

**IN THE INCOME TAX APPELLATE TRIBUNAL  
PUNE BENCH "B", PUNE**

**BEFORE SHRI G.S. PANNU, ACCOUNTANT MEMBER  
AND Ms. SUSHMA CHOWLA, JUDICIAL MEMBER**

**ITA No.1616/PN/2011  
(Assessment Year: 2005-06)**

Cummins India Limited,  
35A/1/2, Erandawana,  
Pune – 411038

PAN: AAACC7262K .... Appellant

Vs.

The Addl. Commissioner of Income Tax  
Range – 1, Pune .... Respondent

Appellant by : Shri Arvind Sonde  
Respondent by : Shri Mazhar Akram

Date of hearing : 20-10-2014  
Date of pronouncement : 31-12-2014

**ORDER**

**PER SUSHMA CHOWLA, JM:**

This appeal filed by the assessee is against the order of CIT(A)-I, Pune dated 25.02.2011 relating to assessment year 2005-06 passed under section 143(3) of the Income-tax Act.

2. The assessee has raised the following grounds of appeal:

1.1 *On the facts of the case and in law, the learned Commissioner of Income Tax (Appeals) - I, Pune erred in confirming the disallowance u/s.14A to the extent of Rs. 4,47,010/-.*

1.2 *He erred in not appreciating that there was no dominant and immediate connection between the expenditure incurred and exempted income and therefore there cannot be any adhoc disallowance out of general expenses. He erred in not following the ratio of the following decisions :*

(a) *CIT v Hero Cycles Ltd (2010) 323 ITR 518 (P & H)*

(b) *CIT v Printers House (P.) Ltd (2010) 188 Taxman 70 (Delhi)*

(c) *ITO v M/s. Daga Capital Management Pvt. Ltd. (SB- Mum ITAT)*

(d) *CIT v General Insurance Corporation of India (2002) 254 ITR 203 (Bom.)*

(e) *CIT v BSES Ltd. (2008) 113 TTJ 227 (Mum.)*

(f) *Space Financial Services v ACIT (2008) 115 TTJ 165 (Del.)*

- 1.3 *The learned Commissioner of Income Tax (Appeals) -I, Pune erred in not following the decision of Pune bench of ITAT in the case of Appellant Company for Assessment year 2004-05 where the ITAT has deleted such ad-hoc disallowance made by the learned Assessing Officer.*
- 2.1 *The learned Commissioner of Income Tax (Appeals) -I, Pune erred in law and on the facts of the case in confirming the adjustment amounting to Rs.22.49 lakhs to the value of international transactions entered into by the Appellant with its Associated Enterprises pertaining to export of components and spares disregarding the benchmarking of international transactions using the "aggregation of transaction" approach followed by the Appellant using third party comparable companies.*
- 2.2 *Further, the learned Commissioner of Income Tax (Appeals) I, Pune erred in law and on the facts and in circumstances of the case in comparing segmental profitability of the Appellant i.e. between "export to AEs" segment and "export to third party" segment ignoring the various comparability factors.*
- 2.3 *The learned Commissioner of Income Tax (Appeals) -I, Pune erred in law and on the facts and in circumstances of the case in not granting benefit of +/- 5 percent range from the price computed based on arithmetic mean as provided in proviso to Section 92C(2) of the Act.*
3. *The Appellant Company craves leave to add to, alter, amend, modify and / or delete any or all of the above Grounds of Appeal.*

3. The present appeal was filed by the assessee on 13.12.2011 whereas the due date for filing the appeal was 09.12.2011. The assessee has made an application for condonation of delay in filing the appeal after a delay of 3 days. The reason for non-filing the appeal in time was the inadvertent delay in payment of appeal fee before the prescribed date. Prayer was made to condone the delay in filing the appeal belatedly. In the facts and circumstances, we find merit in the plea of the assessee and we condone the delay of 3 days in filing the

appeal late before us and proceed to decide the appeal after hearing both the parties.

4. The issue raised vide ground of appeal No.1 is against the disallowance of Rs.4,47,010/- under section 14A of the Act.

5. The brief facts relating to the issue are that, during the year under consideration, the assessee had received interest on dividends of Rs.46,75,002/- which was claimed as exempt under sections 10(15), 10(34) / 10(35) of the Act. During the course of assessment proceedings, the assessee was asked to explain as to why proportionate disallowance under section 14A of the Act should not be made. In reply, the assessee claimed that assessee company was having share capital and reserves & surpluses of Rs.101 crores as on 31.03.2005 as against unsecured loans of Rs.64 crores only. Further, it had no secured loans and therefore, the investments in tax free assets were claimed to have been made from own funds of the company. The Assessing Officer observed that no disallowance out of interest costs had to be made. However, as the assessee had incurred certain administrative expenses, it was held that certain disallowance is to be made out of the general and administrative expenses. Applying the provisions of Rule 8D(iii) of the Income Tax Rules, 1962, sum of Rs.8,94,020/- was disallowed under section 14A of the Act.

