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

BEFORE SHRI T. S. KAPOOR, ACCOUNTANT MEMBER
AND
SHRI C. M. GARG, JUDICIAL MEMBER

I.T.A .No.-1110/Del/2014
(Assessment Year-2009-10)

M/s Tianjin Tianshi Biological Development Company Ltd. 10, Community Centre Basant Lok, Vasant Vihar New Delhi-110057 PAN: **AABCT4203A**	**Vs.**	DCIT, Circle-2(2), International Taxation New Delhi.

I.T.A .No.-1117/Del/2014
(Assessment Year-2009-10)

DDIT, Intl. Taxation, Circle-2,(2) New Delhi.	**Vs.**	M/s Tianjin Tianshi Biological Development Company Ltd. 43, Housing Society, South Extension, Part-1, New Delhi. PAN: **AABCT4203A**
(APPELLANT)		**(RESPONDENT)**

Assessee by:-Sh. Hemant Kumar Arora, CA.
Sh. Jeetan Nagpal, FCA. &
Sh. S.D. Kapila, Adv. &
Sh. R.R. Maurya, Adv.
Revenue by:-Sh. Sanjeev Verma, CIT DR.
Sh. Vivek Kumar, Sr.DR.

ORDER

PER C. M. GARG, JM

The above captioned appeals have been preferred by the Assessee and the Revenue against the common order of the Assessing Officer dated 13.01.20014

passed u/s 143(3) read with section 144C(1) of the Income Tax Act, 1961, (for short 'the Act') in pursuance to the directions of Dispute Resolution Panel (DRP) vide its order dated 31.12.2013 passed u/s 144C(5) of the Act for AY 2009-10.

Assessee's Appeal ITA No. 1110/Del/2014

3. The assessee has raised following grounds in this appeal:

> *"1. The ld. AO erred assessing the total income of Tianjin Tianshi Biological Development Company Limited ('the Appellant') at Rs.50,60,71,388 as against the returned income of Rs.7,92,82,894/-.*
>
> *2. The AO/DRP erred in making addition of Rs.42,67,87,494/- being the difference between the value of MRP declared to custom authorities and the value of Maximum Retail Price (MRP) altered by the assessee on account of products sold by it to the Indian AE.*
>
> *2.1 The ld. AO and DRP have failed to appreciate that the concept of MRP is a legal fiction specifically created for the purpose of section 4A of the Excise Act, read with section 3 of the Custom Act and Standard Weight & Measures Act and that MRP has no application under the Income-tax Act to a transaction like the present one where the assessee received contracted consideration for the admittedly "wholesale sales to its Indian group entity i.e., Tianjin Tianshi Indian Private Ltd." (Para 2.1 of assessment order) even though it may have to pay import duty on the basis of MRP.*
>
> *2.2 That the observation of the Ld. DRP that the acceptance of ALP by the TPO "relates to the import price of goods by the assessee's branch office in India and does not relate to the price of goods at which the said goods have been subsequently sold by the assessee's Indian branch office of Tianjin India. As such, the above determination of ALP is of no relevance in deciding the issue of suppressed sales by the assessee" is contrary to the TPO's order as well as the remand report submitted by her to the DRP.*

2.3 The ld. DRP erred in law in increasing the quantum of sales as per accounts to Tianjin India by further adding the difference between the MRP declared earlier and altered MRP despite the fact it does not question the clear finding of fact by the TPO in Para 3 of his Remand Report dt. 18.11.2013, which clearly states that: "The assessee sells it's products to Tianjin Tianshi India Private Limited which is it's AE. Both the assessee nor Tianjin Tianshi India is a retailer but are only the second and third rung respectively in the distribution chain, and therefore they themselves do not sell the products at MRP. The assessee has paid the differential customs duty after the DRI search. The issue which has been raised by ld. DRP is whether after taking into discount the difference in custom duty if paid originally the transaction would be at Arm's Length."

2.4 The ld. AO/DRP have failed to appreciate that MRP (whether originally declared or the altered one) of the products sold by the assessee to Tianjin India has no nexus with and does not impact the actual price charged from Tianjin India.

3. *The ld. DRP erred in not allowing the additional custom duty of Rs.2.58 crores payable on the basis of altered MRP of imported products as the TPO considered this liability as part of operational expenditure this year for the purpose determining the ratio of operational profit to sales under TNM method for computing the arm's length price of the net margin earned on sales to Tianjin India.*

4. *The ld. AO erred in rejecting the books of account despite the fact that as per the direction of the DRP the assessee produced the books, bills and vouchers etc. before the AO during the remand proceedings.*

5. *The ld. DRP erred in refusing to admit the additional evidence.*

6. *The ld. AO has erred in law and facts and circumstances of the case in initiating penalty proceedings under section 271(1)(c) r.w.s. 274 of the Act."*

4. At the outset the ld. Counsel for the assessee submitted that the assessee do not want to press ground no. 3, hence, ground no. 3 of the assessee is dismissed as not pressed.

5. Briefly facts giving rise to this appeal as per written synopsis of the assessee are summarized as under:

> *"(i). Tianjin Tianshi Biological Development Company Limited is a company incorporated under the laws of People's Republic of China. The assessee set up it's branch office in India for the first time in the year 2000. The principal business of the assessee is that of wholesale of food supplements and health care equipments, which it imports into India from the Head Office in China/Group Companies. It primarily sells the same on wholesale basis to Tianjin Tianshi India Private Limited [in short 'Tianjin India']. Tianjin India is an Associated Enterprise [AE] of the Assessee within the meaning of section 92A of the Act. The 'food supplements' etc. are imported into India in retail packaging. The imports in the original packages are primarily sold in bulk to Tianjin, India. Therefore, the Assessee is a whole sale distributor of the products imported by it without any value addition.*
>
> *(ii). An addition of Rs.426,787,494 has been made by the AO on account of alleged suppressed sales based on the information received by him from the Assistant Director O/o DRI, (Customs) Zonal Unit Chennai. Simultaneous searches were conducted by the Director of Revenue Intelligence (under the Customs Law) on the office/warehouse premises of the assessee and Tianjin India on 5.9.11 and a show cause notice dated 14.3.12 was issued to the assessee. The allegations against the assessee primarily are that it has mis-declared the Retail Sale Price.*
>
> *(iii). As allegations of the Revenue the assessee wrongly mentioned the 'RSP' of the imported goods by suppressing the actual Maximum Retail Price ['MRP'] and has mis-classified the dietary supplements as medicaments under the Customs Tariff Code in certain Bills of Entry for the purpose of computing the Custom Duty payable. The assessee admitted the allegations before the Commissioner of Customs and paid the additional custom duty alongwith interest in respect of imports. Thereafter the assessee preferred an application with the Customs and Central Excise Settlement Commission ['the CCE Settlement Commission' or 'the date CCESC'] and the CCESC passed*

the final order no. 3/2013-Custom dated 21.2.13 in the regard.

