

**IT/ILT : Amount of fixed assets written off could not be taken as part of operating costs of manufacturing segment for purpose of carrying out comparability analysis in order to determine ALP of international transactions**

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**[2018] 93 taxmann.com 223 (Mumbai - Trib.)**

**IN THE ITAT MUMBAI BENCH 'K'**

**Owens-Corning (India) (P.) Ltd.**

**v.**

**Assistant Commissioner of Income-tax, Range- 7(3)(1), Mumbai\***

G.S. PANNU, ACCOUNTANT MEMBER  
AND PAWAN SINGH, JUDICIAL MEMBER  
IT APPEAL NO. 5959 (MUM.) OF 2017  
[ASSESSMENT YEAR 2013-14]  
MARCH 23, 2018

**Section [92C](#) of the Income-tax Act, 1961 - Transfer pricing - Computation of arm's length price (Comparables and adjustments/Adjustment - Operating profit/cost) - Assessment year 2013-14 - Whether amount of fixed assets written off could not be taken as part of operating costs of manufacturing segment for purpose of carrying out comparability analysis in order to determine ALP of international transactions - Held, yes [Para 9][In favour of assessee]**

## **CASE REVIEW**

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*Thyssenkrupp Industries India (P.) Ltd. v. Addl. CIT [\[2013\] 33 taxmann.com 107 \(Mum. - Trib.\)](#) and Claas India (P.) Ltd. v. DCIT [IT Appeal No. 3883 (Delhi) of 2010, dated 12-08-2015] (para 9) followed.*

## **CASES REFERRED TO**

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*Thyssenkrupp Industries India (P.) Ltd. v. Addl. CIT [\[2013\] 33 taxmann.com 107 \(Mum. - Trib.\)](#) (para 6), Claas India (P.) Ltd. v. DCIT [IT Appeal No. 3883 (Delhi) of 2010, dated 12-08-2015] (para 6), Serial Innovations India (P.) Ltd. v. Dy. CIT [\[2015\] 60 taxmann.com 406 \(Bang. -Trib.\)](#) (para 6), *Jt. CIT v. Mukund Ltd.* [\[2007\] 106 ITD 231 \(Mum.\)](#) (para 13) and *CIT v. Saraswat Infotech Ltd.* [IT Appeal (L) No. 1243 (Bom.) of 2012, dated 15-1-2013] (para 19).*

**Jehangir D. Mistry, Niraj Sheth and Ketan Ved for the Appellant. Jayant Kumar and V. Jenardhanan for the Respondent.**

## **ORDER**

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**G.S. Pannu, Accountant Member** - The captioned appeal by the assessee is directed against the order dated 23-08-2017 passed by the Assessing Officer u/s 143(3) r.w.s 144C(13) of the Income Tax Act, 1961 (in short 'the Act') giving effect to the directions of Dispute Resolution Panel-II, Mumbai (DRP) dated 26-07-2017.

**2.** In its appeal, assessee has raised the following Grounds of appeal :—

**"1 : 0 Re.: Adjustment of Rs. 19,21,38,016/- to the manufacturing segment :**

1 : 1 The Assessing Officer (AO)/ the Dispute Resolution Panel (DRP)/ the Transfer Pricing Officer (TPO) have erred in making an upward adjustment of Rs.19,21,38,016/- to the total income of the Appellant by holding that the international transactions aggregated under manufacturing segment of the Appellant were not at an arm's length.

1 : 2 The Appellant submits that considering the facts and circumstances of its case and the law prevailing on the subject the international transactions aggregated under manufacturing segment were at an arm's length and hence no adjustment in respect thereof was called for and the stand taken by the AO/the DRP/ the TPO in this regard is misconceived, erroneous and incorrect.

1 : 3 The DRP has erred in rejecting the additional ground of objection raised by the Appellant requesting the DRP to direct the AO/TPO to reduce the amount of Rs.9,06,80,292/- being fixed assets written off while computing the operating margin of the manufacturing segment of the Appellant.

1 : 4 The AO/ DRP/ TPO have erred in considering an amount of Rs. 9,06,80,292/- being fixed assets written off as a part of the operating cost while calculating the operating margin of the manufacturing segment of the Appellant.

1 : 5 The AO/ DRP/ TPO have erred in not appreciating the business reasons behind the low margins earned by Appellant under manufacturing segment during the year under consideration.

1 : 6 The Appellant submits that the AO be directed to delete the upward adjustment of Rs. 19,21,38,016/- made by him to the Appellant's total income and to re-compute its total income and tax liability accordingly.

Without prejudice to the aforesaid grounds,

1 : 7 The AO/ DRP/ TPO have erred in not restricting the adjustment, if any, to the value of international transactions aggregated under manufacturing segment of Appellant.

**2 : 0 Re.: Disallowance of amortisation of the premium paid for the leasehold land:**

2 : 1 The AO / DRP has erred in disallowing the amortisation of a sum of Rs.20,14,932/- being the premium paid for acquiring the leasehold land.

2 : 2 The Appellant submits that considering the facts and circumstances of its case and the law prevailing on the subject the amount amortized is deductible in computing its total income and the stand taken by the AO / DRP in this regard is misconceived, illegal, erroneous and incorrect.