6. The CIT(A) applying the ratio laid down by the Hon'ble Bombay High Court in Godrej Boyce Manufacturing Co. Ltd. Vs. CIT (2010) 234 CTR 1 (Bom), held that disallowance made by the Assessing Officer of Rs.8,94,020/- be reduced by 50%.

7. The assessee is in appeal against the order of CIT(A).

8. The learned Authorized Representative for the assessee pointed out that no disallowance was warranted in the case. Further, reliance was placed on the ratio laid down by Delhi Bench of the Tribunal in Interglobe Enterprises Ltd. Vs. DCIT in ITA No.1362 & 1032/Del/2013 and in ITANo.1580/Del/2013, order dated 04.04.2014.

9. The learned Departmental Representative for the Revenue pointed out that the provisions of Rule 8D are applicable and hence the disallowance made by the Assessing Officer needs to be upheld.

10. We have heard the rival contentions and perused the record. The assessee during the year under consideration had received dividend of Rs.46,75,002/- which was declared as exempt. The contention of the assessee that no direct financial cost was attributable to such investments was accepted by the Assessing Officer and no disallowance in this regard was made. However, disallowance under Rule 8D(iii) of the Rules was made on account of administrative and general expenses expanded by the assessee. The Assessing Officer had applied the provisions of Rule 8D(iii) of the Rules in order to compute the said disallowance. However, the CIT(A) had reduced the said disallowance by deleting 50% of the disallowance made by the Assessing Officer. The captioned assessment year in appeal is assessment year 2005-06. As held by various High Courts, the provisions of Rule 8D of the Rules were introduced w.e.f. 01.04.2008 are not applicable to the years prior to the said insertion. However, the Hon'ble Bombay High Court in Godrej Boyce Manufacturing Co. Ltd. Vs. CIT (supra) had elaborately considered the issue of applicability of the provisions of Rule 8D of the Rules to the years prior to 01.04.2008 and it was held that proportionate disallowance out of administrative and personnel expenses may be made, keeping in mind

the facts of the case. In view thereof, we direct the disallowance of Rs.2 lakhs out of administrative expenses. The ground of appeal No.1 raised by the assessee is partly allowed.

11. The issue in ground of appeal No.2 raised by the assessee is against the transfer pricing adjustment of Rs.22.49 lakhs.

12. The brief facts relating to the issue are that, the assessee company was dealing in the business of sale of spares and after sales service of engine manufactured and sold by M/s. Cummins India Ltd. For the year under consideration, the assessee had furnished the return of income declaring total income of Rs.46,06,31,680/-. The Assessing Officer made a reference under section 92CA(1) of the Act for computation of arm's length price in relation to the international transactions as detailed in audit report in Form No.3CEB. The Transfer Pricing Officer (in short TPO) issued a questionnaire to the assessee requisitioning the assessee to furnish the details / explanations in support of the arm's length price computed by it in the audit report in Form No.3CEB. Cummins India Ltd. holds 99.95% of the equity share capital of the assessee company. The parent company Cummins India Ltd. in turn, 51% was held by Cummins (INC, USA), which was the leading designer and manufacturer of diesel engines from 55 to 350 HP. The said company was listed in USA and was operating through its subsidiaries and joint venture companies in different parts of the world. The assessee was engaged in distribution / sale of Cummins after sales products i.e. spares through its network of dealers throughout India, Nepal and Bhutan. It also provided overhauling job work services, reconditioning services and operations and maintenance services for IC engines sold by Cummins India Ltd. During the year, the TPO noted that the assessee had entered into the

following international transactions which were reported in Form No.3CEB.

Sr No.	International Transaction	Amount Rs.	Method adopted
1	Import of components & spares of IC engines	29,45,48,522	Transactional Net Margin Method
2	Export of components & spares of IC engines	87,48,479	Transactional Net Margin Method
3	Receipt of services, such, access to customized parts catalogues, international site license, annual subscription charge, etc.	2,43,127	Transactional Net Margin Method
4	Receipt of IT support services	1,09,20,790	Transactional Net Margin Method
5	Payment of training fees	94,235	Transactional Net Margin Method
6	Rendering of services - warranty claims lodged with Associated Enterprises	76,55,292	Transactional Net Margin Method
7	Provision of technical services	3,29,017	Transactional Net Margin Method

