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

[Coram: I C Sudhir JM and Pramod Kumar AM]

I.T.A. Nos.: 5648, 5649 and 5650/Del/12
Assessment years 2003-04, 04-05, 05-06

Wrigley India Pvt Ltd ***……………….Appellant***
206, Okhla Industrial Estate Phase III
New Delhi 110 020 [PAN: AAACW1789P]

Vs.

Assistant Commissioner of Income Tax
Circle 18(1), New Delhi ***……………Respondent***

I.T.A. Nos.: 5987, 5988 and 5989/Del/12
Assessment years 2003-04, 04-05, 05-06

Assistant Commissioner of Income Tax
Circle 18(1), New Delhi ***……………….Appellant***

Vs.

Wrigley India Pvt Ltd ***……………Respondent***
206, Okhla Industrial Estate Phase III
New Delhi 110 020 [PAN: AAACW1789P]

I.T.A. No. 5224/Del/10
Assessment years 06-07

Wrigley India Pvt Ltd ***……………….Appellant***
206, Okhla Industrial Estate Phase III
New Delhi 110 020 [PAN: AAACW1789P]

Vs.

Additional Commissioner of Income Tax
Range 18 New Delhi ***……………Respondent***

Appearances by:

KanchanKaushal, *alongwith* Ravi Sharma and Sankalp Sharma**,** *for the appellant*
Peeyush Jain *for the respondent*

Date of the hearing : November 24, 2014.
Date of pronouncing the order : December 31, 2014.

O R D E R

Per Pramod Kumar AM:

1. Out of these seven appeals, first six appeals are cross appeals, filed by the assessee as also the Assessing Officer, against a consolidated order dated 11th September 2012 passed by the CIT(A) in the matter of assessment under section 143(3) of the Income Tax Act, 1961 *[hereinafter referred to as 'the Act']*, for the assessment years 2003-04, 04-05 and 05-06. The seventh appeal is assessee's appeal against order dated 29th October 2010 passed by the then Assessing Officer under section 143(3) r.w.s. 144C of the Act, for the assessment year 2006-07. All these appeals pertain to the same assessee, involve some common issues arising out of a common set of facts, and were heard together. As a matter of convenience, therefore, we are disposing of all these appeals togetyher by this consolidated order.

2. One common issue in all the assessment years is the challenge to the correctness of arm's length price adjustment made to the billing for contract manufacturing by the assessee, to its associated enterprises based abroad. We will begin by taking up this common issue. The short question, as learned counsel for the assessee contends, that we have to adjudicate upon in this bunch of appeals is whether Cost Plus Method (CPM), with entrepreneurship profits derived from manufacturing and selling its products in India as the benchmark, would indeed be most appropriate method of determining the arm's length price (ALP)of contract manufacturing of its same products for its associated enterprises abroad. The background in which this question arises is as follows.

3. The assessee company (**Wrigley India**, in short) was set up in India in October 1993 as a wholly owned subsidiary of the legendry William Wrigley Jr Co, USA (**Wrigley USA,** in short) founded in 1891 and is thus part of a large network of business entities associated with Wrigley USA (collectively referred as **Wrigley group**) - world's largest manufacturer and marketers of chewing gum and with its network in more than 180 countries. Wrigley India is engaged in the manufacture and sale of confectionary products like chewing gums, bubble gum lollipops and toffees. The company is manufacturing and selling these products to the associated enterprises (AEs) as also to the independent enterprises (non AEs).The fine line of distinction in respect of these transactions with AEs and non AEs, as canvassed before us, is that while the transactions with the AEs are in the capacity as limited risk contract manufacturer, its transactions with the domestic independent enterprises is a business transaction with regular entrepreneurship risks.

4. The assessee, as we have noted above, started its operations in Indian in the end of the calendar year 1993. The assessee produced and marketed its products in India and since the assessee could not utilize its entire production capacity, the assessee also produced the same products for its AEs abroad. So far as the assessment year 2003-04 is concerned, the transfer pricing study noted that the assessee's operating loss has come down from 76.21% to 39.17% due to reduced capacity underutilization, and that it was so done with the help of exports to AEs abroad. The TP study, *inter alia*, noted as follows:

> **"The losses were on account of lack of demand in the domestic market and substantial underutilization of existing capacity. However, the loss has decreased during the year due to improvement in the capacity utilization.**
>
> **Wrigley India has produced 554 metric tonnes during the financial year ended on March 2003 as against installed capacity of 1951 metric tonnes i.e. a capacity utilization rate of 28 percent. The improvement in the**

capacity utilization as compared to 12 percent is on account of increased demand in the export market.