(iv). As per stand and submissions of the assessee the assessee sells it's goods primarily to Tianjin India on wholesale basis. The AO referred the assessee's case to the Transfer Pricing Officer ['TPO'] for verification of the Arm's length Price of the international transactions entered into by the assessee with it's AE's. The TPO vide an order dated 18.1.13 has accepted all international transactions with the AEs, including the one relating to sale of Food Supplements, Health Equipments and Business Kits (which is the subject matter of present dispute) amounting to Rs.313,413,859 to have been made at Arm's Length Price.

(v). Based on the information obtained by the AO from the Assistant Director, DRI, Zonal Unit, the contents of the SCN and the order of the Settlement Commission, the AO arrived at an inference that the assessee had suppressed the value of it's actual sales.

(vi). The ld. AO has also alleged that the books of accounts were called for examination by him on 25.3.2013, 26.3.13, and 28.3.13 and that the assessee failed to produce the same. Accordingly, the books of account have been rejected and the claim of expenses is disallowed to the extent of 10% of the total expenses. A disallowance of Rs.9,265,306 was made by the AO in the draft assessment order passed to be made on this account.

(vii). Being aggrieved by the draft assessment order the assessee submitted objections to the DRP u/s 144C of the Act. The DRP remanded the matter back to the file of the AO directing him to provide the assessee with an opportunity to produce books of accounts and other relevant bills and vouchers. Further TPO was asked to re-examine the ALP of international transactions in light of the declaration of the assessee before the customs authorities.

(viii). The AO and the TPO submitted their remand reports. Based thereon, the DRP accepted the assessee's objections to ad-hoc addition of Rs.92.65 lacs out of total expenses claimed by the assessee but rejected the assessee objection on addition of the MRP as it's sales value to Tianjin India and made an addition of Rs.42.67 crores by holding that the book result of assessee regarding sales are unreliable hence the same are rejected and the DRP computed the amount of

suppressed sale of 42.67 crores by multiplying the differential MRP to the quantity of goods sold as per financial statement of the assessee. The AO in pursuance to the above order of the DRP, passed impugned assessment order vide date 13.01.2014.

(ix). The aggrieved assessee has prepared ITA No.1110/Del/2014 against the impugned addition of Rs.42.67 crores and the Revenue has also preferred ITA No.1117/Del/2014being aggrieved by the second part of the order of the DRP which deleted the ad hoc disallowance of 10% of expenses claimed by the assessee."

Ground No. 3

6. In the very beginning of the arguments, the ld. counsel appearing for the assessee submitted that the assessee does not want to press ground no.3, hence, the same is dismissed as not pressed.

Ground No.4

7. Apropos ground no.4, ld. Counsel for the assessee submitted that the AO was not justified in rejecting the books of accounts of the assessee despite the fact that as per direction of the DRP, the assessee produced books of accounts, required bills and vouchers etc. before the AO during the remand proceedings. Ld. Counsel pointed out that the AO has no sufficient cause for rejecting the books of accounts of the assessee.

8. Ld. DR replied that admittedly, the assessee produced books of accounts during remand proceedings before the AO. The DR further submitted that during the verification of books of accounts, it was found that the assessee has not accounted custom duty paid on revised MRP as revealed by the assessee before the Directorate of Revenue Intelligence (DRI). The DR has also drawn

our attention towards remand report dated 26.11.2013 and submitted that the assessee had no reason which prevented the assessee to produce the books of accounts at the time of draft assessment proceedings and the genuineness of the expenditure incurred by the assessee could not be verified by the AO due to short span of time during remand proceedings.

9. Ld. Counsel for the assessee submitted the rejoinder to above averment of the DR and contended that when DRP found it appropriate to allow the assessee to produce books of accounts and other related bills and vouchers before the AO, then during the remand proceedings, the AO is bound to allow the assessee to produce the books of accounts of the assessee and other related bills and vouchers. Ld. Counsel also contended that merely because the assessee had not accounted the additional custom duty paid on revised MRP and the AO had short span of time for verification, cannot be the basis for rejection of books of accounts of the assessee.

10. On careful consideration of above submissions, we note that as per section 145(3) of the Act where the AO is not satisfied about the correctness or completeness of the account of the assessee, or where the method of accounting provided in sub-section (1) of section 145 of the Act or accounting standard as notified in sub-section (2) of section 145 of the Act have not been regularly followed by the assessee, the AO may make an assessment in the manner as provided in section 144 of the Act. Thus, according to statutory provisions of section 145(3), the AO has to record his dissatisfaction about the correctness

and completeness of the accounts of the assessee before rejecting books of accounts. In the peculiar facts and circumstances of the present case, we observe that the DRP allowed the assessee to produce books of accounts and other related books and vouchers before the AO, hence, the AO is duty bound to accept the same during the remand proceedings and merely because the assessee had not accounted the additional custom duty paid and the AO had short span of time for verification of books of accounts and related bills and vouchers, the books of accounts of the assessee cannot be rejected. We also hold that when the DRP is allowing the assessee submission of books of accounts, then it is not open for the AO to examine the sufficient cause which prevented the assessee to submit books of acoutns during draft assessment proceedings. Finally, we are inclined to hold that the action of the AO rejecting the books of accounts of the assessee is not based on justified and legal reasoning, hence, ground no. 4 of the assessee is allowed.

Ground No.5

11. Apropos ground no.5, ld. Counsel of the assessee submitted that the DRP erred in refusing to admit additional evidence submitted by the assessee. Ld. DR vehemently replied and contended that from the impugned order of the DRP, there is no mention of denial or refusing to admit additional evidence. The DR also contended that the DRP allowed the assessee to submit its books of accounts and other related bills and vouchers before the AO during remand

proceedings which is a conscious support by the DRP to the assessee adhering to the principles of natural justice.

12. On careful consideration of above and perusal of the impugned order of the DRP, we observe that the DRP has allowed the assessee to submit its books of accounts and other relevant bills and vouchers before the AO during remand proceedings, hence, we are unable to accept this contention of the assessee that the DRP refused or declined to admit the additional evidence. Accordingly, ground no.5 of the assessee being devoid of merits is dismissed.

Ground No. 1 & 2, 2.1, 2.2, 2.3 & 2.4 of the assessee

13. We have heard argument of both the sides and carefully perused the material placed on record inter alia order of the DRP impugned order of the AO and written synopsis and arguments filed by the Assessee and the Revenue.

