आयकर अपीलीय अधिकरण, अहमदाबाद न्यायपीठ ''डी' अहमदाबाद।

IN THE INCOME TAX APPELLATE TRIBUNAL
"D" BENCH, AHMEDABAD

श्री जी0सी0 गुप्ता, उपाध्यक्ष एवं श्री एन0एस0 सैनी, लेखा सदस्य सदस्य के समक्ष

BEFORE SHRI G.C. GUPTA, VICE PRESIDENT AND
SHRI N.S. SAINI, ACCOUNTANT MEMBER

ITA (TP) No. 2881/Ahd/2012
Assessment Year 2008-09

M/s. Siemens Healthcare Diagnostics Limited (now merged with Siemens Ltd), 589, Sayajipura, Ajwa Road, Baroda-390019. PAN: AAACB8542M	Vs	The Assistant Commissioner of Income Tax, Circle-4, Baroda.
अपीलार्थी/ Appellant		प्रत्यर्थी / Respondent

Revenue by :	Shri Vimalendu Verma, DR
Assessee(s) by :	Karishma Popat Phatarphekar, AR

सुनवाई की तारीख/**Date of Hearing : 11/09/2014**
घोषणा की तारीख /**Date of Pronouncement: 19/09/2014**

आदेश/O R D E R

PER SHRI N.S. SAINI, ACCOUNTANT MEMBER:

This is an appeal filed by the assessee against the order of the Dispute Resolution Panel, Ahmedabad dated 26.09.2012.

2. Ground nos. 1, 2, 3, 5, 6 and 7 of the appeal read as under:

1. On the facts and in the circumstances of the case and in law, the learned Deputy Commissioner of Income Tax (TPO) - II, Ahmedabad ('TPO') and the learned Assistant Commissioner of Income-tax Circle-4, Baroda ('AO') under directions issued by

the Hon'ble Dispute Resolution Panel, Ahmedabad ('DRP'), erred in making an addition of Rs. 18,763,625 to the Appellant's total income based on the provisions of Chapter X of the Income Tax Act, 1961 ('the Act').

2. On the facts and in the circumstances of the case and in law, the learned AO/TPO erred and the Hon'ble DRP further erred in upholding / confirming the action of the learned TPO in not accepting the two comparables selected by the Appellant i.e. Casil Health Products Ltd and Monozyme India Ltd on the premise of "functional comparability", without appreciating the fact that the same were considered as "functionally comparable" in earlier assessment year (AY) i.e. AY 2007-08.

3. On the facts and in the circumstances of the case and in law, the learned AO/TPO erred and the Hon'ble DRP further erred in upholding / confirming the action of the learned TPO in not accepting the comparables selected by the Appellant based on updated search performed by the Appellant during the course of assessment proceedings before the TPO, on the basis that the international transactions of the Appellant ought to be benchmarked separately, without appreciating the fact that the said international transactions are closely linked and cannot be separated.

5. On the facts and in the circumstances of the case and in law, the learned TPO erred and the Hon'ble DRP further erred in upholding / confirming the action of the learned TPO in rejecting the use of multiple year data for computing the operating margin of the comparable companies.

6. On the facts and in the circumstances of the case and in law, the learned TPO erred and the Hon'ble DRP erred in upholding / confirming the action of the learned TPO in not allowing the benefit of 5 per cent variation available under the second proviso to Section 92C(2) of the Act.

7. On the facts and in the circumstances of the case and in law, the leaned Assessing Officer/TPO erred in not providing the calculation for the revised upward adjustment made on account of transfer pricing to the income of the Appellant after giving effect to the directions of the Hon’ble Dispute Resolution Panel.

At the time of hearing, the Authorized Representative of the assessee did not make any submission in respect of the above grounds. Hence, these grounds are dismissed for want of prosecution.

3. Ground no. 4 of the appeal is directed against the order of Dispute Resolution Panel upholding the action of the Transfer Pricing Officer in not allowing adjustment to the profitability on account of depreciation for "like to like" comparison of business model of the assessee and comparable company.

