Toyota Kirloskar Motors Pvt. Ltd.*,) for A.Y. **2003-04** and **ITA No.525/2014 for A.Y.2007-08.**

He also relied upon the decision of this Court in the case of **Ganapathi Subraya Bhat vs. Land Tribunal, Honnavar (2002(4) KCCR 2328)**, in which, the case under Karnataka Land Reforms Act, 1961, the co-ordinate Bench of this Court hold that the remand to the Land Tribunal in the facts and circumstances of the case would only be an academic and therefore, was not required to be made.

5. Learned counsel for the Respondent-Revenue supported the impugned order of the learned Tribunal before us.

6. Having heard the learned counsels, we are of the opinion that no substantial question of law arises out of the said order with remand directions of the learned Tribunal. The exercise of Transfer Pricing Analysis on the **‘Combined Transaction Approach’** and not on different segment basis, deserves to be undertaken and in our opinion, the learned Tribunal

was justified in remanding the case back to the TPO/AO for undertaking such Transfer Pricing Analysis for determining the ALP of the Royalty payments made by the Assessee-Indian company to the Associated Enterprises of Japan.

7. The factual exercise of determination of ALP, whether it results in any T.P. adjustments or not, is not an issue before us at this stage. It is for the authority concerned to look into these facts and figures by undertaking the requisite exercise of T.P. Analysis on the basis of comparables selected by the authorities in accordance with the parameters available with them.

8. We also do not find the aforesaid judgment of this Court in **Ganapathi Subraya Bhat (supra)** relied upon by the learned senior counsel is of any help to the Assessee, as the facts and context in which the co-ordinate Bench of this Court found that the remand was not justified are not available in the present set of facts.

9. We do not feel here that this remand direction would entirely an academic exercise only and TPO/AO should be allowed to undertake this exercise in the present case and therefore, we are not inclined to interfere with the findings of the learned Tribunal in any manner and no substantial question of law arises out of the said order of the learned Tribunal requiring our consideration for further interference in the present appeal.

10. The appeal filed by the Assessee is accordingly dismissed. No costs.

**Sd/-
JUDGE**

**Sd/-
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