14. The ld. Counsel for the assessee has submitted written synopsis on behalf of the assessee as well as he has argued the case of the assessee in detail and addressed all the issues and angels pertaining to the impugned addition of Rs.42.67 crores. For the sake of proper adjudication on the all issues raised by the assessee and contentions of the Revenue, the arguments of the assessee as per written synopsis of the assessee may be summarized as follows:

15. The ld. counsel explained the business model of Tianjin Group. Tianjin China being the HQ in China has set up branch offices in India. The branch offices deal in health/food supplements and health equipments and sell their

products through a Multi Level Marketing Mode. The assessee has three branches in India and the business commenced in India in the year 2000. The concept of Maximum Retail Price (in short MRP) was explained in detail having regard to Excise Laws and Customs Law. According to the ld. AR the concept of MRP is a legal fiction created by section 4A of the Excise Act and section 3 of the Customs Act for the purpose of valuation of imported goods on which customs duty is levied. The ld. counsel further elaborated the contentions that how the concept of MRP is applied while charging excise duty and Customs duty and thereafter how prices are charged at different stages of the distribution chain and the MRP comes into play only at retail end of the distribution chain which is obviously the ultimate customer. The assessee i.e. the branch office of the Tianjin China imports goods from the Tianjin China i.e. HQ, and then sells it to its 100% subsidiary in India i.e. Tianjin India. Tianjin India further sells it to distributors and franchisee who in turn sell it to final consumers at MRP or at a price which could be lesser than the MRP. The ld. AR further explained that there is always a scope for discount on MRP and cited some examples. He said that at each distribution chain, the prices are negotiated in accordance with the MRP and stated that it is an admitted fact that the assessee had altered the MRP for Customs valuation purposes.

16. The ld. counsel also submitted that the assessee had made imports of Rs.9.64 crores and sold the same for Rs.31.34 crores to Tianjin India which in turn had sold the same goods for Rs.72.00 crores to the distributors. On behalf

of the assessee the ld. counsel explained that sales were being accounted for in different hands of the supply chain and further drew our attention to a chart showing the figures of purchase and sale and explained that if the AO's contention is accepted that the assessee effected sale of Rs.74.00 crores, then in that case Tianjin India automatically goes into loss because it is selling the same goods at Rs.72.00 crores which would lead to an unacceptable absurdity. The ld. counsel submitted a chart which is part of the written submissions to explain the figures relating to import by Indian branch of Tianjin China (HO) sale and purchase effected by Indian Branch of the assessee to Tianjin India and by Tianjin India to its distributors and franchisee. The ld. counsel explained that sale made by branch office of the assessee to Tianjin India was Rs.31.34 crores which was also precisely the value of purchase in the case of Tianjin India which was accepted by the same TPO/AO and DRP. The ld. counsel also contended the fact that in the case of Tianjin India, the TPO earlier had applied the TNMM and made an adjustment of Rs.16 crores to the purchases made from Tianjin China i.e. assessee, meaning thereby that Tianjin India's purchases from the assessee Tianjin China (HQ) were only Rs.15 crores and subsequently the DRP accepted the objections filed by Tianjin India and directed the TPO to apply RPM method, after which the purchase were accepted at Rs.31.34 crores as declared by Tianjin India. The ld. counsel made a mention about the TPO order in assessee's case and stated that the TPO has accepted the international transaction made by the assessee to be in conformity with the arm's length principle (page 298 Paper Book-II of assessee).

17. The ld. counsel also sought our attention to the fact that the DRP had called for a remand report from the AO and TPO and read the contents of the letter of the DRP calling for remand report. The ld. counsel further submitted that the AO referred the matter to the TPO for fresh consideration of the ALP. Reading from the TPO's remand report addressed to the DRP the ld. counsel stress on paras 1, 2, & 3 thereof and strenuously contended that neither the assessee nor Tianjin Tianshi India is a retailer but they are only the second and third entity respectively in the distribution chain, and therefore, they do not sell the products at MRP to the ultimate consumer. The ld. counsel further explained that the TPO treated the HO in Chiana, the manufacturer as the first entity in sale chain, the importer i.e. BD as the second entity the sole distributor (Tianjin India) as third entity and the retailers (small distributors and franchise) as fourth stage entities in the supply chain and read the concluding paragraph of the TPO's remand report dated 18.1.2013 (paper book page 260) wherein the TPO has stated that even after taking into account the additional customs duty, the OP/Sales of the assessee is more than that of comparable and therefore the international transactions are at Arm's length Price. The ld. counsel mainly contended that the TPO has taken into consideration both the purchases and sale and not just sales, as the ratio which has been taken is OP/Sales and also invited our attention to the DRP directions and argued that the DRP had erred in stating that TPO has only dealt with the purchase price of the assessee and not sale actual proceed of sales. The ld. counsel also contended that the TPO remand report clearly stated that OP/Sales comes down after taking into account the

additional customs duty of Rs.2.58 crores, thereby suggesting that the international transaction involving sales was duly considered by the TPO and the same was held to be at arm's length and DRP was wrong in stating otherwise that the report of the TPO has no relevance and in rejecting the TPO report. The ld. counsel argued that these observations of the DRP deserve to be rejected.

18. According the ld. counsel of the assessee the AO erred in substituting the actual value of sales made by the assessee to Tianjin India with a hypothetical value by substituting the actual sale price with the MRP declared by the assessee before Customs authorities, which was relevant only for levy of customs duty, making an addition of Rs.42.67 crores.

19. It was further submitted that the ld. AO/DRP have erred in law in disregarding the arm's length price of sale of goods to Tianjin India as determined by the TPO and in increasing the sale price. The ld. counsel also submitted that keeping in view the fact that the impugned sales is indisputably international transaction, the same squarely covered by the provisions of section 92(1) of the Act, which reads as under:

> *"92. (1) Any income arising from an international transaction shall be computed having regard to the arm's length price."*

20. The ld. counsel also drawn our attention towards section 92CA(4) of the Act (w.e.f. 1.6.2007) which reads thus:

> *(4) On receipt of the order under sub-section (3), the Assessing Officer shall proceed to compute the total income of the assessee under sub-section (4) of section 92C in conformity with the arm's length price as so determined by the Transfer Pricing Officer.*

21. The ld. AR relied on the decision in Aztec Software case (107 ITD 141), wherein the Special Bench of the ITAT Bangalore has held thus:

> *"Now, the words "having regard to" have been replaced by the words "in conformity with". So now the Assessing Officer after introduction of sub-section (4) above is required to pass the assessment order in conformity with the order of the Transfer Pricing Officer determining the arm's length price. Now the order of the TPO has been expressly made binding on the Assessing Officer. From the above it is clear that there was a lacuna in the Act as appropriate language was not used earlier. This has been modified and with effect from June 1, 2007, the order of the TPO is binding on the Assessing Officer who now has no choice but to pass an order in conformity with the order of the TPO. "*

22. Thereafter the ld. counsel submitted an alternate argument with the aid of a chart (at page 535-537 in paper book –V), that only some of the products were involved in the case where MRP was altered. The list of such products was provided as a part of chart. The ld. counsel further submitted that there is no dispute with regard to the quantity sold by the assessee to Tianjin India and the dispute was about the valuation of the sale price and the MRP was altered only on retail products which are subject to MRP. The ld. counsel further explained that the calculation made by DRI for the financial year 2008-09 (relevant to AY 2009-10) and contended that for the products, on which MRP was altered, the total revised MRP worked out by DRI was Rs.40.90 crores and the earlier reported MRP of such products was Rs.13.86 crores. Accordingly, the variance in MRP was only about Rs.27 crores and the undeclared sales worked out by the AO was Rs.42.67 crores which was much more than the MRP worked out by the DRI. The precise contention was that the AO had arbitrarily applied the

differential of MRP of three most expensive products to compare 8,83,618 units of 83 kind of products even though all products were not in dispute with the Customs. The ld. counsel placed above argument without prejudice to the stand earlier stand of the assessee that MRP had no relevance for income tax purposes.