4. The assessee submitted before the Transfer Pricing Officer as under:

> ***"a. Adjustment on account of depreciation***
>
> *The assessee follows two types of business models for its distribution function. In the first model, the assessee sells instruments on an outright basis to the customers. In the second model, the assessee provides instrument to the customers on lease basis, with the condition that customers will have to buy reagents from the assessee over an agreed period. The assessee uses this mechanism to ensure a committed sale of consumables. The assessee thus follows a unique business model, wherein diagnostic instruments are sold to customers on lease basis and during the lease period diagnostic instrument is used by the customers and depreciation on such instruments is recorded by the assessee.*
>
> *In second business model, the instruments are rented ("seeded") and used by the customers but capitalized in the books of the assessee as "Fixed Asset". Thus the depreciation on the instruments is recorded in the books of the assessee.*
>
> *In the following table, the assessee has compared the ratio of Depreciation Cost to the total operating cost of the assessee vis-a-vis Span Diagnostics Ltd for FY 2007-08:*

Particulars	***SHDL***	***Span Diagnostics Ltd.***
Depreciation Cost	*63,502,982*	*14,465,868*
Total Operating Cost	*792,291,108*	*549,724,372*
Depreciation as % of Total Operating Cost	*8.02%*	*2.63%*

> *Thus, from the aforesaid analysis, it is evident that ratio of depreciation cost to total cost ratio is almost three times higher in the case of the assessee as compared to Span Diagnostics Ltd. Hence, for the purpose of "like to like" comparison an adjustment in respect of depreciation cost while computing margin of the assessee and comparable companies is claimed.*
>
> *Accordingly, the assessee has computed the operating margins of the assessee and the comparable companies without considering*

depreciation cost. Based on above, operating margin of the assessee and Span Diagnostics Ltd works out to as follows.

Particulars	***Span Diagnostics Ltd.***	***The Assessee***
NPM	*13.28 percent*	*13.30 per cent*

Hence, the international transactions entered into by the assessee appear to be consistent with the arm's length standard from an Indian Transfer pricing perspective."

5. In support of above submission, the assessee placed reliance on the decision of the Delhi Bench of the Tribunal in the case of Schefenacker Motherson Ltd. Vs. ITO (2009) 123 TTJ 509 (Del) wherein the Tribunal held that depreciation could be excluded while computing the margin of the comparable companies and tested party, if depreciation is resulting in a large differences in margin of tested party and comparable company.

6. After going through the submissions of the assessee, the Transfer Pricing Officer held as under:

"*There are valid reasons for computing net margin under TNMM after allowing deduction on account of depreciation as :-*

(a) It is undisputed fact that depreciation is a cost incurred in generation of revenue accordingly; net margin is to be computed only after allowing depreciation.

(b) Depreciation is compulsorily allowable deduction in computing net margin Under the Indian Income Tax Act,

(c) Failure to factor in a reasonable allowance for usage of an asset will over inflate the result given by the TNMM.

(d) Taxpayer always include rent / lease rent that it pays in the cost base for computing net margin under TNMM accordingly, excluding depreciation expense incurred while it owns an asset, cannot be envisaged.

(e) If one examines international practices like USA transfer pricing provisions then it is noticed that section 482 of US regulation which define "operating expense" stipulates deduction of depreciation. In the USA IRSAPA training manual depreciation is included in the cost bases while computing margin under TNMM.

(f) Hon'ble ITAT in case of E-gain communication Pvt. Ltd. (Pune ITAT) has also approved computation of net margin under TNMM after taking into account depreciation.

F.10 Considering the above, it is clear that depreciation is required to be taken into account for the purposes of calculation of the PLI. In addition to the above as noted in the discussion above, the assessee should have benchmarked its international transactions in respect of trading of goods and the international transactions representing income earned on renting of equipments separately. In such a situation that depreciation could have been considered to he taken out from the calculations for the benchmarking of simple trading transactions, on the basis of the facts so presented. However, since the assessee has benchmarked all its transaction! at an entity level, if the proposal for taking out depreciation from PLI is accepted, it will tantamount to taking out all the transactions, representing purchase of capital goods from the AE and capitalized in the books of account, from the purview of the benchmarking exercise. This is so because the effect of the international transactions, representing asset purchase from AE, on the margin is only through depreciation. Therefore since the entity level margin is considered by the assessee, the depreciation is to 'be included necessarily to find out the correct benchmarking for the international transactions representing purchase of capital goods. Thus this contention is not accepted."

7. On appeal before the Dispute Resolution Panel, the assessee submitted as follows:

"Any receipt or expenditure having no bearing on price or margin of profit can be ignored. Depreciation can be taken into account or disregarded in computing profit depending upon the context and purpose for which profit is to be computed. There is no formula which would be applicable universally and in all circumstances. "Net profit" used in Rule 10B can be taken to mean commercial profit. Depreciation, which can have varied basis and is allowed at difference rates is not such an expenditure which must be deducted in all situations. It has no direct connection or bearing on price, cost or profit margin of the international transactions. Object and purpose of the transfer pricing is to compare like with the like, and to eliminate differences, if any, by suitable adjustment.

The ratio of depreciation cost to total cost ratio is almost three times higher in the case of the assessee as compared to Span Diagnostics Ltd. Hence, for the purpose of "like to like" comparison, the assessee claimed for adjustment in respect o depreciation cost while computing margin of the assessee and comparable companies.