Breakeven analysis portrays the relationship between the cost of production, volume of production and the sales value. The breakeven point is the level of sales at which the company would neither earn profit nor incur losses. Based on the information made available to us, we understand that the turnover achieved by Wrigley India for the current financial year is still below the breakeven point.

Particulars	***Quantity (In MT)***	***Rs in millions***	***As % of sales***
Sales	542	127.54	100.00%
less: variable costs		85.53	67.06%
Contribution		42.01	32.94%
less : fixed costs		91.97	72.11%
Net Profit		(45.34)	(-) 39.17%
P/V Ratio			32.94%
BEP Sales [Fixed cost/ PV ratio]			218.91%

Other things being equal, Wrigley India will need to achieve minimum capacity utilization of about 60% (of the present installed capacity) to achieve breakeven.

5. In the course of dealing with determination of arm's length price in respect of these transactions, the transfer pricing study noted that CUP method cannot be applied to the facts of this case as **"Wrigley India does not export such products to any unrelated party outside India**" and **"even though Wrigley India sells chewing gums to unrelated parties in India, the terms and risk profile for such transactions differ significantly"** from that of exports to Wrigley group companies". It was also noted that **"there is no**

publicly available information on prices charged in independent transactions of similar or identical nature which reflect characteristics of the products exported to Wrigley group companies". The use of Resale Price Method was ruled out on the ground that "**the RPM is applicable in a resale situation where the property or service purchased from an associated enterprise is sold to unrelated enterprise**". Even as it was recognized that, "**the cost plus method us ordinarily used in cases involving manufacture, assembly or other production of goods that are sold to related parties or where the controlled transaction is a provision of services**", the TP study rejected the same *inter alia* on the ground that, "**differences in cost accounting practices would materially affect the gross profit mark up and the ability to make reliable adjustments for such differences would affect the reliability of results**". It was also added that the CPM method "**has not been considered, in this case, as the most appropriate method, on account of inconsistency in cost accounting practices between the comparable uncontrolled transaction and controlled transaction**". Ironically, even as the assessee was admittedly following cost plus method of billing to the AEs, the cost plus method was rejected for determination of the arm's length price. Be that as it may, as none of these direct method were found to be most appropriate method for determining the arm's length price and as Profit Split Method (PSM) was also found unsuitable for the reason that neither it was a case of '**transfer of unique intangibles'** nor a situation dealing with '**multiple inter-related transactions which cannot be separated**', the assessee finally resorted to the Transactional Net Margin Method (TNMM), for want of applicability of all other methods of ascertaining the arm's length price, for benchmarking its sales transactions with the AEs. The assessee thus adopted TNMM with operative profit on operating cost (OP/OC) as the profit level indicator. The assessee selected eight comparables, namely Britannia Industries Limited, Cadbury India Limited, Cremica Agro Foods Limited, Parry's Confectionary Limited, Priya Food Products Ltd, SampreNutritions Limited, Ravalgaon Sugar Farm Ltd and Veermani Biscuit Industries Limited. The TP study further noted that since the information for the financial year 2002-03

was not readily available and since the TP regulations permit use of data for up to two years prior to the relevant financial year, the financial information for the comparable companies was included for the financial year 2001-02 and 2002-03. The TP study then concluded as follows:

> **Based on our analysis, the potentially comparable companies' operating margins (computed as defined above) lie between (-) 1.37% to 13.17%. The arithmetic mean of the above mentioned range is 6.44%.....**
>
> **Information provided by Wrigley India indicates that the net margin earmarked by Wrigley India on budgeted cost of exports was 10% of costs (excluding SGA***i.e. Sales, General and Administrative Expenses***). Hence, Wrigley India's budgeted net margin of the export transaction is within arm's range computed as defined above, and, therefore can be considered to be at arm's length.**

6. The TP study then, as a corroborative analysis, justified this pricing by pointing out that the realization of export proceeds was in excess of the marginal or incremental costs to the assessee, and, as such, provided a net contribution to the fixed costs which was as high as 36% of sales. A reference was made to the OECD Transfer Pricing Guidelines in support of the contention that while 'margin costing method' is not recognized by the Indian TP regulations, the same may be considered in certain situations as a corroborative to primary analysis.