13. The assessee had determined the arm's length price by using Transactional Net Margin Method by considering the operating margins on net sales as Profit Level Indicator in its TP study. The TPO issued a show cause notice to the assessee which is reproduced under para 7 on pages 3 to 5 of the TPO order. The objection of the TPO was that the assessee had aggregated its different international transactions which were distinguishable in their nature and scope and further, the transactions were such, where separate profitability in respect of the transactions could be arrived at, if an attempt was made. The TPO further observed that the aggregation or grouping of the various international transactions undertaken by the assessee and benchmarking them under the umbrella of TNMM was not acceptable and a proposal was made for making the following adjustments to international transactions relating to export of bought out spares:-

“During the year under consideration it is seen that the assessee has exported bought out spares to AEs for Rs.87.49 lakhs against which the assessee has earned profit before taxation to sales at 28.83%. Assessee has also exported the spares to the third parties against which the company has earned profit before taxation, to sales at 54.54%. It is clear from these figures that

assessee has earned less by a profit margin of 25.71% in case of exports to AEs. It is accordingly requested to show cause as to why adjustments of an amount corresponding to the difference in the margins from exports to third parties and exports to Associated Enterprises as indicated above, be not made to the international transactions relating to export of bought out spares of IC Engines to the AEs.”

14. In reply, the assessee objected to the proposal made by the Assessing Officer as the said proposed comparison would not provide accurate results. The reply of the assessee is summarized under para 8 at pages 5 to 7 of the TPO order. The TPO dismissed the submissions of the assessee because the assessee company had exported variety of spares to its AEs as well as to third parties. As per the TPO, the adjustment proposed was on the basis of internal TNMM method and not by adopting Comparable Uncontrolled Price (CUP). In the case of the assessee, it was noted by the Assessing Officer that what had been sold to associated enterprises and third parties outside India were the spares of IC engines, which were bought out by the assessee. It was thus, held that assessee's international transaction was one of trading and was being proposed to be compared with the trading of similar item with third parties. The TPO further held that with reference to Rule 10B and OECD Guidelines at para 1.19, the assessee had contended that specific characteristics of the property transferred or the services provided were the key factors to be considered for examining the comparability. The TPO held that what had been transferred was the property in the shape of spares to the associated enterprises and also to the third parties and they remained the same and there was no difference as far as specific characters of the property transferred was concerned. It was further observed that there might have been difference in the total quantum of exports to third parties and to the associated enterprises, but that itself would not change the specific characters distinct of the transactions. The

plea of the assessee that the exports to third parties were made at premium was rejected in the absence of complete details not being available. Further, the TPO noted that the quantum of exports of spares was about Rs.90 lakhs as compared to the total turnover of the assessee at Rs.430 crores. The TPO thus, held that the exports to associated enterprises and third parties were nothing but need based purchases by associated enterprises and third parties and basic characteristic of the transaction were identical. It was further contention of the TPO that if the assessee contends to have charged premium to third parties, then the same should have been charged to the associated enterprises as well. The second contention of the assessee with reference to the Rule 10B of the I.T. Rules in respect of the difference and geographical location size of the market, government orders in force, etc. was rejected by the Transfer Pricing Officer in the absence of the assessee having furnished complete facts and figures in that regard. The method adopted by the assessee of clubbing the transactions and then applying TNMM method at the entity level was rejected by TPO for the reason that the Indian Transfer Pricing Regulations as well as OECD Guidelines have provided for clubbing of transactions only under certain circumstances. As the assessee had failed to separately benchmark its transactions relating to export of spares to its associated enterprises, the TPO held that the assessee had failed to discharge its primary onus of proving the international transactions to be at arm's length price. The Assessing Officer in view thereof, was of the view that *accordingly adjustment as proposed in the show cause notice corresponding to the difference in the profit earned before taxation to sales at 54.54% in case of the third parties and that earned at 28.83% in case of the AEs which comes to 25.71%, calculated on the value of total exports to AEs at Rs.87.49*

*lakhs is made to the international transactions relating to export of part of the spares of I.C. engines to AEs.* The TPO thus proposed the adjustment at Rs.22.49 lakhs in relation to the export of bought out spares of IC engines to AEs. The Assessing Officer applied the recommendations of the TPO and made an addition of Rs.22.49 lakhs to the transaction value of export of spare parts of IC engines, while framing the assessment order under section 143(3) of the Act.

15. The CIT(A) after considering the reply of the assessee which is reproduced under para 4.2 at pages 16 to 24 of the appellate order observed that there was no merit in the plea of the assessee that no adjustment on this account had been made in the earlier years even though case of the assessee was subjected to transfer pricing since assessment year 2002-03. The next objection of the assessee relating to rejection of aggregation method applied for benchmarking, the CIT(A) upheld the observations of the TPO to be more appropriate. Another objection of the assessee before the CIT(A) was that the TPO had no basis or reason for rejecting the external TNMM adopted by the assessee. The CIT(A) held that where exports to associated enterprises was not a regular activity but was as per the business exigency of the group company, it was important to look at the third party uncontrolled transactions available internally before looking for such transactions outside internal ambit. The CIT(A) further held that the internal TNMM method was more appropriate comparable as the same would be nearest in characteristics. As per the CIT(A), internal TNMM method had to be first given preference. The next objection of the assessee was that two comparables adopted by the TPO without any specific characteristics was found to be not only not based on Indian Transfer Pricing guidelines but mis-conceived and without any basis.