23. The ld. counsel pointed out that the DRP had remanded the matter to the AO with directions to afford the assessee another opportunity to produce books of accounts. During remand proceedings, the assessee did produce books of accounts before the AO and he was completely satisfied with the books of accounts (Paper Book page 415-416). According to the ld. counsel there has been bias against the assessee which is evident from the fact that the AO prepared two contradictory remand reports in this case which was discovered by the Chartered Accountant of the assessee during the course of inspection of assessment record. The ld. Counsel has drawn our attention towards paper book page no. 415 & 416 and submitted that in the first remand report, the AO mentions that he had examined the books of accounts on test check basis and found nothing adverse. Then, he has further drawn our attention towards paper book page 430-433 and contended that the second remand report was prepared and actually sent to the DRP which is completely different from the first report and in the second remand report the AO had completely taken a U-turn and gone against the assessee wherein the AO stated that assessee did not produce books of account even after repeated opportunities during draft assessment proceedings and therefore additional evidences deserve to be rejected. The initial remand report dated 22.10.2013 is available on pages

415 to 416 of paper book-iv and second remand report is available at pages 430-430 of the same paper book.

24. Ld. Counsel further submitted that the DRP erred in law in increasing the quantum of sales as per accounts to Tianjin India by further adding the difference between the MRP declared earlier and altered MRP despite the fact that the DRP has not raised any dispute to the finding of fact by the TPO in para 3 of his remand report dated 18.11.2013 wherein it has been held that after taking into account the difference in custom duty if paid originally to transaction would be at arm's length. Ld. Counsel vehemently contended that the AO and DRP have failed to appreciate that the MRP whether originally declared or the altered one of the products sold by the assessee to Tianjin India has no nexus and impact, the actual price charged from Tianshi India.

25. On the issue of MRP, ld. DR replied that the ultimate sales effected by Tianjin India to the ultimate customer was made on MRP which was altered by the assessee in India, and therefore, the MRP is relevant and has impact on the actual price charged by the assessee from Tianshi India. Ld. DR fairly accepted that the TPO in para 3 of his remand report dated 18.11.2013 has concluded that after taking into consideration the difference in custom duty, if paid, originally the transaction would be at arm's length.

26. Apropos these grounds, ld. Counsel appearing for the assessee pointed out undisputed facts and the ld. DR has fairly accepted the same as undisputed, which may be summarised as under:-

i) M/s Tianjin Tianshi Biological Development Company Ltd. is a company incorporated under the laws of People's Republic of China which is primarily engaged in the manufacturing and sale of food supplements and health care equipments. Non-resident company operates and markets its products in the Indian market through its branch office in India which started operations in the year 2000. The said branch office is independently a PE under Indo China Tax Treaty whose income from business in India is offered to tax. The assessee sells the goods imported by it exclusively to its subsidiary i.e. Tianjin Tianshi India Private Limited. The assessee company group does not undertake any retail selling and follows the marketing model of Multi Level Marketing Model and there are no retail outlets for sale of assessee's products in India. The network marketing is based on word of mouth and independent canvassing by distributors of the assessee company. About the functional marketing model of the assessee, the revenue authorities have not disputed the flow of sales of goods from assessee company to its India branch office, India branch office to its wholly owned subsidy, wholly owned subsidy to franchisees and distributors and franchisees and distributors to ultimate customer. Franchisees and distributors purchase the products from Tianshi India and resell the ultimate to the customers directly. The franchisees and distributors are entitled to profit margin on retail sale and also upon various types of commission on sale. This model has been carved out

by the assessee company for the purpose of savings on expenditure and the heavy advertisement, show room and sales in cost including other related direct selling expenses. For the year under consideration, the assessee company through its branch office had booked sale of Rs. 31,44,97,241 as per profit and loss account (page no. 95 of paper book volume 1) including export sale of Rs.23,80.720 and Inland sales of Rs.31,21,16,521 in India was made by the assessee to Tianjin Tianshi India Private Limited which is 100% subsidiary of the assessee company and also its sole distributor in India. Tianjin India is assessee's associated enterprise as per provisions of section 92A of the Act.

ii) That the said sales transaction is subject to transfer pricing provisions as contained in chapter I of the Act and the sales made by the assessee to Tianshi India is an international transaction as defined in section 92B of the Act.

iii) Ld. Counsel of the assessee submitted that the AO/DRP erred in making addition being the difference between the value of MRP declared to custom authorities and the value of MRP altered by it on account of products sold by it to the Indian AE. Ld. Counsel contended that the AO and the DRP had failed to appreciate that the concept of MRP is a legal fiction being created for the purpose of section 4A of the Excise Act r/w section 3 of the customs and relevant provisions of the Standard Weights and Measure Act and the MRP has

no application under the Income Tax Act to the impugned transaction where the assessee receives contracted considered even though it may have to pay import duty on the basis of Maximum Retail price (MRP). Ld. Counsel further contended that the observations of the DRP that the acceptance of ALP by the TPO relates to the import price of the goods by the assessee branch office in India and does not relate to the price of goods at which the said goods have been subsequently sold by the assessee's India branch of Tianjin India because the said determination of ALP is of no relevance in deciding the issue of suppressed sales by the asessee and these observations of the DRP are contrary to the order of the TPO as well as remand report submitted by the TPO before the DRP.

27. On careful consideration of above, we respectfully note the ratio of the decision of **Hon'ble Supreme Court in the case of KJMS Mohd. 197 ITR 196(SC)** and **Coca Cola Export Corporation 231 ITR 200 (SC)** wherein it has been held that where the meaning of specific terms used has been legislated with a different object in the other statutory provisions, then the same cannot be blindly imported to the Income Tax Act in the present case. The revenue authorities picked up MRP which was used by custom and excise department for the purpose of levy of additional custom duty on the assessee but the same cannot be used for the purpose of determination of amount of sale effected by the assessee in India through its 100% owned subsidiary. The MRP may be

useful for the purpose of estimation of sales effected by the fanchisees and distributors to the ultimate customers but the MRP cannot be accepted to estimate the amount of sales effected by the assessee in India through its branch office or through its 100% owned subsidiary Tianjin India. Hence, the action of the revenue authorities in this regard is not sustainable.

