

* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Decided on: 22.11.2017

+ **ITA 484/2017**

PR. COMMISSIONER OF INCOME TAX-6 Appellant

Through: Mr. Rahul Chaudhary Sr. Standing Counsel and
Mr. Sanjay Kumar, Jr. Standing Counsel.

versus

MATRIX CELLULAR INTERNATIONAL SERVICES PVT. LTD.
.... Respondent

Through: Mr. Himanshu Sinha with Ms. Vrinda Tulshan,
Advocates.

CORAM:
HON'BLE MR. JUSTICE S. RAVINDRA BHAT
HON'BLE MR. JUSTICE SANJEEV SACHDEVA

S. RAVINDRA BHAT, J (ORAL)

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1. These appeals by the Revenue, under Section 260A of the Income Tax Act, 1961 (hereinafter referred to as '*the Act*'), impugn the order of the Income Tax Appellate Tribunal, Delhi Bench ("ITAT"), dated 17.10.2016, for the assessment year (AY) 2009-10. The ITAT allowed the assessee's appeal. The Revenue, in this appeal, urged three questions. By order dated 04.08.2017, this Court declined to frame questions on the issue of disallowance under Section 14A, as well as the issue of advertisement expenditures. The Court issued notice only on the issue of transfer pricing.

2. The facts necessary are that the assessee, is a private company engaged in the business of sale of airtime, renting out of handsets and SIM cards. It filed its return of income on 26.09.2009 declaring loss of ₹15,67,73,021/-. Its case

was selected for scrutiny and notice under section 143(2)/142(1) was issued to it. The assessing officer (AO) noticed that during the relevant financial year the assessee had undertaken international transactions with its associated enterprises (AE) and therefore, referred the case to the Transfer Pricing Officer under (TPO) Section 92CA(1) of the Act for determination of the arm's length price for the international transactions undertaken by the assessee during the financial year 2008-09. The TPO accepted the Transaction Net Margin Method ("TNMM") adopted by the assessee, as the Most Appropriate Method (MAM) for benchmarking international transactions with the AE. However, the TPO rejected the claim for adjustments on account of unutilized capacity in terms of (a) human resources expenses (b) operating/administrative expenses (c) extraordinary expenses in terms of advertisement and publicity as claimed by the assessee. After considering the TPO's report, the AO passed a draft assessment order dated 22.03.2013, whereby an adjustment of ₹6,26,21,285 was made on account of the transfer pricing order, along with disallowance of advertisement and publicity expenses, and disallowance under section 14A of the Act.

3. Aggrieved by the draft assessment order, the assessee filed objections before the Dispute Resolution Panel (DRP). The DRP however, rejected the assessee's claims. On 20.02.2014 the AO made the assessment order under section 143(3) read with section 144C of the Act in terms of the directions issued by the DRP. The order made transfer pricing adjustment of ₹3,92,90,855, together with disallowance of publicity and advertisement expenses, and disallowance under section 14A of the Act. Aggrieved, the assessee carried the matter in appeal to the ITAT.

4. The ITAT, by order dated 17.10.2016 allowed the appeal of the assessee and deleted all the additions/disallowances made in the assessment order.

5. The Revenue's grievance is that the learned ITAT erred in adopting the Resale Price Method (RPM) as the Most Appropriate Method under Section

92C of the Act. It is urged by the revenue that the assessee in its transfer pricing report furnished before the TPO had adopted the Transactional Net Margin Method (TNMM). Given that the assessee considered TNMM as the Most Appropriate Method for determining the arms' length price for its transactions, and the TPO, as well as AO and the DRP adopted the same, it was not open to the ITAT to reject the TNMM and adopt the RPM as the Most Appropriate Method.

6. On the other hand, the assessee's counsel contends that there is no infirmity with the approach or the order of the ITAT. It is urged that even in the transfer pricing study report furnished by the assessee before the Transfer Pricing Officer, to justify its losses at the net level, RPM was used as a secondary method. In any case, since the ITAT concluded that the assessee's business was purely of trading, without any value addition to the goods, its finding that the RPM method was applicable was irreproachable.