Further, the argument of the assessee on difference in risks and geographical locations was theoretical in nature per the CIT(A), could not be accepted. The order of the TPO / AO was thus, upheld by the CIT(A).

16. The assessee is in appeal against the order of CIT(A).

17. The learned Authorized Representative for the assessee pointed out that the assessee was a distributor / trading company and was engaged in the sale of spare parts i.e. the components of diesel engines sold by M/s. Cummins India Ltd. It was further pointed out by the learned Authorized Representative for the assessee that the assessee was the local supplier for components and was also selling spare parts to the companies, who had purchased products from M/s. Cummins India Ltd. The learned Authorized Representative for the assessee pointed out that the assessee had entered into various international transactions and in the TP study, transaction at serial No.1, 2, 3, 4 and 6 i.e. except the payment for training services and amounts received for technical services were considered as one segment which was the sourcing activity which in turn, was linked to assessee's trading activity. It was further stated by the learned Authorized Representative for the assessee that the total turnover of the assessee company for the year under consideration was Rs.430 crores, out of which Rs.32 crores was the related party transaction. The TPO disregarded the international transactions grouped together by the assessee in its TP study and picked up only export of spare parts at Rs.0.87 crores for benchmarking international transactions. It was pointed out by the learned Authorized Representative for the assessee that the TPO compared the profitability on export of spare parts of Rs.0.87 crores i.e. one of the activities undertaken by the assessee and

compared the results with direct sales to non-AEs of Rs.4 lakhs and applied the said rate of profit, for working out the adjustments, whether the same were at arm's length price or not. The plea of the learned Authorized Representative for the assessee before us was that the assessee was engaged in integrated activity having inter-linked transactions. Our attention was drawn to the TP report placed at pages 75 to 182 of the Paper Book and it was pointed out by the learned Authorized Representative for the assessee that the activities of the assessee were for aftermarket support of internal combustion engines in the form of spare parts supports and also, for rendering after sales service. For carrying out the aftermarket support for the IC engines sold by Cummins India Ltd. and other Cummins entities, the assessee was engaged in sale of spare parts, administration, reconditioning services for Cummins engines sold and also for the training programmes and publishing various types of literatures to its customers in using the Cummins engines. Our attention further was drawn to the FAR analysis carried out in the TP study which is placed at pages 101 onwards of the Paper Book and as per the learned Authorized Representative for the assessee, sourcing activity was integrated and inter-linked activity. The learned Authorized Representative for the assessee further pointed out that for the said sourcing activity, comparable companies search was carried out and by using the prowess data base, TNMM method was applied to the operating profits and total turnover which is 2.13% over 15.8%. The learned Authorized Representative for the assessee thereafter, took us through the communication with the TPO placed at pages 188 onwards and the reply of the assessee thereafter and pointed out that the total exports to the associated enterprises were at Rs.87,48,479/- as against the exports to third parties during the year at Rs.4,16,326/-

After carrying out the said analysis, it was reported by the assessee company that in view of the volume of transactions and the variety of items exported, the management of the company was of the view that it was not feasible to disclose quantitative details in respect of export of IC engine spare parts to the associated enterprises. The said note was appended and is part of an Appendix-I to the submissions made to the TPO and placed at pages 200 to 204 of the Paper Book.

18. The learned Authorized Representative for the assessee then referred to the information sought by the TPO in respect of segmental Profit & Loss Account from exports made by the assessee to associated enterprises and non-associated enterprises and in this regard, it was pointed out that there was significant variation in the exports to the third parties and to the associated enterprises and also the spare parts exported to third parties and associated enterprises were different in nature. Further, the exports were made to the third parties on urgent basis and there was a premium price attached to it. The plea of the assessee before the TPO was that the said comparison would not provide any results as economic value of the transactions, risk involved were different. The learned Authorized Representative for the assessee referred to the submissions placed at pages 271 to 280 of the Paper Book and pointed out that the TPO on the other hand picked up the figures of export sales and applied the percentage of profit on sales to third parties to work out arm's length price. It was further pointed out by the learned Authorized Representative for the assessee that the export of spare parts and payments made for IT support received from associated enterprises facilitate the assessee's business of both import and export of spare parts.