Alternatively, the operating profit excluding depreciation should be considered for the purpose of comparison as depreciation is leading to large differences in margins of the assessee and Span Diagnostics Ltd."

8. The Dispute Resolution Panel decided the issue as under:

> *"We have considered the facts of the case. The assessee's business is asset intensive. The instruments etc are given "on lease to earn income. It is not pure trading. In such circumstances removing depreciation will mean retaining the income but removing the corresponding expenditure/costs/ charges. This will project a distorted picture of assessee's accounts. Hence we are in agreement with the TPO that depreciation will have to be included in the PLI working."*

9. Before us, the Authorized Representative of the assessee submitted as under:

> "*According to Rule 10B(1)(e)(iii), adjustment has to be provided to account for any differences between the international transaction and the uncontrolled comparables.*
>
> *TPO has misread the Rules to say that the Assessee needed to demonstrate that its depreciation has impact on the margin in the open market.*
>
> *In fact the Rules state that if any difference arises between the Assessee and the comparable, adjustment needs to be made.*
>
> *In Assessee's case, the percentage of depreciation to total operating cost was 8.05% whereas that of Span Diagnostics was 21.61% (Refer Calculation of Percentage of Depreciation (HD7)).*
>
> *Assessee follows SLM while charging depreciation while Span Diagnostics follows WDV. Since both these methods adjustment is warranted to bring Span Diagnostics in line with Assessee. (Refer relevant extracts of Annual Report of Spam and Assessee HD8 and 9)).*
>
> *Therefore, our plea is to either exclude depreciation or adjust the comparable's depreciation to the Assessee's level of depreciation.*
>
> *More so, considering that there is only one company that the TPO is comparing, it is important to make this truly comparable on all parameters.*
>
> *Alternatively, if fresh comparables are added to Span, the average margin would not be heavily dependent on one comparable and may better represent the arm's length scenario.*
>
> *The Assessee's plea is on principle grounds that if there are differences in its own facts vis-à-vis facts of comparable then adjustment is warranted. Adjustment can be made by excluding depreciation or adjusting the level of depreciation."*

10. In support of the above submission, the Authorized Representative of the assessee quoted following judgments:

1. Schefenacker Motherson Ltd. v. ITO (2009) 123 TTJ 509 (Del)
2. DCIT v. Reuters India Pvt. Ltd. (2013) 24 ITR (Trib) 231 (Mum)
3. Pentair Water India Pvt. Ltd. v. Addl. Commissioner of Income Tax (2014) 47 taxmann.com 132 (Panaji)
4. Market Tools Research Pvt. Ltd. v. ACIT ITA No. 2066/Hyd/2011

11. We have heard the rival submissions and perused the orders of lower authorities and material available on record. In the instant case, the assessee is engaged in the business of trading of diagnostic instruments and consumables manufactured by its associated enterprises. The assessee entered into international transactions representing purchase of goods from the associated enterprises. The conclusion arrived by the assessee in respect of arm's length nature of the transaction was not found to be acceptable by the Transfer Pricing Officer. It is not in dispute that the arm's length price of the aforesaid international transaction is to be benchmarked on Transaction Net Margin Method (TNMM). To compute Transaction Net Margin Method of the assessee, data of M/s. Span Diagnostics Limited was found to be comparable by Transfer Pricing Officer. As per the Transfer Pricing Officer, the Transaction Net Margin Method of M/s. Span Diagnostics Limited works out to 9.22% whereas the Transaction Net Margin Method of the assessee in respect of aforesaid international transactions comes to 5.75%. Therefore, the Transfer Pricing Officer added Rs 2,91,87,164/- to the income of the assessee. The assessee claimed before the Transfer Pricing Officer that there is huge difference between the depreciation of the assessee and the depreciation of the comparable case in as much as ratio of depreciation to total cost ratio is almost three times higher in the case of the assessee as compared to M/s. Span Diagnostics Limited, the comparable case. The depreciation in the case of the assessee comes to 8.02% of operating cost whereas the depreciation to the total operating cost comes to

2.63% only in the case of M/s. Span Diagnostics Limited. The assessee also pointed out that the depreciation charged by the assessee in its books of accounts is on Written Down Value (WDV) method whereas the depreciation charged in the case of M/s. Span Diagnostics Limited is on Straight-line method, hence for comparing Transaction Net Margin Method of the two companies, adjustment in respect of depreciation is must. However, the Transfer Pricing Officer had given no finding on the variation in the amount of depreciation as well as effect of variation in two different methods of providing depreciation employed in the two cases. In the opinion of the Transfer Pricing Officer, depreciation is must for arriving at net margin and therefore depreciation cannot be excluded.

