

**IN THE INCOME TAX APPELLATE TRIBUNAL,
DELHI I BENCH, NEW DELHI
[Coram : Pramod Kumar AM and Rajpal Yadav JM]**

I.T.A. No.: 4620/Del/2011
Assessment year: 2004-05

***Dy Commissioner of Income Tax
Circle 14(1), New Delhi***

.....**Appellant**

Vs.

***Panasonic AVC Networks India Co Ltd
D 13/4, Okhla Industrial Area Phase II
New Delhi 110 020 [PAN: AAACM6492M]***

.....**Respondent**

Appearances by:

Peeyush Jain and Y K Verma, *for the appellant*
Deepak Chopra, *for the respondent*

Date of concluding the hearing : December 24,2013
Date of pronouncing the order : February 21,2014

O R D E R

Per Pramod Kumar:

1. By way of this appeal, the Assessing Officer has challenged the correctness of learned Commissioner (Appeals)'s order dated 11th August 2011, in the matter of assessment under section 143(3) of the Income Tax Act, 1961 (hereinafter referred to as 'the Act') for the assessment year 2008-09.

2. The appeal is time barred by 2 days but the Assessing Officer has moved a petition praying that the delay be condoned. Learned counsel for the assessee does not oppose this marginal delay in filing of the appeal. Having perused the petition, and having heard rival contentions on the same, we deem it fit and proper to condone the delay and take up appeal for disposal on merits.

3. Grievances of the Assessing Officer, relate to learned CIT(A)'s deleting the arm's length price (ALP) adjustment amounting to Rs 5,72,16,360, and are as set out below:

1. On the facts and circumstances of the case, the Ld. CIT(A) has erred in using the margins of the assessee after allowing for adjustment for capacity utilization. As per A.O., the capacity utilization was due to extraordinary business circumstances and not been explained on facts.

2. On the facts and circumstances of the case, the Ld. CIT(A) has erred in allowing the use of two comparables vis. Carrier Aircon Ltd. and Whirpool of India Ltd. which were not used by the A.O. and one comparable Videocon International has been excluded on the basis of functional profile.

4. So far as first ground of appeal is concerned, the issue in appeal lies in a very narrow compass of material facts. The assessee is engaged in the business of manufacturing and sale of colour television sets. During the course of assessment proceedings, the international transactions entered into by the assessee with its AEs were referred to the Transfer Pricing Officer for determination of arm's length price. The assessee had used the TNMM with net profit margin on sales as profit level indicator. While this method was accepted by the TPO as well, one of the issues on which TPO did not agree with the assessee was adjustments for capacity utilization. The TPO rejected the assessee's claim for capacity utilization on the ground that, "all the comparables are also operating in same economic environment and all are playing same game of price cutting and volume generation" and "therefore, any adjustment on account of these two factors (i.e. capacity adjustment and risk adjustment) will change the level playing field and benchmarking of international transaction will not be correct reflection of economic activities undertaken by the assessee". The assessee was not satisfied with the stand so taken by the TPO and the matter was carried in appeal before the CIT(A). Learned CIT(A) took note of assessee's submission that the assessee's production in the relevant previous year was much below the installed capacity, that such capacity underutilization explained higher fixed costs and lower profits, and that the assessee's brands, i.e. 'National' and 'Panasonic', were premium brands with high end prices whereas Indian television market was dominated by certain Korean brands

which were producing high volumes on the basis of low profits. Learned CIT(A) was of the view that in case a reasonably accurate method of making adjustment for such low capacity utilization can indeed be made, such an adjustment will meet ends of justice particularly as the assessee had utilized only 31.75% of its installed capacity. Learned CIT(A) also noted that the details of installed capacity and utilized capacity are available in the financial statements of the companies, and is in public domain. It was in this backdrop that he directed the capacity underutilization adjustment in depreciation allowance, by making adjustments in depreciation figures of the tested party as also of the comparables, as the figures of depreciation as also of capacity utilization were available in respect of the comparables. It was also directed that in the case of companies with multi product profile, weighted average of capacity utilized for each product, using per unit sale price as weight, be used to compute the capacity utilized. Revenue is aggrieved of the directions so given by the CIT(A) and is in appeal before us.

5. Having heard the rival contentions and having perused the material on record, we see no reasons to interfere in very well reasoned findings and directions of the learned CIT (A). Rule 10 B (1)(e)(ii) of the Income Tax Rules 1962 does indeed provide that the net profit margin realized in a comparable uncontrolled transaction is adjusted, inter alia, for differences in enterprise entering into such transactions, which could materially affect the net profit margin in open market. Capacity underutilization by enterprises is certainly an important factor affecting net profit margin in the open market because lower capacity utilization results in higher per unit costs, which, in turn, results in lower profits. Of course, the fundamental issue, so far as acceptability of such adjustments is concerted, is reasonable accuracy embedded in the mechanism for such adjustments, and as long as such an adjustment mechanism can be found, no objection can be taken to the adjustment. In our considered view, the learned CIT(A)'s approach is reasonable in this regard and the adjustments are on a conceptually sound basis. In any case, as pointed out by the learned

counsel, the adjustments so directed by the learned CIT(A) have duly been made by the Assessing Officer, and there have been no issues regarding implementing these adjustments. We approve the conclusions arrived by the CIT(A) on this issue and decline to interfere in the matter.