19. Another objection raised by the learned Authorized Representative for the assessee was that though the Assessing Officer dis-agreed on aggregation of transactions but the Assessing Officer has not disturbed the TNMM analysis but has disturbed the aggregation of transactions. The learned Authorized Representative for the assessee stated that both in the earlier years and in the subsequent years, same principle of aggregation had been accepted by the TPO and no adjustment had been made on account of arm's length price. Further, reliance was placed on the following decisions:-

1. Demag Cranes & Components (India) Pvt. Ltd. Vs. DCIT in ITA No.1683/PN/2011;
2. M/s. Panasonic India Pvt. Ltd. Vs. ITO in ITA No.1417/Del/2008 and another; and
3. M/s. Intimate Fashions (India) Pvt. Ltd. Vs. ACIT in ITA Nos.2116/Mds/2010 & 2108/Mds/2011.

20. The learned Departmental Representative for the Revenue in response placing reliance on the orders of authorities below pointed out that the assessee was engaged in trading of spares and out of total turnover of 4 billion exported to associated enterprises was not main business of the assessee. Since it was not regular business of the assessee, going on the basis of OCED guidelines, the TPO segregated the activities and applied the percentage which needs to be upheld.

21. We have heard the rival contentions and perused the record.

22. The assessee was engaged in the aftermarket support for IC engines sold by Cummins entities. The activities of the assessee company consisted of customer support through sale of spare parts of Cummins Engines, of Cummins products manufactured worldwide and also by Cummins India Ltd. The assessee claimed that it has nationwide network of 5 Zones, 6 Regional and 14 area offices and

over 90 dealers and 7 parts depots. The assessee warranties for the spare parts. Another line of activity was that the assessee provided other services which included annual maintenance contracts and publication of literature in relation to the said Cummins Engines sold by the Cummins entities. Further, every IC engine sold by Cummins India Ltd. was communicated to the assessee by way of engine dispatch advice and on receipt, the assessee company warrants the products by agreeing to provide 4 free services for a period of two years. Out of the various activities carried on by the assessee, trading of spare parts constitute one of the main activities of the assessee. The international transactions were claimed by the assessee to consist of import of spare parts from the associated enterprises and other transactions including export of spare parts, provision of warranty administration, other services to, and receipt from various services from the associated enterprises. The assessee was thus, engaged in providing services both to the parties in India and to its associated enterprises. The assessee claims that in its export of spare parts to the dealers outside India, the transaction was through associated enterprises which in turn, transacts with the dealers who in eventuality feed the consumers. However, in the sales to third parties, direct sales were being made to the consumers. The assessee during the year under consideration had entered into various international transactions with its associated enterprises which were as under:-

Sr No.	International Transaction	Amount Rs.	Method adopted
1	Import of components & spares of IC engines	29,45,48,522	Transactional Net Margin Method
2	Export of components & spares of IC engines	87,48,479	Transactional Net Margin Method
3	Receipt of services, such, access to customized parts catalogues, international site license, annual subscription charge, etc.	2,43,127	Transactional Net Margin Method
4	Receipt of IT support services	1,09,20,790	Transactional Net Margin Method

5	Payment of training fees	94,235	Transactional Net Margin Method
6	Rendering of services - warranty claims lodged with Associated Enterprises	76,55,292	Transactional Net Margin Method
7	Provision of technical services	3,29,017	Transactional Net Margin Method

23. The assessee applied TNMM method to benchmark its international transactions by aggregating its different international transactions except item Nos.5 and 7, claiming that the said transactions were source activities. While applying the TNMM method, the assessee searched for external comparable companies. The assessee applied operating margins on net sales as Profit Level Indicator in its TP study. The TPO objected to the aggregation of the different international transactions which as per him were distinguishable in their nature and scope and further, the transactions were searched with separate profitability in respect of each of the transactions. The TPO thus, rejected the aggregation of the various international transactions undertaken by the assessee and also held that the benchmarking the said transaction under the umbrella of TNMM was not acceptable. The TPO thereafter, noted that the assessee had exported bought out spares to its associated enterprises and had also exported the spares to third parties against which, it had earned higher profits. The TPO was of the view that adjustments had to be made on account of difference in the margins from exports to third parties as compared to exports to associated enterprises. The TPO thus, applied internal TNMM method and worked out the arm's length price of the international transactions resulting in adjustment of Rs.22.49 lakhs in relation to export of bought out spares of IC engines to its associated enterprises. The said addition was applied by the Assessing Officer and upheld by the CIT(A).