12. On appeal before the Dispute Resolution Panel, the assessee reiterated its submissions made before the Transfer Pricing Officer.

13. The Dispute Resolution Panel has also not recorded any finding in respect of the claim of the assessee about the difference in the amount of depreciation as well as in respect of difference in the method of providing depreciation employed in the case of the assessee vis-à-vis the method employed in the case of M/s. Span Diagnostics Limited. The Dispute Resolution Panel without recording any finding on this issue confirmed the action of the Transfer Pricing Officer. We find that the Delhi Bench of the Tribunal in the case of Schefenacker Motherson Ltd. vs. ITO & Anr. (2009) 123 TTJ 509 (Del) has held as under:

> "*In the present appeal, ALP of transactions carried was to be determined by comparing net profit of the taxpayer (tested party) with mean net profit of comparables. Only receipts and expenditure, having connection with international transactions, were required to be taken into account. Any receipt or expenditure having no bearing on price or margin of profit could not be taken into consideration. It is evident from statutory provisions that it is nowhere provided that deduction of depreciation is a must. Depreciation can be taken into account or disregarded in computing profit depending upon the context and purpose for which profit is to be computed. There is no formula which*

would be applicable universally and in all circumstances. "Net profit" used in r. 10B can be taken to mean commercial profit as held by the TPO and confirmed on appeal by the CIT(A). But depreciation in such profit on commercial principles has to be the "actual" amount by which the assets of business got depleted between the two dates separated by a year. It cannot be depreciation under tax or companies rules or as per policy of the company. In the case in hand, Revenue authorities went wrong in disregarding the context and purpose for which the "net profit" was to be computed. Depreciation, which can have varied basis and is allowed at different rates, is not such an expenditure which must be deducted in all situations. It has no direct connection or bearing on price, cost or profit margin of the international transactions. Object and purpose of the transfer pricing to compare like with the like, and to eliminate differences, if any, by suitable adjustment is to be seen. Therefore, there was justification on the part of the taxpayer in pleading that profits be taken without deduction of depreciation as depreciation was leading to large differences in margins for various reasons. The taxpayer also relied upon para 22.4 of Guidance Note on Transfer Pricing issued by ICAI suggesting cash - profit/sales as one of the ratios to be applied for computing ALP under the TNMM as per Indian Regulations. Contention that depreciation would depend upon type of technology employed, age and nature of machinery used, is quite well-founded. Above, along with size of enterprise and investment in plant/machinery were important factors to be taken into account for comparison and for computing profit. There is considerable support for the contention raised on behalf of the taxpayer in the OECD Guidelines on Transfer Pricing. The claim of depreciation can lead to great difference in computing profits of comparables as depreciation is permitted depending upon nature of plant/machinery and year of use. In 5th or 6th year of commencement, depreciation can be 25 to 30 per cent of amount allowed in first year to an enterprise. In these appeals, the TPO had excluded certain comparables after noting differences in their year of start of operations. Thus, age of plant/machinery and other related information is available on record and, therefore, contention of the taxpayer on differences in claim of depreciation is fully established on record. Obviously there are differences between the machinery employed by the taxpayer and other comparable concerns which is reflected in amount and percentage of depreciation claimed. How this variation and difference could be ignored under TP Regulations is neither shown nor explained. The taxpayer has debited high amount/ratio of depreciation as per rules as it was first or second year of commencement of its business. Other enterprises nave claimed depreciation at much lower amounts. It is more than 5 and 15 times of the taxpayer. Size of the assets besides the age of the assets of comparables was leading to difference in the profit margins and in mean margin. On the contrary, claim of depreciation is eating up large chunk of profit in the case of the taxpayer. How above differences were not considered in applying FAR analysis? The CIT(A) has not said a word on "asset" employed and "risks" suffered by the tested party and the comparables. Thus, material differences needing suitable

adjustment were ignored and a flawed analysis was carried even in appellate proceedings. The AO, after looking into details of financial results of comparable enterprises, excluded all companies except the three, although two of companies selected, namely CCML and RPL percentage of depreciation to total cost had differences of more than 2 per cent which is quite substantial. The CIT(A) is right in holding that working of mean profit of the TPO on the basis of three selected companies was not correct. But then the CIT(A) also failed to give due regard to the nature, type and age of the machinery employed by comparables or size of the companies leading to material differences. Without considering obvious material differences, the contention of the taxpayer to take profit without depreciation was rejected. This rejection is not sound in law.