7. The dispute before the Court is whether the ITAT erred in adopting the RPM in order to determine the arms' length price in relation to the assessee's business. In the relevant assessment year, the assessee had four AEs. Three of them were wholly owned subsidiaries, whereas in the fourth, the assessee held 49% shareholding. The ITAT found that the AEs were engaged in the business of identifying, negotiating and buying SIM cards from the networks of different countries and selling them to the assessee. This arrangement, according to the assessee, foreign networks were reluctant to deal with foreign companies. The ITAT, relying on the TPO's order, found that the business of the assessee only involved re-selling or distributing the SIM cards imported from the AEs, without making any value addition. The ITAT also found that there was no distinction between airtime and SIM cards, as no value could be added to the airtime resold by the assessee. Since the SIM cards are resold without making any value addition, the ITAT concluded that the assessee carried out purely

trading business, and hence the RPM was the Most Appropriate Method for calculating arms' length price.

8. This Court finds that once the ITAT, on considering the relevant facts as well as the order of the TPO, had concluded that the business of the assessee was merely that of a pure trader, and there was no value addition made before re-selling the particular products (i.e. the SIM cards), its consequent finding that RPM is the Most Appropriate Method, is irreproachable. In *Nokia India (P) Ltd. v. Deputy Commissioner of Income Tax*, (2015) 167 TTJ (Del) 243, the Delhi bench of the ITAT held:

“A close scrutiny of the above two sub-clauses along with the remaining sub-clauses of r. 10B(1)(b) makes it clear beyond doubt that RPM is best suited for determining ALP of an international transaction in the nature of purchase of goods from an AE which are resold as such to unrelated parties. Ordinarily, this method presupposes no or insignificant value addition to the goods purchased from foreign AE. In a case the goods so purchased are used either as raw material for manufacturing finished products or are further subjected to processing before resale, then RPM cannot be characterized as a proper method for benchmarking the international transaction of purchase of goods by the Indian enterprise from the foreign AE.”

9. Similarly, in *Swarovski India Pvt. Ltd. v. ACIT*, ITA No. 5621/Del/2014, the ITAT held:

“Adverting to the facts of the instant case, we find that the assessee purchased Crystal goods and Crystal components from its AE. No value addition was made to such imports. The goods were sold as such. In the given circumstances, the RPM is the most appropriate method for determining the ALP of the international transaction of Import of Crystal goods and Crystal components.”

10. A similar view has been adopted by the Mumbai bench of the ITAT in *Mattel Toys v. Deputy Commissioner of Income Tax*, (2013) 158 TTJ (Mum)

461:

“Thus, the RPM method identifies the price at which the product purchased from the A.E. is resold to a unrelated party. Such price is reduced by normal gross profit margin i.e., the gross profit margin accruing in a comparable controlled transaction on resale of same or similar property or services. The RPM is mostly applied in a situation in which the reseller purchases tangible property or obtain services from an A.E. and reseller does not physically alter the tangible goods and services or use any intangible assets to add substantial value to the property or services i.e., resale is made without any value addition having been made.”

11. This view has also been affirmed by the Bombay High Court in its judgment dated 07.11.2014 in *Commissioner of Income Tax v. L'Oreal India Pvt. Ltd.* (ITA No. 1046 of 2012), where the Court found that there was no error in law committed by the ITAT when it held that RPM was the Most Appropriate Method in case of distribution or marketing activities especially when goods are purchased from associated entities and there are sales effected to unrelated parties without any further processing. In fact, a Division Bench of this Court in its decision in *Bausch & Lomb Eyecare (India) Pvt. Ltd. v. Additional Commissioner of Income Tax*, (2016) 381 ITR 227 (Del), while considering the decision of this Court in *Sony Ericsson Mobile Communications India Pvt. Ltd. v. Commissioner of Income Tax*, (2015) 374 ITR 118 (Del), noted that:

“The RP Method loses its accuracy and reliability where the reseller adds substantially to the value of the product or the goods are further processed or incorporated into a more sophisticated product or when the product/service is transformed.”

12. Therefore, *a contrario*, when the reseller does not add any value to the product of the goods, the RP method would be appropriate for determining the arms' length price.