7. This approach to benchmarking the assessee's transactions with the AEs, however, did not find favour with the Transfer Pricing Officer. He rejected this analysis for the short reason that the TNMM requires comparison of net margin realized by the assessee with the net margin realized by the comparables, and that the comparison of budgeted margins with actual margins of the comparables was not permissible. The TPO adopted Cost Plus Method, with

gross mark up on costs as the profit level indicator, and adopted the internal comparable as gross mark up realized on the domestic sales. In other words, what the TPO held was that the arm's length price products exported to the AEs can be arrived at by adopting the same mark up on costs of such products, as was achieved on the domestic sales. It was noted that the assessee had achieved 41.29% of mark upon costs so far as its domestic sales was concerned, and, accordingly, the arm's length price of the products exported to AEs should also have been cost plus 41.29%. It was on this basis that an ALP adjustment of Rs. 2,71,55,592 was recommended in the TPO's order. Similar ALP adjustment, based on the same reasoning and on materially similar facts- barring the variations in figures, were also required by the TPO's orders for the assessment years 2004-05 and 2005-06.

8. In 2006-07, there were some noticeable deviations in the TP study but conclusions remained the same. The TP study specifically mentioned, as pricing policy, that "**for sale of goods made by the Wrigley India, the company changes on Cost Plus (cost plus 7.5%) basis to the AEs in respect of goods sold to them**" and that "**the costs include direct and indirect costs relating to the manufacture of goods**". It was also noted that "**since the Wrigley Group deals in FMCG sector which is characterized by impulsive buying by the consumers, heavy expenditure is required to be made on planning and execution of sales promotion**" and that "**these expenditure were incurred by the Wrigley Group to penetrate new market as well as to retain share in the existing market**". It was also noted in the TP study that **"in respect of sales promotion, both Wrigley India and the AEs carry out this function in their respective market"**. As for the reasons of rejecting the CPM in determination of ALP, it was stated that, **"Wrigley India does not undertake similar functions and risks in its related and unrelated party transactions"** and, for this reason also, CPM would not be appropriate method for the purpose of determining the ALP. As for the computation of ALP determination in 2006-07, mercifully the TP study abandoned the comparison with budgeted costs and noted that actual margin (OP/TC) of the Wrigley India was 3%, as against 8.07%

in the selected comparables, but then since sales price, as per comparables, was to be 108.07 on a total cost of Rs 100, and since sales price of Rs 103, as achieved by the assessee, was within 5% range (up to Rs 108.07), the price at which goods were exported by the assessee were within permissible range of arm's length price. The same TP approach, though for slightly different reasons, was adopted by the assessee. The TPO, however, following his stand for the earlier two assessment years, rejected this approach as well. Similar adjustments were held appropriate by the TPO for this assessment year as well.

9. It was in this backdrop that the AO made the ALP adjustments with respect to the arm's length price of assessee's export transactions with the AEs. Aggrieved by the adjustments so made by the Assessing Officer, on the basis of the TPO's order, the assessee carried the matter in appeal before the CIT(A) but without any success. Learned CIT(A) passed a common order for the assessment years 2003-04, 2004-05 and 2006-07, and, following the order dated 5th August 2011 in assessee's own case for the assessment year 2006-07, upheld the impugned ALP adjustment. The assessee is not satisfied and is in appeal before us.

10. As for the Tribunal's order in the assessment year 2006-07, which was on direct appeal against the assessment order as the assessee had taken the DRP route, so far as adjudication on ALP adjustment is concerned, it has since been vacated by Hon'ble jurisdictional High Court. While doing so, Their Lordships have, *inter alia*, observed as follows:

> **One of the pleas raised by the appellant is that the Tribunal did not examine the submission of the appellant that in the succeeding years, i.e. 2007-08, 2008-09 and 2009-10, the Transactional Net Margin Method (TNMM) has been accepted by the Transfer Pricing Officer as the most appropriate method, as against the Cost Plus Method which had been adopted in the present year i.e. 2006-07. It is also been submitted by the**

learned counsel that in respect of the assessment years 2004-05 and 2005-06, appeals were pending before the CIT(A) when decision of the DRP as well as the Tribunal in the present case were announced. Subsequently, the CIT(A) has decided the appeals in respect of assessment years 2004-05 and 2005-06 by adopting he Cost Plus method. The appellant has filed appeals in respect of those assessment years which are now pending before the Tribunal. It is contention of the learned counsel that the present matter be remitted to the Tribunal so that all the years could be considered by the Tribunal and a decision could be arrived at as to which is the most appropriate method, namely, whether it is Cost Plus method or whether it is Transactional Net Margin Method……… we feel that since the other assessment years, i.e. assessment years 2004-05 and 2005-06 are to be considered by the Tribunal and appeals in respect thereof are pending before the Tribunal, the present year i.e. 2006-07 should also be reconsidered by the Tribunal so far as transfer pricing issues are concerned…….

11. The very foundation, on which adjudication by the learned CIT(A) rests for the assessment years 2003-4, 2004-05 and 2005-06,ceases to exist. The order of the Tribunal for the assessment year 2006-07 ceases to hold good in law as well.

12. It is in this backdrop that we have come to be in seisin of assessee's appeals against order of the learned CIT(A) for the assessment years 2003-04, 2004-05 and 2005-06 and the order of the Assessing Officer, read with directions of the Dispute Resolution Panel under section 144C(13), for the assessment year 2006-07. The assessee is aggrieved of these orders and is before us.

13. We have heard the rival contentions, perused the material on record and duly considered facts of the case in the light of the applicable legal position.

14. The question that we must decide at the threshold is as to which is the most appropriate method of determining arm's length price on the facts of this case. On this aspect of the matter, the dispute is confined to even narrower a question, i.e. whether or not CPM is the most appropriate method on the facts of this case, because neither revenue authorities have justified any other method of determining the ALP, nor is it in dispute that, if the CPM fails, the TNMM, as canvassed by the assessee, is the only method which can be applied.

15. Rule 10B(1)(c) defines the cost plus method, i.e. CPM, as follows:

Cost plus method, by which,-

(i) the direct and indirect costs of production incurred by the enterprise in respect of property transferred or services provided to an associated enterprise, are determined;

(ii) the amount of a normal gross profit mark-up to such costs (computed according to the same accounting norms) arising from the transfer or provision of the same or similar property or services by the enterprise, or by an unrelated enterprise, in a comparable uncontrolled transaction, or a number of such transactions, is determined;

(iii) the normal gross profit mark-up referred to in sub-clause (ii) is adjusted to take into account the functional and other differences, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect such profit markup in the open market;

(iv) the costs referred to in sub-clause (i) are increased by the adjusted profit mark-up arrived at under sub-clause (iii);

(v) the sum so arrived at is taken to be an arm's length price in relation to the supply of the property or provision of services by the enterprise

16. The fundamental input for application of CPM method, next only to ascertainment of historical costs, is ascertainment of the normal mark-up of profit over aggregate of such direct costs and indirect costs in respect of same or similar property or services in a "comparable uncontrolled transaction" or, of course, a number of such "comparable uncontrolled transactions". When compared with CUP method, as against the "price" of a comparable uncontrolled transaction, one has to find out "normal mark up of profit" in a comparable uncontrolled transaction. Whether it is "price" or "normal mark up of profit", the starting point of both these exercises in the CUP and the CPM is finding a "comparable uncontrolled transaction". In order for such comparisons to be useful, the economically relevant characteristics of the situations being compared must be sufficiently comparable. It is only elementary, as is also noted in the OECD Transfer Pricing Guidelines, that "to be comparable means that none of the differences *(if any)* between the situations being compared could materially affect the condition being examined in the methodology *(e.g. price or margin),* or that reasonably accurate adjustments can be made to eliminate the effect of any such differences".

17. Let us, in the light of the above discussions, take a look at the situation before us. What the assessee is doing for its AEs is manufacturing the products, and, as noted elsewhere in this order, it is an uncontroverted position that the assessee's AEs, collectively constituting Wrigley group, deal**" in FMCG sector which is characterized by impulsive buying by the consumers, heavy expenditure is required to be made on planning and execution of sales promotion**" and that "**these expenditure were incurred by the Wrigley Group to penetrate new market as well as to retain share in the existing market**". It is also an uncontroverted position that **"in respect of sales promotion, both Wrigley India and the AEs carry out this function in their**

respective market". What in effect, thus, assessee does is that the assessee manufactures the products and sells those products to the AEs but sales promotion is required to be done by the respective AE in its respective market. To this extent, there is no dispute whatsoever on factual aspects by the parties before us.