28. Ld. counsel for the assessee reiterated the business model of the Tianjin Group with the Tianshi in China being its headquarters in China has set up branch offices in India, the branch office deals in health/food supplements and health equipments and further sell their products through Multi Level Marketing Model. Ld. counsel further accepted that the assessee i.e. branch office of the assessee company import goods from Tianjin China and then sells it to its 100% subsidiary in India i.e. Tianjin India.

29. The Tianjin India further sells it to distributors who in turn sell it to customers at MRP or at a price which could be lesser than the MRP. Ld. Counsel further submitted that there is always a scope of discount on MRP as at each distribution chain the prices are negotiable in accordance with the MRP. Ld. Counsel further stated that in the said flow of sales from Tianjin China to ultimate customer, the assessee company had made imports of Rs.9.64 crore and sold the same to Tianjin India , sole all India distributor at Rs.31.34 crores as the TPO/AO accepted the purchase price of Rs. 31.34 crore in the case of Tianjin India. Ld. Counsel further contended that if the AO accepted that the assessee's sale was of Rs. 74 crore, then Tianjin India automatically goes into

loss because as per revenue authorities, Tianjin India is selling the goods at Rs.72 crore which would lead to an absurdity. Ld. Counsel vehemently contended that the value of purchase in the case of Tianjin India was accepted by the same TPO and DRP. Ld. Counsel submitted that in the case of Tianjin India, the TPO applied TNMM and made adjustment of Rs. 16 crore to the purchases made from the assessee. If the order of the TPO is being given effect, then it would result that purchases from the assessee were only of Rs. 15 crore and therefore, the DRP accepted the objections filed by Tianjin India and directed the TPO to apply RPM method after which purchases were accepted in toto at Rs. 31.34 crore as declared by Tianjin India. Ld. Counsel has drawn our attention towards page 262 to 295 and submitted that finally in the case of Tianjin India, the TPO has accepted the international transaction made by the assessee with Tianjin India to be in conformity with the ALP.

30. Ld. Counsel has further drawn our attention towards the fact that the DRP had called a remand report from the TPO and the AO referred the matter to the TPO for fresh consideration of the ALP. Ld. Counsel has drawn our attention towards remand report of the TPO and submitted that the TPO has concluded that neither the assessee nor the Tianjin India are the retailer but are only second and third respectively in the distribution chain and, therefore, they themselves do not sell the products at MRP.

31. Replying to the above contentions, the DR supported the orders of the authorities below and submitted that the ALP is of no relevance in deciding the

issues of sales effected by the assssee in India. Ld. DR has drawn our attention to para 4.4.1 of the DRP and submitted that in spite of repeated request, the assessee did not produce books of accounts before the AO during draft assessment proceedings. He further contended that the assessee took a stand that the books were maintained on computer, telesystem, then why the assessee could not produce the same despite sufficient and repeated opportunities being provided by the AO during the draft assessment proceedings.

32. The DR further contended that the AO has also mentioned in the remand report that the custom duty paid on the revised MRP in pursuance to the DRI search has not been accounted by the assessee which shows the absence of due diligence in recording the transaction effected by the assessee. Ld. DR further submitted that the AO and DRP rightly observed that the assessee failed to substantiate the fact that the differential MRP in respect of zinc capsules, cell rejuvenation capsules, chewable calcium did not result in extra profit to the assessee. The DR further contended that the assessee has failed to demonstrate as to how above increase in sale price has not resulted in any extra profit to it and if there was no extra profit for the assessee, then what was the need to indulge in such large scale of MRP sticker, it was found during the DRI search operation.

33. Ld. DR also contended that the assessee has admitted to the large scale suppression of MRP before the custom authorities and has paid huge amount of fine and penalty for the same and, therefore, the DRP was right in agreeing that

the conclusion of the AO that the book results of the assessee regarding sale are unverifiable. The DR further contended that the AO had no option but to compute the amount of suppressed sale by multiplying the average of differential MRP to the quantum of goods sold as per assessee's financial statements. The DR supporting the action of the authorities below submitted that the proposed action of the AO with regard to the suppressed sale did not require any interference by the DRP and, therefore, the same was upheld.

34. On careful consideration of above submissions, we observe that in the case of Tianjin China i.e. headquarter or parent company, the TPO vide its order dated 18.1.2013 has held that no adverse inference is drawn in respect of international transaction undertaken by the assessee during FY 2008-09 pertaining to the AY 2009-10 which is assessment year under consideration. The relevant operative part of this order reads as under:-

> *"2.2 The Group is primarily providing high quality health products for consumers globally. TIENS is the brand name of Tianshi Group products, the food supplements manufactured by the Group are unique in constitution, owning to their formulations from Chinese herbs and the health care equipments are innovations combining ancient Chinese health theories with developments in science and technology,*
>
> *The major international transactions undertaken by assessee with its AE, and during the F.Y 2008-09 are as under;*

S.No.	*Nature of Transaction*	*Method selected*	*Value of transactions*
1	*Purchase of Food Supplements and health equipment*	*TNMM*	*9,64,49,953*
2	*Sale of Food Supplements, Health Equipments and Business Kits*	*TNM*	*31,34,13,859*
3	*Freight Recovery*	*At Cost*	*1,93,830*

4. The Transfer pricing documentation, which contains the functional and economic analysis of comparables and of assessee, has been examined and placed on record.

5. In view of the functional and economic analysis of assessee and of comparables, no adverse inference is drawn in respect of the international transactions undertaken by the assessee during the F.Y 2008-09."

33. We further observe that in the case of Tianjin India, the TPO vide its order dated 22.1.2013 directed the AO to reduce Rs.16,73,35,606 from the purchase price paid by the assessee to its AE i.e. related party. But we also observe that this order dated 22.1.13 was further rectified u/s 154 of the Act and the TPO concluded that the price paid by the assessee for purchases to its associated enterprises being lower than the ALP worked out in accordance with Rule 10B(1)(b) of the Income Tax Rules, 1962. No adjustment is required in this regard. Relevant operative part of this order at page 298 of the Paper Book of the assessee reads as under:-

"The assessee has paid Rs.31,10,33,139 for purchases made from its AEs as against Rs.35,29,83,970 which is the ALP worked out in accordance with Rule 10B(1)(b). The price paid by assessee for purchases being lower than the ALP worked out as above, no adjustment on this account is being made."