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The CIT(A) has observed "fresh investment was being made in automobile ancillary industry which was in expansion phase and, therefore, there is no requirement to exclude depreciation in computing PLI". What expansion, when made, the date and year of expansion, its comparability with taxpayer's case? Nothing relevant is stated in the impugned orders. One does not know how differences on account of depreciation could be ignored on the facts stated above merely on general observations that automobile ancillary industry is in the expansion phase. Taxpayer is seeking adjustment of differences on account of depreciation and no plausible reason has been given for not accepting this claim. There is no finding that there are no differences in claim of depreciation and, therefore, it should have been excluded in computing "operating profit" as warranted by rules. On the other hand, the differences as per the chart are accepted. The finding that cash profit cannot be considered is not legally correct. The taxpayer in order to get adjustment of difference in depreciation furnished arm's length working after excluding depreciation and by taking all other expenses into consideration and showed that such profit of the taxpayer was quite comparable to the mean margin of comparables similarly computed. This demonstratively showed that deduction of depreciations was making huge difference and required suitable adjustment. This claim has not been challenged. It is clear that the best way to adjust difference on account of depreciation was to ignore depreciation both in case of the party and the comparables. After all TP adjustments are to be made of differences in price charged or for international transactions and not of difference in the claim of depreciation as has been done in this Such adjustments also matched the requirement of the context (TP principles). The basic issue was whether the cost paid or charged for international transactions was at arm's length or not. The factors which go to influence price, cost or profit are/were relevant for computing profit and not depreciation having no direct connection with price or profit but responsible for wide differences. The case of the Revenue is not clear. If depreciation is not leading to any difference, its exclusion is immaterial. If it is leading to differences, then differences are required to be adjusted, as

required by provisions of IT Regulations. There is no way to dislodge the claim of the taxpayer. The context and purpose of legislation and facts of case overwhelmingly approve adoption of cash profit only. The taxpayer in both the assessment years showed before the Revenue authorities that profit shown by the taxpayer satisfies arm's length requirement on ratio of cash profit to sales if uniformly applied. As the deduction of depreciation is leading to wide differences, the same should be excluded. The only reason given for rejecting taxpayer's analysis and for making adjustment in the two years is that use of ratio of cash profit without depreciation is not permitted under the law. This view in the light of above discussion cannot be accepted as correct and is disapproved."

14. Further, the Panaji Bench of Tribunal in the case of Pentair Water India Pvt. Ltd. v. ACIT (2014) 47 taxmann.com 132 (Panaji) has held as under:

"The common contention in respect of computation of TNMM i.e. operating profit taken by the ld. AR in respect of the comparables is that while computing the profit ratio, profit prior to depreciation should be computed as it will give true and fair profit ratio without being affected by the depreciation charged by each of the companies. We noted that different companies have adopted different method of depreciation. In fact, for charging depreciation to the Profit & Loss account there are different prevalent recognized methods of depreciation. Some Assessee opt of Straight Line method, some opt for Written Down method and some opt for Sum of Digit method or even Replacement Cost method. Selection of each method will affect the rate and quantum of depreciation even if the nature of the asset is the same and ultimately, the net profit derived by the company will vary. For determining the fair and true profit, in our opinion, it is appropriate that the effect of the depreciation must be excluded out of the operating profit for determining the operating profit ratio. Therefore, the best way of computing the operating profit, in our opinion, will be to compute the profit before depreciation in respect of each of the company. This will take out the inconformity or the variation in the profit level of the comparables arising due to adoption of different method of charging depreciation. We have gone through the order of the Bombay Bench of this Tribunal in the case of Reuters India (P.) Ltd. as has been relied on by the ld. AR. We noted that the Tribunal in this case has adopted the cash profit/operating cost as the correct profit level indicator under the TNMM method. If the net operating profit ratio is computed in respect of the CDR unit before depreciation, it will be as under:

Particulars		***Total***
Revenue from CDR Operations		*109,449,682*
Notional revenue		*1,629,003*
Total		*111,078,685*
Total Operating Cost	*97,289,193*	
Less: Adjustment for Excess Depreciation provided	*13,565,825*	
Adjusted Operating Cost		*83,723,368*
Operating Profits		*27,355,317*
Net Operating Profit/Operating Cost		*32.67%*

15. In the above facts and circumstances, in our considered view, it shall be fair and in the interest of justice to restore the matter back to the file of the Transfer Pricing Officer for proper verification of the claim of the assessee regarding huge difference in the amount of depreciation between the assessee company and the chosen comparable case and also the difference in the method of providing of depreciation in the two companies. In our considered view, if the methods of depreciation adopted by the two companies are different, then the net margins arrived at are not strictly comparable unless suitable adjustment is made in the amount of depreciation so as to adopt depreciation under the same method in the two cases. Therefore, the Transfer Pricing Officer is directed to take into consideration the difference in the method of providing depreciation in the case of the assessee and the chosen comparable case and if the methods are different, then to make suitable adjustment for the same as per law.