24. The first issue arising in the present appeal is whether in view of the OECD guidelines and the Indian Transfer Pricing provisions, aggregation of transactions could be made or not. We find that Pune Bench of the Tribunal in Demag Cranes & Components (India) Pvt. Ltd. Vs. DCIT (supra) had elaborately considered the OECD guidelines under Chapter – III and also the guidance Notes issued by the Institute of Chartered Accountants of India on transfer pricing in para 13.7 and had held as under:-

*“30. We have carefully considered the rival submissions. Section 92B of the Act provides the meaning of expression “international transaction” as a transaction between two or more associated enterprises. Rule 10A(d) of the Rules explains the meaning of the expression “transaction” for the purposes of computation of ALP as to include a number of closely linked transactions. Rule 10B of the Rules prescribes the manner in which the ALP in relation to an international transaction is to be determined by following any of the methods prescribed. Shorn of other details, it would suffice to observe that on a combined reading of Rule 10A(d) and 10B of the Rules, a number of transactions can be aggregated and construed as a single ‘transaction’ for the purposes of determining the ALP, provided of course that such transactions are ‘closely linked’. Ostensibly the rationale of aggregating ‘closely linked’ transactions to facilitate determination of ALP envisaged a situation where it would be inappropriate to analyse the transactions individually. The proposition that a number of individual transactions can be aggregated and construed as a composite transaction in order to compute ALP also finds an echo in the OECD guidelines under Chapter III wherein the following extract is relevant:-*

*“Ideally, in order to arrive at the most precise approximation of arm’s length conditions, the arm’s length principle should be applied on a transaction-by-transaction basis. However, there are often situations where separate transactions are so closely linked or continuous that they cannot be evaluated adequately on a separate basis. Examples may include 1. Some long term contracts for the supply of commodities or services; 2. Rights to use intangible property; and 3. Pricing a range of closely linked products (e.g. in a product line) when it is impractical to determine pricing for each individual product or transaction. Another example would be the licensing of manufacturing know-how and the supply of vital components to an associated manufacturer; it may be more reasonable to access the arm’s length terms for the two items together rather than individually. Such transactions should be evaluated together using the most appropriate arm’s length method. A further example would be the routing of a transaction through another associated enterprise; it may be more appropriate to consider the transaction of which the routing*

*is a part in its entirety, rather than consider the individual transactions on a separate basis."*

31. In this background, considering the legislative intent manifested by way of Rule 10A(d) read with Rule 10B of the Rules, it clearly emerges that in appropriate circumstances where closely linked transactions exist, the same should be treated as one composite transaction and a common transfer pricing analysis be performed for such transactions by adopting the most appropriate method. In other words, in a given case where a number of closely linked transactions are sought to be aggregated for the purposes of benchmarking with comparable uncontrolled transactions, such an approach can be said to be well established in the transfer pricing regulation having regard to Rule 10A(d) of the Rules. Though it is not feasible to define the parameters in a water tight compartment as to what transactions can be considered as 'closely linked', since the same would depend on facts and circumstances of each case. So however, as per an example noted by the Institute of Chartered Accountants of India (in short the 'ICAI') in its Guidance Notes on transfer pricing in para 13.7, it is stated that two or more transactions can be said to be 'closely linked', if they emanate from a common source, being an order or contract or an agreement or an arrangement, and the nature, characteristic and terms of such transactions substantially flow from the said common source. The following extract from the said Guidance Notes is worthy of notice:-

*"13.7 The factors referred to above are to be applied cumulatively in selecting the most appropriate method. The reference therein to the terms 'best suited' and 'most reliable measure' indicates that the most appropriate method will have to be selected after a meticulous appraisal of the facts and circumstances of the international transaction. Further, the selection of the most appropriate method shall be for each particular international transaction. The term 'transaction' itself is defined in rule 10A(d) to include a number of closely linked transactions. Therefore, though the reference is to apply the most appropriate method to each particular transaction, keeping in view, the definition of the term 'transaction', the most appropriate method may be chosen for a group of closely linked transactions Two or more transactions can be said to be linked when these transactions emanate from a common source being an order or a contract or an agreement or an arrangement and the nature, characteristics and terms of these transactions are substantially flowing from the said common source. For example, a master purchase order is issued stating the various terms and conditions and subsequently individuals orders are released for specific quantities. The various purchase transactions are closely linked transactions.*

*13.8 It may be noted that in order to be closely linked transactions, it is not necessary that the transactions need be identical or even similar. For example, a collaboration agreement may provide for import of raw materials, sale of finished goods, provision of technical services and payment of royalty. Different methods may be chosen as the most*

*appropriate methods for each of the above transactions when considered on a standalone basis. However, under particular circumstances, one single method maybe chosen as the most appropriate method covering all the above transactions as the same are closely linked.” (Underlined for emphasis by us).*

32. In this background, we may now examine the facts of the present case. The primary activity of the assessee is to manufacture material handling equipments viz. cranes and hoists. It is seen from the documents placed in the Paper Book that the assessee enters into a single negotiation with the customers, which, inter-alia, includes manufacturing and supply of the material handling equipment, provision of commissioning and installation services, etc. Though the assessee raises different invoices for supply of equipments and separately for erection and commissioning charges, however, it is evident that the negotiations for the same are carried on at one go. In fact, at the time of hearing, it was specifically queried from the learned counsel as to whether the assessee is undertaking installation/commissioning activities independent of its own-supplied material handling equipments. It was clarified that the servicing and commissioning charges are earned only in relation to services performed for own-supplied manufacture/assembled material handling equipments. The aforesaid factual assertion is not disputed. Factually, it is the activity of manufacturing/assembling of cranes etc. done by the assessee and sales thereof, which brings into play the activities of installation and commissioning of such products. Therefore, it is quite evident that such services are not independent but in-effect are as a result of manufacturing of material handling equipment undertaken by the assessee and as they arise from a single negotiation with the customers, the source of all such transactions is also to be understood as common.