35. At this juncture, we may take cognizance of the decision of Special Bench as relied by the assessee in the case of Aztec Software & Tech. Ltd. vs ACIT (2007) 107 ITD 200 (Bang.)(SB) wherein speaking for the Special Bench, it was held that prior to the sub-section 4 of section 92CA of the Act, the

order of the TPO was not binding on the assessee but this has been modified w.e.f. 1.6.2007 and thereafter the order of the TPO is binding on the AO who now has no choice but to pass an order in conformity with the order of the TPO. The relevant operative part of the order of the Special Bench (supra) at page 206 and 207 reads as under:-

> *"It is clear from above that decision of Supreme Court in the case of Rajesh Kumar (supra) itself indicate that words 'having regard to' suggest that assessment is to be made having regard to the report of the TPO which is required to be considered with other relevant material available on record.*
>
> *There is nothing to suggest that TPO's report on transfer pricing is conclusive and debars Assessing Officer from looking at any other material.*
>
> *The aforesaid conclusion is also in line with latest change made in Section 92C by the Legislature through the Finance Act, 2007. Sub-section (4) of Section 92CA has been substituted with the following sub-section w.e.f. 1.6.2007:*
>
> *[(4) On receipt of the order under Sub-section (3), the Assessing Officer shall proceed to compute the total income of the assessee under Sub-section (4) of section 92C in conformity with the arm's length price as so determined by the Transfer Pricing Officer]*
>
> *53. Now words "having regard to" have been replaced by words "in conformity with". So now Assessing Officer after introduction of subsection (4) above is required to pass assessment order in conformity with the order of the Transfer Pricing Officer determining arm's length price. Now the order of the TPO has been expressly made binding on the Assessing Officer. From the above it is clear that there was a lacuna in the Act as appropriate language was not used earlier. This has been modified and w.e.f. 1.6.2007, the order of TPO is binding on the Assessing Officer who now has no choice but to pass an*

order in conformity with the order of the TPO. The word "having regard to" did not convey the same meaning. For all the aforesaid reasons, we hold that prior to substitution of Sub-section (4) by a new section, the order of the TPO was not binding on the Assessing Officer."

36. Ld. DR submitted a rejoinder and has drawn our attention towards para 4.5 of the impugned order of the DRP and submitted that the determination of ALP by the TPO is of no relevance in deciding the issue of alleged suppressed sale by the assessee. The ld. Counsel contended that in view of decision of Special Bench in the case of Aztec Software & Tech. Ltd. vs ACIT (supra), the AO is duty bound to pass order in conformity with the order of the TPO. The assessment cannot be made beyond the ambit of the order of the TPO.

37. In view of above rival contentions and submissions, we respectfully follow the ratio laid down by the Special Bench in the case of Aztec Software & Tech. Ltd. vs ACIT (supra) wherein it has been held that the AO does not have any way out but to accept the value of the international transaction between the assessee and its Associated Enterprise in conformity with the value determined by the TPO for the post amendment section 92CA(iv) w.e.f. 1.6.2007. The present case is related to AY 2009-10 which relates to FY 2008-09 and obviously, the ratio laid down by the Special Bench in the case of Aztec Software & Tech. Ltd. vs ACIT (supra) is squarely applicable in the present case. We also note that the TPO vide its order dated 18.1.2013 has held that the transfer pricing documentation which contains functional and economical analysis of the comparables of the assessee shows that no adverse inference may

be drawn in respect of international transaction undertaken by the assessee with its branch office in India and from branch office to 100% owned subsidiary company Tianjin India. We further note that the TPO through its order dated 28.2.2014 passed u/s 154 of the Act rectifying the DRP assessment order dated 26.12.2013 have held that the assessee paid Rs.31,10,33,139/- for the purchases made from its AE as against Rs. 35,29,83,970/- which is the ALP worked out in accordance with Rule 10B(1)(b) of the Act and the price paid by the assessee for purchases being lower than the ALP worked out therein, no adjustment on this account is being made. Thus, we further hold that the AO/DRP is duty bound to pass an order in this regard in conformity with the value determined by the AO and the provisions of the Act do not allow this authority to take a different stand or view against the order of the TPO. From the order of the DRP, we also observe that in para 4.4, the DRP has held that the determination of ALP by the TPO is of no relevance in deciding the issue of suppressed sale by the assessee. We also note that the sales shown by the assessee to Tianjin India has been accepted by the AO in the case of purchaser i.e. Tianjin India, hence, the sales made by the assessee cannot be disturbed by baseless estimation in the name of suppressed sales as wrongly alleged by the Revenue.

38. Coming to the issue of alleged suppressed sale by the assessee, we observe that the AO prepared remand report dated 22.10.2013 (Paper Book IV page 415-416) wherein the AO reported to the DRP that on verification of books of accounts, nothing adverse has been found (last line at page 416). We further observe that in the remand report dated 26.11.2013 (Paper Book Volume IV page 430-433), we observe that the AO has taken a U turn for the earlier conclusion of the report dated 22.10.2013 and has mentioned that the books of

accounts produced by the assessee cannot be accepted and reliance cannot be taken into account. The relevant operative part of this remand report is being reproduced for the sake of clarity in our findings which reads as under:-

> *"On perusal of note sheet entries, questionnaire u/s 142(1) issued on 17 .08.2011 and 10.10.2012 and the facts given in the, assessment order, it is seen that the contention of the assessee in this regard is not correct, as sufficient opportunity has been afforded to the assessee for producing books of accounts. In order to substantiate, copy of questionnaire u/s 142(1) issued on17.08:2011 and 10.10.2012 is enclosed herewith which clearly indicate that the assessee was asked to produce the books of accounts much before the date as mentioned by the assessee before the Hon'ble DRP i.e., 25.03.2013. Therefore, the assessee's communication to DRP-II about direction to produce books of accounts on 25.03.2013 is incorrect and misrepresentation of the facts.*
>
> *Besides, it is also seen that nothing new has been incorporated by the assessee.*
>
> *Before the Hon'ble DRP on this ground accept misrepresenting the facts. Further, though, the books of accounts i.e. cash book, bank book, expense ledger, sales register; stock register & vouchers above Rs. 50,000/- head wise for indirect expenses has been produced but there is no reason for admittance of these evidences at this stage as the assessee has not given any reason which prevented assessee to produce the books of accounts at the time of assessment proceedings, also the genuineness of the expenditures incurred by the assessee cannot be verified in this short span of time.*
>
> *In view of the same, the books of accounts produced by the applicant before the undersigned cannot be accepted and reliance cannot be taken into account at this stage."*

*3*9. In view of above, we observe that the AO took a very contradictory view in two remand reports as we note that in the first remand report dated 22.10.2013, the AO mentioned that on verification of books of accounts, nothing adverse has been found. On the other hand, in the subsequent remand

report dated 26.11.2013 which was actually sent to the DRP, the AO rejected the books of accounts of the assessee and held that the genuineness of the expenditure incurred by the assessee cannot be verified in this short span of time and the assessee has not given any reason which prevented the assessee to produce the books of accounts at the time of draft assessment proceedings. This approach of the AO is not acceptable and justifiable in view of our conclusion regarding ground no. 4 of the assessee, which have been adjudicated in favour of the assessee.