16. Further, in view of the above two decisions of the Tribunal as quoted above, it is observed that if in case depreciation of the assessee and the comparable case are not on the similar method, then for comparing the results of the two companies the cash margin also can be adopted for comparing the Transaction Net Margin Method of the two companies. The Transfer Pricing Officer is directed to take into consideration the above cited

decisions for deciding the issue afresh as per law. Needless to mention that proper opportunity of hearing shall be allowed to the assessee before adjudicating the issue afresh. We order accordingly. Thus, this ground of appeal of the assessee is allowed for statistical purposes.

17. Ground no. 8, 9 & 10 of the appeal are directed against the order of Dispute Resolution Panel confirming the order of the Assessing Officer disallowing the claim of Rs 1,30,17,067/- being depreciation in respect of instruments placed at customers' site and capitalized in the books of accounts.

18. The Assessing Officer held as under:

> *"On perusal of submission, it is seen that assessee has placed newly purchased plant and machinery with its customers and charging nothing from them and has claimed depreciation. The assessee was asked as to why the claim of depreciation should not be disallowed as the machineries are not utilized for the purpose of business following the stand taken in earlier years.*
>
> > *"In point 5 of your captioned notice you intend to disallow depreciation claimed on the instruments placed at customers place on the plea that same are not used for the purpose of our business. In that respect first of all we wish to inform you that you have taken incorrect figures of additions as well as depreciation. The addition in respect of instruments placed at customers place and used for more than 180 days is Rs 6,51,66,908/- and balance Rs 3,800/- is addition towards mobile instruments. The addition of instruments used for less than 180 days is Rs 4,32,27,079/- and balance Rs 8,20,802/- is towards other installations not related to instruments placed at customers place. Accordingly, the correct figure of depreciation is Rs 97,75,036/- (for 180 days or more) and Rs 32,42,031/- (for less than 180 days) totalling to Rs 1,30,17,067/-.".*
>
> *The submission of the assessee has been perused and duly considered. The assessee has reiterated its arguments as argued in earlier years. Since, the department is in appeal on this issue, the plea of assessee is not sustainable. Therefore, a sum of Rs 1,30,17,067/- being depreciation claimed on machinery placed with customers is disallowed and added back to the total income of the assessee.*

The objection has been raised by the assessee before the DRP, against this addition also. The Ld. DRP held that it is mentioned in the AO's order that this issue is pending before the ITAT in earlier years. In such circumstances, we refrain from issuing any direction on this issue. Hence, a sum of Rs 1,30,17,067/- being depreciation claimed on machinery placed with customers is disallowed and added back to the total income of the assessee. Penalty proceedings u/s. 271(1)(c) of the Income Tax Act, 1961 are separately initiated."

19. On appeal, the Dispute Resolution Panel held as under:

"It is mentioned in the AO's order that this issue is pending before the ITAT in earlier years. In such circumstances, we refrain from issuing any directions on the issue. The AO should follow the decision of the higher appellate authorities."

20. The Authorized Representative of the assessee filed before us copy of the order of this Tribunal in the case of the assessee itself for Assessment Year 2005-06 dated 12.11.2013 passed in ITA No. 1842/Ahd/2010 and submitted that in that order, the Tribunal has restored the matter back to the file of the Assessing Officer and following the same in this year also, the issue should be restored back to the file of the Assessing Officer for adjudication afresh as per the same directions as given in the Assessment Year 2005-06.

21. The Departmental Representative had no objection to the above submission of the Authorized Representative of the assessee

22. We find that the Tribunal in the Assessment Year 2005-06 in the case of the assessee itself vide order dated 12.11.2013 passed in ITA No. 1842/Ahd/2010 restored the matter back to the file of the Assessing Officer by observing as under:

"5. After hearing both the sides and carefully perusing the materials on record, we are of the considered view that the Id. AO is right in its rim to examine the agreements entered between the assessee company and its customers for determining the nature of transaction. It is the primary duty of the assessee to furnish all such agreements if

required by the Revenue. In this instant case, the assessee has failed to do so in spite of the repeated requests made by the Id. AO. Therefore, in the interest of justice, we remit the issue back to the file of Id. AO for the limited purpose of examining these agreements. Further we make it clear that if the Id. AO arrives at a conclusion that the ownership of the asset is not transferred to customers of the assessee, then the assessee is entitled to claim the benefit of the depreciation under section 32 of the Act and the ld. Assessing Officer shall pass orders accordingly. Thus, this ground raised by the Revenue is remitted back to the file of the ld. Assessing Officer to pass appropriate order as indicated hereinabove."