33. The TPO in this regard has observed that assessee has invoiced separately for such activities and therefore, they have to be understood as different transactions. The TPO has also observed in his order that in a case where profits of each individual transaction can be segregated then the aggregation of transaction is not intended by the transfer pricing regulations. The learned TPO has also referred to the segmental profitability in this regard computed by the assessee during the course of transfer pricing proceedings before him. In our considered opinion, the point made out by the learned TPO is not justified, inasmuch as, separate invoicing of an activity, flowing from a singular contract/negotiation, would not ipso facto lead to an inference that they are individual/independent transactions. In-fact, it is the nature and characteristic of the activities which would be required to be analyzed having regard to the facts and circumstances of each case as to whether they can be considered as individual/independent transactions or a single transaction for the purpose of transfer pricing regulation. In the present case, as we have noted earlier, it is only on account of the manufacturing activity that the activity of commissioning and installation of the equipment arises and pertinently all the aforesaid activities are negotiated and contracted for at one instance. With regard to the segmental profitability referred by the Assessing Officer, the

*position has been clarified by the assessee. According to the assessee, in the financial statements affirmed by the Auditors, the activities have been clubbed together in accordance with the Accounting Standards prescribed by the ICAI. It was clarified that the segmental profits were worked out by the assessee only at the asking of the TPO during the proceedings before him. The learned counsel pointed out with reference to the chart in this regard placed in the Paper Book and submitted that the segmental profitability was not computed on the basis of any separately maintained records viz. books of account or vouchers but was computed by undertaking a statistical exercise. The costs were allocated as a proportion of sales/revenues and not an actual basis. In view of the aforesaid fact situation, we do not find that the availability of separate segmental profits in the present case can be a justifiable ground for the TPO to say that the transactions are not ‘closely linked’ within the meaning of Rule 10A(d) of the Rules. Thus, the activity of installation and commissioning/engineering services is ‘closely linked’ with the manufacturing activity and deserves to be aggregated and construed as a single transaction for the purposes of determining the ALP as per the method adopted.*

*34. In view of the aforesaid discussion, in our opinion, the approach of the TPO, in out-rightly rejecting the aggregation of all the transactions itemized at 1 to 7 in para 7 is flawed having regard to the facts and circumstances of the case. Further, it is noticed from the tabulation in para 7 of this order, that the assessee is also rendering marketing services, technical know-how and professional services, etc., which have also been aggregated. For such activities no specific point has been made out by the assessee as to why they can be classified as ‘closely linked’ transactions for the purposes of Rule 10A(d) of the Rules. Considering the entirety of the facts and circumstances, we are of the opinion that the issue be revisited by the AO/TPO in the light of our aforesaid discussion. The AO/TPO shall take into consideration the pleas and the material sought to be placed by the assessee in the light of the aforesaid discussion and thereafter adopt a combined transaction approach after considering each of the transaction itemized at 1 to 7 as to whether the same are to be bench marked after aggregation or not. Needless to say, the Assessing Officer shall allow the assessee a reasonable opportunity to put forth material and submissions in support of its stand and only thereafter the Assessing Officer shall pass an order afresh on the above aspect in accordance with law. Thus, on this Ground, assessee succeeds for statistical purposes.”*

25. Similar principle has been laid down by the Delhi Bench of the Tribunal in M/s. Panasonic India Pvt. Ltd. Vs. ITO (supra) and M/s. Intimate Fashions (India) Pvt. Ltd. Vs. ACIT (supra).
26. In view of the ratio laid down by Pune Bench of the Tribunal in Demag Cranes & Components (India) Pvt. Ltd. Vs. DCIT (supra), it is

held that where number of transactions are closely linked transactions, then the same can be aggregated and construed as a single transaction for the purpose of determining the arm's length price. In case, there is close link exists between the different transactions, the same should be treated as composite transaction and appropriate method should be applied to work out the transfer pricing analysis. Where two or more transactions emanate from common source being an order or contract or an agreement or an arrangement, then such transactions could be said to be closely linked as the nature, characteristic and terms of such transaction substantially flow from the said common source.