40. Turning to the issue of alleged suppressed sale by the assessee, after careful consideration of written submissions and arguments placed by both the both sides, at the outset, we observe that the DRP held that the determination of ALP is of no relevance in deciding the issue of suppressed sale by the assessee and went on to estimate the value of suppressed sale on account of difference between the value of MRP declared to the custom authorities and MRP altered on the products sold to the Tianjin India. At the cost of repetition we reiterate our above noted observation that the legal fiction created by the Central Excise Act and the Customs Act provides a measure for levy of excise/custom duty which cannot be followed or imported to the Income Tax Act. In view of decision of Hon'ble Apex Court in the case of KTMS Mohd. (supra) and Coca Cola Export Corporation (supra) the meaning of MRP in Central Excise & Customs Act have been legislated with a different object to evaluate and

calculate excise and custom duty which cannot be blindly imported for provisions of Income Tax Act.

41. On this issue, we also respectfully taken note of the decision of **Hon'ble Supreme Court in the case of ITC Ltd. vs CCE (2004) 7 SCC 591** wherein their lordships have held that a legal fiction has been created for prescribing the measure for the purposes of levy of custom duty on the manufacturer and the deemed value of sales taking MRP as a benchmark cannot substitute the real value of the sales for the purpose of computing the taxable income under the provisions of the Act. We may also note that the MRP may be the maximum price at which the retailer or a shop keeper ultimately sell the product to the consumers but the DR has not disputed the point that the assessee's branch office in India and assessee's 100% subsidiary company i.e. Tianjin India is not retailer or shop keeper who sell the product to the ultimate customer but they are second and third stage entity in the chain of multi level marketing of the Tianjin Group wherein the assessee through it branch office makes sales to its 100% owned subsidiary i.e. Tianjin India who further sells the product to the distributors/franchisees/shopkeepers and the price of this second and third level sales is always negotiable which cannot be equated with the MRP by any stretch of imagination.

42. From the operative part of the order of the DRP passed u/s 144C(5) of the Act, we observe that the DRP alleged that the assessee did not produce the books of accounts before the AO and as per remand report dated 22.10.2013

and 26.11.2013, we decline to accept this allegation of the DRP against the assessee. From para 4.1 of the DRP at page 11 of the impugned order, we further observe that the DRP has taken the basis of the remand report of the AO wherein it has been mentioned that the custom duty paid on the revised MRP as per DRI's search has not been accounted by the assessee. But the TPO in its order dated 18.1.2013 has mentioned that even after taking into account the revised total expenditure with 2.58 crore differential custom duty the revised operative profit in this scenario would work out to Rs. 5.05 crore and after considering the payment of differential custom duty, there would not be any impact on the ALP determined by the TPO.

43. From a careful reading of the operative part of the DRP, we note that the DRP has noticed differential MRP of only three products i.e. zinc capsules, cell rejuvenation, calcium tablets and the DRP further adopted average of differential of these three items and applied the same to the 83 products of which 883618 units were sold by the assessee in India. Ld counsel for the assessee on this point has drawn our attention towards pages 535 to 537 of Paper Book V of the assessee and submitted that only some of the products were involved in the case where MRP was entered and the list of such products was provided as part of chart and it was also submitted that the revenue has not disputed the quantity of the products as stated to be sold by the assessee to Tianjin India.

44. Ld. Counsel further contended that the addition made by the DRP and affected by the AO was based on the MRP which has no relevance for the purpose of quantification of sales adopted either by the assessee through its branch office or by Tianjin India to the distributors/retailers/shopkeepers. Ld. Counsel further submitted that the calculation made by DRP for the purpose of quantification of custom duty has no relevance to the actual value of sale effected by the assessee Tianjin India to the distributors/franchisees. Ld. Counsel further contended that for the products on which MRP was altered a total revised MRP worked out by the DRP was Rs.40.90 crore and the earlier reported MRP of such products was Rs.13.86 crore. Accordingly, the differential amount in MRP was of Rs. 27 crore which was calculated for the purpose of levy of excise/custom duty and which has no relevance to the calculation of actual sale effected by the assessee through its branch to Tianjin India and from Tianjin India to subsequent distributors/stockists/franchisees. Ld. Counsel also contended that the revenue authorities have not brought out any fact which could substantiate the allegation of the revenue that the assessee, or its branch office in India or its 100% owned subsidiary company Tianjin India suppressed the actual value of sales at any stage of multi level marketing channel. Ld. Counsel has drawn our attention at page 535 to 537 of the Paper Book V of the assessee and submitted that the AO at sl. No. 39 has accounted 407300 caps of bottles which have been included in the units of total quantity sold of 883618 and the average differential of 483 as noted by the AO in para 11 at page 7 of the assessment order) cannot be used for estimation of amount

of suppressed sale adopted by the assessee or its 100% owned subsidiary company. On this issue, the DR fairly accepted that the basis of calculation envisaged in para 11 of the assessment order is not explicit and the same is inclusive of 407300 caps of bottles and several other items of similar kind.

45. In view of above discussion, we are inclined to hold that the DRP was not right in keeping aside the reports of the TPO which approved and confirmed that the international transaction effected by the assessee and its associates in India was in conformity with the comparables adopted for determination of ALP. The AO/DRP proceeded to make the addition by estimating the suppressed sale adopted by the assessee by making estimation. We also note that for the purpose of estimation of alleged suppressed sale, the AO picked up three items and their average differential was adopted for the purpose of quantification of alleged suppressed sale. For final calculation, the AO considered the quantity of 883618 of 83 various products sold by the assessee in India which includes petty items of very minimal value such as cap of bottles, tie pins, umbrella, buttons, CD, Cloth covers etc. We further note that the AO took average of differential of only three vital items and multiplied the same to the total, units of all 83 products i.e. 883618. To the best of our understanding, we are unable to accept the basis of the AO and the DRP as noted above for quantification of value of alleged suppressed sale of the assessee.

46. On the basis of foregoing discussion, we reach to a logical conclusion that the estimation of suppressed sale made by the AO in para 11 at page 7 of

the assessment order dated 13.1.2014 is not justified, cogent and acceptable and we further hold that the DRP was not right in upholding the draft assessment order on this issue. Thus, we find it appropriate to set aside the observations, findings and conclusion of the revenue authorities on this issue and we set aside the same. Accordingly, ground no. 1, 2, 2.1, 2.2, 2.3 and 2.4 of the assessee are allowed.

Ground No. 6

47. Ground no. 6 of the assessee is premature and consequential to the main issue and we dismiss the same without any adjudication.