As the facts in the present year of appeal are also the same, therefore we set aside the orders of the lower authorities and remand the matter back to the file of the Assessing Officer to adjudicate the issue afresh in the line of the directions given by the Tribunal in Assessment Year 2005-06 as quoted above. Thus, these grounds of appeal are allowed for statistical purpose.

23. Ground nos. 11 & 12 are directed against the order of Dispute Resolution Panel confirming the order of the Assessing Officer disallowing the claim of Rs 4,12,609/- on provision of sick leave u/s. 43B.

24. The Assessing Officer observed as under:

"During the year under consideration, the assessee has debited an amount of Rs 4,12,609/- being provisions for sick leave.

The assessee was asked to justify the claim of such vis-à-vis section 43B or 37(1) of the Act. The assessee was apprised with the provisions of section 43B of the Act.

The provisions of section 43B of sub clause (f) envisages that any sum payable by the assessee as an employer in lieu of any leave at the credit of his employee shall only be allowed on actual payment.

The submission of the assessee on this point reads as under:

> *"In respect of provisions for sick leave to the tune of RS 4,12,609/- during the year under consideration based on valuation report, we wish to submit that the same is in accordance with and to comply with Accounting Standard-15 "Employee Benefits". Through inadvertence, the same is mentioned as Retirement Benefits in the last submission. We further wish to submit that ours is a listed company and*

compliance of accounting standard is mandatory. Non-compliance of the said accounting standard could lead to qualification of the Auditors as well as breach of Company Law requirements as to disclosure of true and fair view to shareholders. It is further submitted that the valuation is done on scientific basis and by the Actuary, who is expert in the field."

The reply of the assessee is perused but it is not acceptable. The provision of sick leave is in the benefit of the employee. The acturial valuation of SL (sick leave) Encashment is based on financial assumption such as salary which would be accrued to the employee at the time of encashment/availment. Liability to pay such leave is based on the salary which the employee will be drawing at the time of exit. The Consultant and Actuaries of the assessee has considered all these parameters and assumptions in his report dated 01.04.2009 which is furnished by the assessee. Hence, the assessee had consciously mentioned as "Retirement Benefits" in the earlier submission and it was not in advertence. Therefore, in view of the provisions of section 43B of the Act, provision of RS 4,12,609 on account of sick leave is disallowed and added back to the total income of the assessee.

The assessee has raised the objection before the Dispute Resolution Panel (DRP), against this addition also. The ld. DRP vide his direction dated 26.09.2012 held that if the amount was actually paid in the subsequent year, then the assessee's claim may be allowed this year if the same has not been allowed in the year of payment. However, if it is found that no such payments were actually made even in the next two or three years, then no deduction needs to be allowed for the provisions made for the future contingent liabilities.

On verification of records, it is found that no detail has been submitted by the assessee which shows that the alleged amount has been actually paid in the subsequent year also. Therefore, no deduction has been allowed to the assessee in view of the provisions of section 43B of the Act and provision of RS 4,12,609/- on account of sick leave is disallowed and added back to the total income of the assessee."

25. On appeal, the Dispute Resolution Panel held as under:

"*The assessee made provision for sick leave to the tune of Rs 4,12,609/- based on valuation report. The assessee further argued that the same is in accordance with and to comply with Accounting Standard-15 "Employee Benefits". The valuation is claimed to be based on scientific basis and by the Actuary, who is expert in the field.*

The TPO disallowed the same under section 43B. We direct the TPO to verify whether the amount was actually paid in the subsequent years. If so, then the assessee's claim may be allowed this year if the same has not been allowed in the year of payment. However, if it is found

that no such payments were actually made even in the next two or three yeas, then no deduction needs to be allowed for the provision made for the future contingent liabilities."

26. Before us, the assessee submitted that Section 43B(f) is not valid for provision of leave encashment since the same is not a statutory liability. In support of its submission, the assessee quoted the following judgements:

1. Exide Industries Limited & Anr. v. Union of India & Ors. (2007) 212 CTR 206 (Cal)
2. Eimco Elecon (India) Ltd. v. ACIT (2013) 22 ITR (Trib.) 380 (Ahd)

27. We have heard the rival submissions and perused the orders of lower authorities and material available on record. In the instant case, the deduction claimed in respect of provision made for sick leave of Rs 4,12,609/- was disallowed by the Assessing Officer by invoking the provisions of section 43B (f) of the Act.

