

itxa-1540-2015

IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO. 1540 OF 2014

The Commissioner of Income Tax-8 .. Appellant.
v/s.
Petro Araldite Pvt. Ltd., .. Respondent.

Mr. Anil Singh, ASG with Mr. Arvind Pinto, for the Appellant.
Mr. Nitesh Joshi i/b. Mr. A. K. Jasani, for the Respondent.

**CORAM: M.S.SANKLECHA &
SANDEEP K. SHINDE,JJ.**
DATE : 26th APRIL, 2018.

P.C:-

This Appeal under Section 260-A of the Income Tax Act, 1961 (the Act), challenges the order dated 24th July, 2013 passed by the Income Tax Appellate Tribunal (the Tribunal). The impugned order dated 24th July, 2013 is in respect of Assessment Year 2005-06.

2 Revenue urges the following reframed questions of law, for our consideration:

“(a) Whether on the facts and in the circumstance of the case and in law, the Tribunal was correct in holding that profit margin of the comparable should be applied only to the value of the International Transactions entered into Associated Enterprises to determine the Arms Length Price and not at entity level?

(b) Whether on the facts and circumstances of the case and

in law, the Tribunal is justified in directing the Assessing Officer to take into consideration the adjustment of capacity utilization factor even though it is not prescribed in Section 92CA of the Income Tax Act, 1961 read with Rules 10AB, 10B, 10C of the Income Tax Rules, 1962?

(c) Whether on the facts and circumstances of the case and in law, the Tribunal was justified in not appreciating that the Assessing Officer had correctly computed the deduction year-wise as per clause (iii) of Explanation 1 to section 115JB of the Act?”

3 Re. Question (a):-

- (i) The learned Counsel appearing for the Revenue very fairly states that the issue arising herein stands concluded against the Revenue and in favour of the Respondent-Assessee by the decision of this Court in *CIT v/s. Petro Araldite Pvt. Ltd.*, (Income Tax Appeal No. 1804 of 2013) decided on 24th November, 2015.
- (ii) Moreover, it is also accepted by the Revenue that so far as this Court is concerned, this issue stands concluded against the Revenue by the following decisions of this Court;
 - (a) CIT v/s. Ratilal Becharlal & Sons (Income Tax Appeal No.1906 of 2013), decided on 24th November, 2015;
 - (b) CIT v/s. Goldstar Jewellery Design (P) Ltd. (Income Tax Appeal No.2237 of 2013) decided on 4th February, 2016; and
 - (c) CIT v/s. Alstom Projects India Ltd., (Income Tax Appeal No.362 of 2014) decided on 14th September, 2016.
- (iii) In the above view, question as proposed does not give rise to any substantial question of law. Thus not entertained.

4 **Re. Question (b):-**

(i) The impugned order of the Tribunal for purposes of arriving at the profit margin of comparable uncontrolled transactions to enable determination of the Arms Length Price (ALP) of the Respondent-Assessee's transactions with its Associated Enterprises, had invoked Rule 10-B(1) (e) (iii) of the Income Tax Rules, 1962 (the Rules). Thus, taking into account the capacity utilization as factor which could affect the extent of the profit margin of the comparable for the purposes of determining the ALP of the Respondent-Assessee's transactions.

(ii) The impugned order of the Tribunal reproduced Rule 10-B (1) (e) (iii) of the Rules, which reads as under:-

“(e) transactional net margin method, by which,-

(i) the net profit margin realised by the enterprise from an international transaction entered into with an associated enterprise is computed in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise or having regard to any other relevant base;

(ii) the net profit margin realised by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction or a number of such transactions is computed having regard to the same base;

(iii) the net profit margin referred to in sub-clause (ii) arising in comparable uncontrolled transactions is adjusted to take into account the difference, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of net profit margin in the open market;

(iv) the net profit margin realised by the enterprise and referred to in sub-clause (i) is established to be the same as the net profit margin referred to in sub-clause (iii);

(v) the net profit margin thus established is then taken into account to arrive at an arm's length price in relation to the international transaction”.

- (iii) The impugned order of the Tribunal records that the difference in capacity utilization would affect the profit margin of a manufacturing concern. It points out that the fixed overheads of any manufacturing concern will be constant, irrespective of the capacity utilization. Thus, the profit margin would be affected on account of the difference in capacity utilization. Less utilization of capacity, would result in allocation fixed costs over a smaller number of final products. Thus, reducing the profit margin. The impugned order of the Tribunal with the aid of illustration, points out that higher capacity utilization would lead to higher profitability as fixed costs would be spread over in a larger number of units manufactured. It was in the above context, that the impugned order of the Tribunal held that difference in capacity utilization would materially affect the profit margin. Thus, if there is a difference in the level of capacity utilization of the assessee and the level of capacity utilization of the comparable, then adjustment would be required to be made to the profit margin of the comparable on account of difference in capacity utilization in terms of Rule 10-B (1) (e)(iii) of the Rules.
- (iv) Revenue is not disputing before us that capacity utilization of a comparables manufacturing unit would impact the net profit margin of the comparable.
- (v) In the above view, taking into account the capacity utilization of

the comparable, in the present facts, as it materially affects the profit margin, the invocation of Rule 10-B (1) (e)(iii) of the Rules, cannot be found fault with This is self evident position from the reading of the aforesaid provision that all aspects/ difference between the international transactions and the comparable uncontrolled transactions which materially affects the net profit margin had to be taken into account so as to have the fair comparison while determining the ALP of the tested party's transaction.

- (vi) Therefore, this question does not give rise to any substantial question of law as Rule 10-B (1)(e)(iii) of the Rule is self evident. Thus, not entertained.

5 **Re. Question (c):-**

Appeal admitted on the substantial question of law at (c).

6 Registry is directed to communicate copy of this order to the Tribunal. This would enable the Tribunal to keep papers and proceedings relating to the present appeal available, to be produced when sought for by the Court.

Mr. Joshi, learned Counsel waives service for the Respondent.

(SANDEEP K. SHINDE,J.)

(M.S.SANKLECHA,J.)