13. Accordingly, we find that the ITAT committed no error in law in applying RPM as the Most Appropriate Method for computing the arms' length price. The Revenue's grievance is that the ITAT could not have applied RPM as the Most Appropriate Method, given that the assessee had itself, in its transfer pricing study report, and before the DRP, adopted the TNMM as the Most Appropriate Method to benchmark the international transactions it had undertaken, and only adopted the RPM as a secondary method to justify its losses at the net level. The ITAT relied upon the decision of *Luxottica India Eyewear Pvt. Ltd. v. DCIT*, ITA No. 617/Del/2015 decided on 05.11.2014, where the Tribunal held:

"Coming to the argument that the assessee himself has adopted TNMM as the MAM for its transfer pricing study and hence it can not turn around and argue for adoption of RSPM as the MAM, we find that the Mumbai Bench of the Tribunal in the case of Mattel Toys (I) Pvt. Ltd. in I.T.A. No. 2476/Mum/2008 held as follows.

"41. Now coming to the argument of the Ld. DR that once the assessee itself has chosen TNMM as the MAM in TPR, then it cannot resort to change its method at an assessment or appellate stage. In our opinion, such a contention cannot be upheld because if it is found on the facts of the case that a particular method will not result into proper determination of the ALP, the TPO or the appellate authorities can very well hold that why a particular method can be applied for getting proper determination of ALP or the assessee can demonstrate a particular method to justify its ALP. Thus, even if the assessee had adopted TNMM as the MAM in the TP report, then also it is not precluded from raising the contentions/objections before the TPO or the appellate Courts that such a method was not an appropriate method and is not resulting into proper determination of ALP and some other method should be resorted. The ultimate aim of the TP is to examine whether the price or the margin raising from an international transaction with the related party is at ALP or not. The determination of approximate ALP is the key factor for which the MAM is to be followed. Therefore, if at any stage of the proceedings, it is found that by adopting one of the prescribed

methods other than chosen earlier, the most appropriate ALP can be determined, the assessment authorities as well as the appellate Courts should take into consideration such a plea before them provided, it is demonstrated as to how a change in the method will produce better or more appropriate ALP on the facts of the case. Accordingly, we reject the contentions of the Ld. DR and also the observations of the AO and the Ld. CIT(A) that the assessee cannot resort to adoption of RPM method instead of TNMM.”

14. The ITAT in this case, accordingly held that even though the assessee had in its transfer pricing report, relied on TNMM as the Most Appropriate Method, that *ipso facto*, cannot preclude the transfer pricing officer or the appellate authorities from adopting a different method for calculating the arms' length price, if that is found to be the Most Appropriate Method.

15. This Court finds that the ITAT's reasoning on this issue is without flaw. The ITAT's reasoning, relying on the decision in *Luxottica (supra)*, that since the ultimate aim of the transfer pricing exercise is to determine an accurate value of the arms' length price for the purpose of taxation/and therefore the appellate authorities would not be barred from adopting a different method, from that adopted by the assessee in the transfer pricing report, if the latter is not found to be the Most Appropriate Method. Accordingly, this Court does not discern any illegality in the ITAT's approach in determining that RPM was, in the given circumstances, and having regard to the business of the assessee, the Most Appropriate Method for determining the arms' length price. The mere fact that the assessee had relied on TNMM and had only used RPM as a secondary method in its transfer pricing report, would not in any way preclude the ITAT from adopting the RPM as the Most Appropriate Method under Section 92C of the Act, if it so finds in the circumstances of the case. *Kedarnath Jute Manufacturing Co. Ltd. v. Commercial Tax Officer*, AIR 1966 SC 12 is an authority for the proposition that tax authorities and adjudicators as well as assesseees are not precluded by the positions taken in returns, documents

or accounts and have the duty (and a corresponding right) to apply the correct legal principle. Thus, the use of one method in a transfer pricing report does not estop the assessee from later claiming that another method is the most appropriate one, provided that is indeed the correct position.

16. For the above reasons, we are of the opinion that no substantial question of law arises. The appeal is accordingly dismissed.

**S. RAVINDRA BHAT
(JUDGE)**

**SANJEEV SACHDEVA
(JUDGE)**

NOVEMBER 22, 2017