18. The question that arises is whether these transactions can be compared with the sales of similar product to distributors or other entities in the domestic market and particularly in a situation in which not only the market is geographically different but also entire business model is different vis-à-vis transactions with the AEs, inasmuch as the sales in domestic market necessitates substantial expenditure by the assessee for marketing support and sales promotion strategy. In other words, whether "**export price of product *simplictor,* without any marketing support in the related market**" can have a "**comparable uncontrolled transaction**" in "**domestic sale price of a product in a situation in which entire marketing function and sales promotion is seller's responsibility**".

19. In our humble understanding, the answer has to be an emphatic 'No'.The two situations, i.e. sale *simplictor* of a FMCG product for an overseas AE without any costs being incurred on the marketing and sales promotion amongst the end users, and sale of a FMCG product to a domestic independent enterprises with full responsibilities for marketing and sales promotion amongst the end users, are not 'comparable transactions' in the sense that profitability in the latter cannot be a proper benchmark for profitability in the former. It is not only in the marketing and sales promotion that the difference lies, but it extends to the fundamental business model itself particularly as the sale is not to an end user, such as in the cases of plant and equipment etc, but to an intermediary who, in turn, has to sell it to, through yet another tier or tiers of intermediaries, the end user. The sale of products to the non-resident AEs is more akin to contract manufacturing arrangement, while the sale of products to independent enterprises domestically is a regular business entrepreneurial venture. As a

matter of fact, it has been one of the arguments of the assessee before us, and the assessee has also filed some documents and copies of contracts in support of that contention, that the assessee had done the contract manufacturing for its overseas AEs as it had idle and underutilized capacity, but, as there are no findings by the authorities below on this aspect of the matter and as we can anyway dispose of the matter without giving any categorical findings on that aspect of the matter, we see no need to deal with that contention at this stage. Suffice to say that whether contract manufacturing or not, as long as the business models of sales to AEs and sales to non AEs are different, the transactions under these business models cannot be "comparable transactions" for the purposes of transfer pricing. In the first business model, creation of market in the end users is not the responsibility of the vendor, but in the second business model, it is job of the vendor to create and maintain the market of end users as well. The product may be the same but the FAR profile is materially different and it is this FAR profile which governs the profitability. The basic notions of transfer pricing recognize the impact of FAR profiling on the profitability. When profitability levels in two business situations, due to significant differences in FAR profiles of two situations, are expected to be different, such transactions cease to be comparable transactions for the purposes of transfer pricing analysis.

20. In OECD Transfer Pricing Guidelines, this aspect of the matter, so far as comparability analysis is concerned, has been explained thus:

> **1.47 The functions carried out (taking into account the assets used and the risks assumed) will determine to some extent the allocation of risks between the parties, and therefore the conditions each party would expect in arm's length transactions. <u>For example, when a distributor takes on responsibility for marketing and advertising by risking its own resources in these activities, its expected return from the activity would usually be commensurately higher and the conditions of the transaction would be different from when the distributor acts merely as an agent,</u>**

> **being reimbursed for its costs and receiving the income appropriate to that activity. Similarly, a contract manufacturer or a contract research provider that takes on no meaningful risk would usually expect only a limited return.**

[Emphasis, by underlining, supplied by us]

21. The UN Transfer Pricing Manual, elaborating upon the comparability analysis and which is broadly on the same lines as OECD Transfer Pricing Guidelines in this respect, states as follows:

> **5.1.5. A controlled and an uncontrolled transaction are regarded as comparable if the economically relevant characteristics of the two transactions and the circumstances surrounding them are sufficiently similar to provide a reliable measure of an arm's length result. It is recognized that in reality two transactions are seldom completely alike and in this imperfect world, perfect comparables are often not available. It is therefore necessary to use a practical approach to establish the degree of comparability between controlled and uncontrolled transactions. To be comparable does not mean that the two transactions are necessarily identical, but instead means that either none of the differences between them could materially affect the arm's length price or profit or, where such material differences exist, that reasonably accurate adjustments can be made to eliminate their effect. Thus, in determining a reasonable degree of comparability, adjustments may need to be made to account for certain material differences between the controlled and uncontrolled transactions. These adjustments (which are referred to as "comparability adjustments") are to be made only if the effect of the material differences on price or profits can be ascertained with sufficient accuracy to improve the reliability of the results.**