ITA No. 1117/Del/2014 Revenue's Appeal,

48. The grounds raised by the Revenue read as under:

> *"1. Whether on the facts and in circumstances of the case, the Hon'ble Dispute Resolution Panel ('DRP') has erred in directing the Assessing Officer to delete the proposed addition of Rs.92,65,306/-, being 10% of the total expenses claimed by the assessee, proposed to be disallowed by the Assessing Officer on account of failure of the assessee to produce, without any reasonable cause, the books of accounts and vouchers despite repeated opportunities during the course of the draft assessment proceedings.*
>
> *1.1 Whether the Hon'ble DRP has erred in holding that the proposed addition of Rs.92,65,306/- was without any rational basis, not appreciating the fact that the onus was on the assessee to substantiate the claim of expenditure by producing the books of accounts & vouchers and in the absence of the books of accounts and vouchers etc. the Assessing Officer was justified in the circumstances of the case in disallowing a part of the expenses on estimate basis.*

1.2 Whether the Hon'ble DRP, having once accepted the findings of the AO that the assessee had failed to produce the books of accounts & vouchers despite sufficient and repeated opportunities during the draft assessment proceedings, erred in proceeding to hold that there was no rational basis for the proposed addition by the AO.

1.3 Whether the Hon'ble DRP failed to appreciate the AO was justified in maintaining his stand in the remand proceedings that in the absence of reasonable cause for failure to produce the books of accounts & vouchers during the draft assessment proceedings, the same could not be admitted and verified at the remand stage and that the genuineness of the expenses was not amenable to verification in such a short span of time.

1.4 Whether the Hon'ble DRP erred in directing the AO to delete the proposed addition on account of unverifiable expenses on the ground that nothing adverse in relation to the expenses claimed by the assessee had come to light during the proceedings before the Directorate of Revenue Intelligence (DRI) & Customs Authorities, not appreciating the fact that the scope of the action taken against the assessee by the said authorities was completely different and that neither the quantum nor the genuineness of business expenses is the subject-matter for inquiries in the proceedings before these authorities."

ITA No.1117/Del/2014 – Revenue's Appeal

Ground No. 1, 1.1, 1.2, 1.3 & 1.4 of the Revenue

49. Apropos aforementioned grounds of the Revenue, ld. DR submitted that the DRP has erred in directing the AO to delete the proposed addition of Rs.92,65,306/- being 10% of the total expenses claimed by the assessee, proposed to be disallowed by the AO on account of failure of the assessee to produce, without any reasonable cause, the books of accounts and vouchers

despite repeated opportunities during the course of the draft assessment proceedings. The DR further contended that the DRP has erred in holding that the proposed said addition was without any rational basis by not appreciating and ignoring the fact that the onus was on the assessee to substantiate the claim of expenditure by producing the books of accounts, bills and vouchers and in absence of the same, the AO was justified in disallowing 10% of the expenses on estimate basis.

50. The DR further contended that once the DRP has accepted the findings of the AO that the assessee has failed to produce the books of accounts and vouchers despite sufficient and repeated opportunities during the draft assessment proceedings, then the DRP grossly erred in holding that there was no rational basis for estimated addition by the AO. The DR also contended that in absence of reasonable cause, which prevented the assessee to produce the books of accounts and vouchers during the draft assessment proceedings, the same could not be admitted at the remand stage and in this situation, genuineness of the expenses claimed by the assessee was not possible to verify in such a short span of time during remand proceedings. The DR parted with the argument with this final submission that the DRP erred in directing the AO to delete the proposed addition on account on unverifiable expenses on the ground that nothing adverse in relation to the expenses claimed by the assessee had been brought to light during proceedings before the DRI and custom authorities and the DRP was not justified in ignoring the fact that the basis and

scope of the action taken against the assessee by the DRI and custom authorities was competently different, that neither the quantum nor the genuineness of the business expenses was the subject matter for the inquiry in the proceedings before these authorities. The ld. DR supported the action of the AO and submitted that the impugned DRP order may be set aside by deleting the impugned addition.

51. Ld. counsel of the assessee replied that the AO was directed to by the DRP to allow the assessee to produce its boos of accounts along with relevant bills and vouchers during remand proceedings but the AO in the beginning of the order simply alleged that the custom duty paid on revised MRP has not been accounted and subsequently the AO observed that the assessee has not given any reason which prevented the assessee to produce the books of accounts at the time of draft assessment proceedings and the genuineness of the expenditure incurred and claimed by the assessee cannot be verified in the short span of time. Ld. Counsel strongly contended that the AO during the remand proceedings rejected books of accounts despite directions of the DRP that the assessee should be allowed to produce books of accounts and relevant vouchers and the action of the AO is also contrary to the letter and spirit of provisions of section 143(3) of the Act. Ld. Counsel further contended that while the action of the AO rejecting books of accounts of the assessee is not valid and justified, then the disallowance of 10% of claimed expenditure on estimated basis is not

sustainable, therefore, the DRP deleted the impugned addition with a cogent and reasonable observations and findings.

52. On careful consideration of above, we find it appropriate to reproduce the relevant operative part of the DRP which deleted the ad hoc addition made by the AO on estimated basis. The relevant para 4.4.3 of the DRP reads as under:-

> *"4.4.3 Coming to ground no. 2.1 relating to the proposed adhoc disallowance of Rs.92,65,306/- being 10% of total expenses, we find that the AO has not given any rational basis for the same either in the draft assessment order and or in the remand report. Nothing adverse in relation to the expenses claimed by the assessee has also come to light in the proceedings before DRI/ customs authoriteis. In the event, the above adhoc disallowance proposed by the AO is found to be without any basis. The AO is, therefore, directed to delete the same.*"

53. In view of above, we note that the AO examined the books of accounts produced by the assessee during remand proceedings and categorically stated in the first remand report that nothing adverse was found therein. However, when the DRP had remanded the matter to the AO with direction to examine the books of accounts, then it was the duty cast upon the AO to follow the directions of the superior authority. We are unable to see and understand any valid reason which prompted the AO to change his stand in the second remand report objecting to the admission of books of accounts. From a bare reading of the draft assessment order and the remand report, we note that nothing adverse has been brought out by the AO to the genuineness and quantum of expenses claimed by the assessee. Under these circumstances when rejection of books of accounts by the AO is not valid and justified, then the impugned ad hoc

disallowance of 10% of the expenditure claimed by the assessee, as proposed by the AO, is not sustainable and held to be without any basis. Therefore, we are inclined to hold that the DRP was right in deleting impugned ad hoc disallowance of Rs.92,65,306/- being 10% of total expenses claimed by the assessee. Accordingly, ground no.1 to 1.4 of the revenue being devoid of merits deserves to be dismissed and we dismiss the same.

54. In the result, the appeal of assessee is partly allowed as indicated above and appeal of the revenue is dismissed.

Order pronounced in the open court on 28.11.2014.

Sd/- Sd/-

(T.S. KAPOOR) (CHANDRAMOHAN GARG)
ACCOUNTANT MEMBER JUDICIAL MEMBER

DT. 28th NOVEMBER, 2014
'GS'

Copy forwarded to:-

1. Appellant
2. Respondent
3. C.I.T.(A)
4. C.I.T. 5. DR

By Order

Asstt. Registrar