6. Ground No. 1 is thus dismissed.

7. Coming to the second ground of appeal, we find that this grievance has two facets – first, against the admission of two new comparables by the CIT(A) and – second, against CIT(A)'s exclusion of a comparable which was used by the Transfer Pricing Officer in his determination of arm's length price under the transactional net margin method. So far as acceptance of the additional comparables is concerned, the CIT(A) has done so after calling for a remand report and in the light of special bench decision of this Tribunal in the case of DCIT Vs Quark Systems Pvt Ltd (132 TTJ 1 SB). The only objection taken by the Assessing Office in the remand report was that these comparables were rejected by the assessee in its own TP study report. The assessee does not dispute it. The submission of the assessee is that these comparables were rejected by the assessee on the presumption that since these comparables have significant share capital holdings abroad, it could be presumed that these comparables had significant related party dealings. However, as subsequent judicial precedents ruled, it was not appropriate to reject such companies on the presumption of related party transactions. It was for this reason that the assessee, at the appellate stage, prayed for admission of these comparables. Learned CIT(A), relying upon Special Bench decision in the case of Quark Systems (supra), has held that there cannot be any estoppel against pointing out assessee's own errors in selection of comparables and that aspect of the matter is to be decided on merits, and on merits as also since the AO has not made any submissions against the same in remand report, these additional comparables can be accepted. So far as second facet of this dispute, i.e. exclusion of Videocon

International, is concerned, the reasoning adopted by the CIT(A) in the exclusion is this. It is observed that Videocon is not a comparable company because its turnover is substantially higher at Rs 4,000 crores, because it has done the backward integration, because it also produces different product profile items, because it has made significant investment in research and development and because it is enjoying several tax exemptions due to its location in backward areas. The Assessing Officer is aggrieved of the stand so taken by the CIT(A) and is in appeal before us.

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

9. So far as the admission of additional comparables is concerned, we have noted that the only objection of the Assessing Officer is that when assessee himself has discarded these comparables at the stage of assessment, it should not be open to him to pick the same comparables at the appellate stage. However, as learned representatives agree, this issue is now covered, in favour of the assessee, by a special bench decision in the case of Quark Systems (*supra*). In this view of the matter, and having regard to the entirety of the case, we approve the stand of the CIT(A) and decline to interfere in the matter. That takes us to Assessing Officer's grievance against CIT(A)'s excluding the one comparable, i.e. Videocon International, on the ground that there are major dissimilarities between the tested party and this comparables. During the course of hearing, the assessee was asked to demonstrate that this kind of an analysis, as was done to argue on unsuitability of Videocon International, was also done on the other comparables. Learned counsel admittedly his inability to do so but fairly accepted that the matter can be remitted to the file of the learned CIT(A) for fresh adjudication by applying uniform norms on the analysis of all the entities picked up as comparables. Learned Departmental

Representative was also satisfied with this course of action. In our considered view also, there cannot be a cherry picking for deciding parameters of rejection of a comparable, and the parameters have to be broad enough of being general application. In the scheme of things envisaged under the TNMM, it is inevitable that there will be some differences between the comparables and the tested party but the impact of these differences is substantially mitigated by the averaging. If a comparable is being sought to be rejected on the ground of its differences vis-à-vis the tested party, similar criteria must be adopted for deciding suitability of other comparables as well. It cannot be open to any judicial authority to reject a comparable on the ground that the comparable has significant differences vis-à-vis the tested party, unless the differences are broad enough of general application, are such as materially affecting the profitability, as not being capable of reasonably accurate adjustments to eliminate the impact of such differences, and as are also not found in other comparables. All the comparables must face the same test on which comparability of a particular comparable is being sought to be rejected. Accordingly, in our considered view, the matter should be restored to the file of the CIT(A) for adjudication de novo, on the issues of rejection of Videocon International as a comparable, in accordance with the law, in the light of, inter alia, our above observations, by way of a speaking order and after giving a fair and reasonable opportunity of hearing to the assessee. We order so.

10. Ground no. 2 is thus allowed for statistical purposes.

11. In the result, the appeal is partly allowed for statistical purposes in the terms indicated above. Pronounced in the open court today on 21st day of February, 2014.

Sd/xx

Rajpal Yadav
(Judicial Member)
New Delhi, the 21st day of February, 2014

Sd/xx

Pramod Kumar
(Accountant Member)

*Copies to : (1) The appellant
(2) The respondent
(3) C I T
(4) CIT(A)
(5) Departmental Representative
(6) Guard File*

By order etc

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