5.1.6 The aforesaid degree of comparability between controlled and uncontrolled transactions is typically determined on the basis of a number of attributes of the transactions or parties that could materially affect prices or profits and the adjustment that can be made to account for differences. These attributes, which are usually referred to as the five comparability factors, include:

- **Characteristics of the property or service transferred;**
- **Functions performed by the parties taking into account assets employed and risks assumed, in short referred to as the "functional analysis";**
- **Contractual terms;**
- **Economic circumstances; and**
- **Business strategies pursued.**

[Emphasis, by underlining, supplied by us]

22. On the facts of the present case, however, the comparability analysis has been confined to the first segment itself, i.e. characteristic of the property transferred. Undoubtedly, the product comparability is an important factor but its certainly not the sole or decisive factor. The assessee was producing the same products for its AEs as it was producing for independent enterprises but that was all so far as similarities were concerned. The FAR profile was not the same, the contract terms were not the same, the economic circumstances were not the same and the business strategies were not the same. Viewed thus, necessary precondition for application of CPM, i.e. finding normal mark up of profit in comparable uncontrolled transactions, could not have been fulfilled. When uncontrolled transactions were not comparable, the normal mark up on profit on such transactions could not have been relevant either.

23. In view of the above discussions, in our considered view, the authorities below were not justified in holding that the cost plus method was the most

appropriate method on the facts of this case. One of the necessary ingredient for application of CPM, i.e. normal mark up of profit in the comparable uncontrolled transactions- whether internal or external, was not available as no comparable uncontrolled transactions were brought on record by the authorities below. What was brought on record as an internal comparable uncontrolled transaction, i.e. manufacturing for the domestic independent enterprises, was uncomparable as the FAR profile was significantly different. Undoubtedly, direct methods of determining ALP, including cost plus method, have an inherent edge over the indirect methods, such as TNMM, but such a preference can come into play only when appropriate comparable uncontrolled transactions can be identified and analysed accordingly. That has not been done in the present case. There is, therefore, no good reason to disturb the TNMM method adopted by the assessee. We have also noted that the TPO himself has accepted the TNMM for the assessment years 2007-08, 2008-09 and 2009-10. Learned Departmental Representative does not dispute that the facts for all these assessment years are similar in material respects. For this reason also, there was no good reason to disturb the ALP determination on the basis of TNMM in respect of the assessment years before us, i.e. 2003-04, 2004-05, 2005-06 and 2006-07.

24. Having held so, we must also point out that the transfer pricing reports with respect to the impugned determination of ALP leave a lot to be desired. Just because the action of the authorities below, in adopting cost plus method in the above manner, is legally unsustainable, the ALP determination by the assessee cannot be taken as correct. These TP reports as also certifications by the chartered accounts inspire no confidence and, quite to the contrary, raise doubts about efficacy of the built in checks and balances in transfer pricing regulations. It is somewhat fashionable to criticize the revenue authorities for their lack of objectivity or even inefficiency but what in the world can justify such a pathetic level of professional work relied upon by even the large corporate entities. If the tax judicial system is clogged by frivolous litigation today and if the tax finality still takes decades to reach, these saviours of taxpayers are as much to be blamed for this situation as anybody else. No