28. On appeal, the Dispute Resolution Panel held as under:

"*The assessee made provision for sick leave to the tune of Rs 4,12,609/- based on valuation report. The assessee further argued that the same is in accordance with and to comply with Accounting Standard-15 "Employee Benefits". The valuation is claimed to be based on scientific basis and by the Actuary, who is expert in the field.*

The TPO disallowed the same under section 43B. We direct the TPO to verify whether the amount was actually paid in the subsequent years. If so, then the assessee's claim may be allowed this year if the same has not been allowed in the year of payment. However, if it is found that no such payments were actually made even in the next two or three yeas, then no deduction needs to be allowed for the provision made for the future contingent liabilities."

29. We find that this Tribunal in the case of Eimco Elecon (India) Ltd. v. ACIT (2013) 22 ITR (Trib.) 380 (Ahd) held as under:

"3.1 It was submitted by the Ld. Authorized Representative of the assessee that the disallowance was made by the A.O. by invoking the provisions of clause (f) of Section 43B. He submitted that as per the decision of Hon'ble Apex Court rendered in the case of Bharat Earth Movers as reported in 241 ITR 428 and also as per the judgment of Hon'ble Calcutta High Court rendered in the case of Exide Industries Ltd. and Another Vs. UOI and Others as reported in 292 ITR 470 (Cal.), disallowance of leave encashment is not justified. He submitted that in the first case, it was held by the Hon'ble Apex Court that leave encashment is not a contingent liability if the provision is made on some scientific basis. He also submitted that in the second case, Hon'ble Calcutta High Court has duly considered the provisions of clause (f) of Section 43B and it was held that the amendment as per which this clause (f) was inserted by the Finance Act 2001 w.e.f. 01.04.2002 is held to be as arbitrary by Hon'ble Calcutta High Court and, therefore, the same was struck down by Hon'ble Calcutta High Court being arbitrary, unconscionable and dehors the Hon'ble Supreme Court's decision. He submitted that in view of this judgment of Hon'ble Calcutta High Court, disallowance made by the A.O. is not justified. Ld. D.R. supported the orders of authorities below.

3.2 We have considered the rival submissions, perused the material on record and have gone through the orders of authorities below and the judgment of Hon'ble Calcutta High Court rendered in the case of Exide Industries Ltd. (supra). We find that the A.O. has made disallowance by invoking the provisions of clause (f) of Section 43B and the same was confirmed by Ld. CIT (A) also on the basis of Section 43B. As per the judgment of Hon'ble Calcutta High Court rendered in the case of Exide Industries Ltd. (supra), it was held that clause (f) of Section 43B is arbitrary, unconscionable and dehors of the Hon'ble Supreme Court decision, and therefore, not valid. In view of this, clause (f) of Section 43B is not valid and, therefore, disallowance made by the A.O. on the basis of clause (f) of Section 43B cannot be sustained. We therefore delete the same."

30. The Departmental Representative could not point out any good reason as to why the aforesaid decision of the Tribunal should not be followed in the instant case. We, therefore, following the above quoted decision of the Tribunal delete the disallowance of Rs 4,12,906/- for the reasons mentioned in the above quoted decision. Thus, this ground of the appeal of the assessee is allowed.

31. The assessee has also raised additional grounds of appeal which read as under:

Ground No. 13

On the facts and in the circumstances of the case and in law, without prejudice to the earlier grounds, the Appellant prays that the adjustment, if any, be restricted to the value of the controlled transactions and not on total transactions (i.e. controlled as well as uncontrolled transactions).

Ground No. 14

On the facts and in the circumstances of the case and in law, without prejudice to the earlier grounds, the Appellant prays that alternatively, overall Gross Profit Margin ('GPM') earned by the Appellant should be considered for benchmarking the international transactions entered into by the Appellant during the year under consideration.

At the time of hearing, the Authorized Representative of the assessee did not make any submission in respect of above grounds. Hence, the same are dismissed for want of prosecution.

32. No other point was argued or pressed by the Authorized Representative of the assessee.

33. In the result, the appeal of the assessee is partly allowed in the manner indicated above.

Order pronounced in the Court on Friday, the 19th of September, 2014 at Ahmedabad.

Sd/-	**Sd/-**
(G.C. GUPTA)	**(N.S. SAINI)**
JUDICIAL MEMBER	**ACCOUNTANT MEMBER**

Ahmedabad; Dated 19/9/2014
Ghanshyam Maurya, Sr. P.S.

TRUE COPY

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. संबंधित आयकर आयुक्त / Concerned CIT
4. आयकर आयुक्त(अपील) / The CIT(A)-III, Ahmedabad
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, अहमदाबाद / DR, ITAT, Ahmedabad
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

उप/सहायक पंजीकार (Dy./Asstt.Registrar)
आयकर अपीलीय अधिकरण, अहमदाबाद / ITAT, Ahmedabad