27. In the above said background, we analyse the different international transactions entered into by the assessee as pointed out by us in the paras hereinabove. The business of the assessee company was to provide aftermarket support to IC engines sold, in the form of sale of spare parts and rendering of after sales service including warranty administration. The assessee is thus, providing after sales support for engines sold by Cummins India Ltd., Cummins INC, etc. which were under warranty period and also post warranty period. The servicing, repair and annual maintenance contract, warranty period and for post warranty period were the services provided by the assessee for carrying out most of the above said activities. The sale of spare parts was claimed to be the principal activity of the assessee. The repair & maintenance and the warranty administration including services of the IC engines requires the support of the spare parts which were sold by the assessee. Where the assessee was engaged in aftermarket support of engines manufactured and sold by Cummins entities, the question arises whether the sale of

spare parts could be categorized separately as a trading activity engaged in by the assessee, which in turn is separate from the activity of doing servicing of the IC engines, their repair and maintenance and also warranty administration i.e. support during the warranty period and also annual maintenance contracts and services during post warranty periods. Another activity engaged in by the assessee was payment for customized parts catalogue, which was also aggregated by the assessee company as part of its international transactions, which were claimed to be linked to the sale of spare parts carried on by the assessee.

28. The assessee during the year under consideration had made exports to its associated enterprises on account of the said spare parts totaling Rs.87,48,479/- . The assessee had also made exports to third parties during the financial year totaling Rs.4,16,326/-. The break-up of the exports to associated enterprises and third parties are enlisted at pages 200 to 204 of the Paper Book. Admittedly, there was significant difference in the value of exports made to associated enterprises and the exports made to third parties. The explanation of the assessee in this regard was that the exports made to the associated enterprises were on regular basis and were being made to its associated enterprises, which in turn were supplying to the dealers and through them, to the customers. However, the exports to third parties were directly made to the consumers who could select the spares through the catalogue and order the same to the assessee, who was engaged in providing aftermarket support to the IC engines sold worldwide. Further, the claim of the assessee was that the export to third parties was made on urgent basis and hence, the premium was charged and further, the frequency of such transactions was low and

consequently, higher margins of profits. The first major activity carried on by the assessee was of import of spare parts to Rs.29.45 crores as against which, the export of spare parts was only Rs.0.87 crores. The payment for IT support received from associated enterprises was Rs.1.09 crores and the payment for access to customized part catalogues was Rs.0.02 crores. Further, the assessee had received Rs.0.76 crores against warranty administration. All these international transactions are linked to the main business being carried on by the assessee and such closely linked transactions are to be analysed in aggregate to determine the arm's length price. The aggregation of the import of spare parts, export of spare parts, IT support services, access to customized parts catalogue and amount received for warranty consideration are inter-related transactions, which were the sourcing activities of the assessee company and have to be aggregated in order to benchmark the international transactions. The assessee had benchmarked the arm's length price of all the transactions by comparing results of the comparable companies which were found to be at arm's length price. The assessee had also furnished the segmental Profit & Loss Account for the exports to associated enterprises and as compared to the export to third parties and percentage of services over total sales in respect of export to associated enterprises works out to 0.2069% and in respect of exports to third parties works out to 0.0098%.

29. The plea of the assessee in this regard was that besides difference in the value of exports to third parties and to associated enterprises, the spare parts exported to third parties and to associated enterprises were different in nature. Further, the export value was less and these parties were one of customers and therefore, the risk

involved was high. Further, the frequency of such transactions was very low. In view of the above facts and circumstances, the comparison between the export to associated enterprises and export to third parties would not provide accurate results as economic value of the transactions, risk involved were different. We find merit in the plea of the assessee in this regard. We uphold the aggregation of transactions in the TP study carried on by the assessee where the said transactions after benchmark were at arm's length price, no adjustment was to be made. In view thereof, we find no merit in the analysis carried out by the TPO by benchmarking the transactions of exports to third parties with exports to associated enterprises resulting in addition of Rs.22.49 lakhs. In view of our discussion herein above, we delete the addition of Rs.22.49 lakhs. The grounds of appeal raised by the assessee are thus, allowed.

30. In the result, the appeal of the assessee is allowed.

Order pronounced in the open Court on this 31<sup>st</sup> day of December, 2014.

**Sd/-  
 (G.S. PANNU)  
 ACCOUNTANT MEMBER**

**Sd/-  
 (SUSHMA CHOWLA)  
 JUDICIAL MEMBER**

Pune, Dated: 31<sup>st</sup> December, 2014.  
 GCVSR

*Copy of the order is forwarded to: -*

- 1) The Assessee;
- 2) The Department;
- 3) The CIT(A)-I, Pune;
- 4) The CIT-I, Pune;
- 5) The DR "B" Bench, I.T.A.T., Pune;
- 6) Guard File.

By Order

//True Copy//

Assistant Registrar  
 I.T.A.T., Pune