purpose can be served in reporting by a chartered accountant when such reports do not even point out glaring infirmities in taxpayer's approach vis-à-vis the transfer regulation, in a comparison of budgeted profits margin with actual profit margins realized by the comparables which is stated to be ascertainment of ALP on the basis of the TNMM. It appears that in an alarming number cases, these audit reports, rather than painting a true and fair picture of the relevant facts, tend to epitomize the art of constant hedging and manoeuvring by the professionals so as they stay within the confines of permissible professional conduct and are yet able to sidestep the inconvenient realities. Of course, it will be much worse a situation if they are actually so naïve as to be oblivious of simple provisions of law, of their onerous responsibilities or of the legitimate public expectations. It is not to belittle the brilliant work being done by many a professionals but it is just to point out the dilemma of those who explore the possibilities of relying upon such audit reports and certifications, and also the inertia of those who can do something to salvage this situation and, to thus avoid an inevitable systemic rejection of the ritualistic certifications. We are particularly pained today as the financial period before us is mostly even more than a decade old and yet since the TP reports and certifications before us are, in our considered view, are so much devoid of credibility that, instead of deciding the things one way or the other, we have no choice except to remit the matter to the file of the TPO for fresh ascertainment of ALP on the basis of residuary method, i.e. TNMM.

25. In these circumstances, while we hold that, on the facts of this case, the ALP of international transactions with the AEs is to be determined on the basis of TNMM and we vacate the impugned ALP adjustments on the basis of CPM, we also hold that the matter is required to be examined afresh by the TPO in the light of our above observations. We also make it clear that the assessee will be at liberty to justify the ALP determination under the TNMM on such basis as he may deem appropriate and to make all such submissions and to furnish all such evidences in support of thereof, as he may deem fit and proper, and that the TPO will be required to deal with such contentions, submissions and evidences, by

way of a speaking order, in accordance with the law and after giving a fair and reasonable opportunity of hearing to the assessee.

26. Accordingly, so far as the transfer pricing issue in all these appeals is concerned, while we uphold the grievances of the assessee in principle but remit the matter to the file of the TPO for fresh examination in the light of our observations as above. So far as the appeals filed by the assessee are concerned, that is the only point on which our adjudication was required.

28. In the result, therefore, we allow all the four appeals filed by the assessee (i.e. I.T.A. Nos.: 5648, 5649 and 5650/Del/12 and 5224/Del/10) for the limited statistical purposes and in the terms indicated above.

29. We now take up the appeals filed by the Assessing Officer.

30. The common grievance in all these three appeals is that the learned CIT(A) erred in law and on the facts of this case in deleting the addition of Rs 39,00,813 for the assessment year 2003-04,Rs 9,05,383 for the assessment year 2004-05, and Rs 7,08,793 for the assessment year 2005-06, made by the AO **"by treating the expenses incurred by the assessee on research and development as capital in the nature**". It is also pointed out that the tax implication of the above issue is less than permissible threshold limit in two of the assessment years before us but then as the issue is repetitive in nature, it is covered by the exemption clause in the CBDT instructions in this regard. Learned counsel for the assessee does not dispute this position.

32. We have noted these expenses were disallowed by the AO on the basis that the expenses were treated as research and development expenses resulting in enduring benefit to the assessee and that these expenses pertained to the development of the new product. However, when mater travelled in appeal before the CIT(A) he deleted the disallowance on the ground that these expenses were incurred on "laboratory testing of the products" and were thus

routine revenue expenses in nature. Learned CIT(A) had also noted that "incurring of these expenses has not resulted in creation of any intangible capital asset". The Assessing Officer is aggrieved and is in appeal before us.

33. Having heard the rival contentions and having perused the material on record, we see no reasons to interfere in the conclusions arrived at by the learned CIT(A). There is no material before us to dislodge, or even call into question, the findings of the CIT(A). The expenses incurred on the laboratory testing of the products is a routine process and these expenses have not also resulted in creation of an intangible asset or substantial enduring advantage. Under these circumstances, and bearing in mind entirety of the case, we see no infirmity in learned CIT(A)'s deleting the impugned disallowance. We uphold his order and decline to interfere in the matter.

34. The grievances of the Assessing Officer, as raised in his all the three appeals before us, are dismissed.

35. In the result, while appeals filed by the assessee are allowed for statistical purposes in the terms indicated in this order, the appeals filed by the Assessing Officer are dismissed. Pronounced in the open court today on 31st day of December, 2014,

Sd.xx
I C Sudhir
(Judicial Member)

Sd/xx
Pramod Kumar
(Accountant Member)

New Delhi, the 31st day of December, 2014

Copies to:
(1) The appellant
(2) The respondent
(3) CIT , New Delhi
(4) CIT(A)- , New Delhi
(5) DRP- , New Delhi
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By order etc

Assistant Registrar
Income Tax Appellate Tribunal
]Delhi benches, New Delhi