2 : 3 The Appellant submits that the AO be directed to delete the disallowance so made by him and to re-compute its total income accordingly.

**3 : 0 Re.: Disallowance of depreciation on addition to the fixed assets pertaining to Assessment Year 2006-07:**

3 : 1 The AO / DRP has erred in disallowing depreciation of Rs. 20,75,940/- out of the total depreciation of Rs. 21,83,10,119/- claimed by the Appellant during the year.

3 : 2 The Appellant submits that considering the facts and circumstances of its case and the law prevailing on the subject the Appellant is entitled to claim the depreciation of Rs. 20,75,940/- and the stand taken by the AO / DRP in this regard is incorrect, erroneous and not in accordance with law.

3 : 3 The Appellant submits that the AO be directed to allow depreciation as claimed by it and to re-compute its total income accordingly.

**4 : 0 Re.: Disallowance of depreciation claimed @ 60% on computer software:**

4 : 1 The AO / DRP has erred in restricting the depreciation allowable on software purchased by the Appellant during the year under consideration to 25% as against 60% claimed by the Appellant.

4 : 2 The Appellant submits that considering the facts and circumstances of its case and the law prevailing on the subject it is entitled to claim depreciation @ 60% on the computer software and the stand taken by the AO / DRP in this regard is incorrect, erroneous and not in accordance with law.

4 : 3 The Appellant submits that the AO be directed to allow depreciation as claimed by it and to re-compute its total income accordingly.

**5 : 0 Re.: Disallowance of provision for legal and professional fees of Rs.93,50,000/- and power and fuel of Rs. 47,62,500/- respectively u/s. 37 of the Income-tax Act. 1961 (ITA):**

5 : 1 The AO / DRP has erred in disallowing a sum of Rs. 1,41,20,500/- being the provision made for legal and professional fees of Rs. 93,50,000/- and power and fuel of Rs.47,62,500/- u/s. 37 of the ITA.

5 : 2 The Appellant submits that considering the facts and circumstances of its case and the law prevailing on the subject the expenditure incurred by it had crystallized during the year under consideration was incurred, wholly and exclusively for the purposes of the business and the stand taken by the AO / DRP is based on suspicions, surmises and conjectures and hence is incorrect, illegal, unwarranted and unjustified.

5 : 3 The Appellant submits that the AO be directed to delete the disallowance so made by him and to re-compute its total income accordingly."

**3.** The appellant before us is a company incorporated under the provisions of the Companies Act, 1956 and is, *inter-alia*, engaged in the business of manufacture and trading of fibre glass products. For the assessment year under consideration, it filed a return of income declaring a total income of Rs.41,61,49,410/-, which was subject to scrutiny assessment whereby the total income has been assessed at Rs.62,89,21,060/- in an order passed u/s 143(3) r.w.s. 144C(13) of the Act dated 23-08-2017. Being aggrieved with the enhancement of the returned income, assessee is in appeal before us on the abovestated Grounds of appeal.

**4.** Insofar as Grounds of appeal no. 1.1 to 1.7 are concerned, the same are in relation to an addition of Rs.19,21,38,016/- made by the Assessing Officer on account of a transfer pricing adjustment. In this context, the relevant facts are that the appellant is a subsidiary concern of IPM Inc., Delaware, U.S.A and OC NL Invest Cooperatief UA, U.S.A. In the course of its business activity of manufacturing and trading in fibre glass products, it had entered into international transactions within the meaning of Sec. 92B of the Act with its associate enterprises. In order to compute income arising from such international transactions in terms of Sec. 92(1) of the Act, the Assessing Officer made a reference as per Sec. 92CA(1) of the Act to the Transfer Pricing Officer (TPO) for determination of the arm's length price (ALP) of such international transactions. The TPO computed the ALP of the international transactions relating to the manufacturing segment at an amount higher than the stated value by a sum of Rs.19,21,38,016/- in an order passed u/s 92CA(3) of the Act dated 31-10-2016. The draft assessment order passed by the Assessing Officer on 26-12-2016, based on such a transfer pricing adjustment, was carried before the DRP wherein assessee raised various objections. The DRP vide order dated

26-07-2017 rejected such objections and accordingly, the Assessing Officer has retained the addition of Rs.19,21,38,016/- on account of transfer pricing adjustment in the final assessment order also. In this background, assessee is in appeal before us.

5. It is noted from the order of the TPO that assessee had entered into varied international transactions in the manufacturing segment, trading segment as also in commission segment. The dispute between the assessee and the Revenue relates only to the 'international transactions' entered in the manufacturing segment whose details have been enumerated by the TPO in para 5 of his order. Notably, assessee aggregated different transactions under the manufacturing segment while benchmarking the same in its Transfer Pricing Study report, an aspect on which there is no dispute. In its Transfer Pricing Study, the assessee selected the Transactional Net Margin Method (TNMM) as the most appropriate method, which also is not a subject matter of the difference between the assessee and the TPO. In the Transfer Pricing Study, assessee had determined the weighted average margin of the comparable concerns based on the financial data of three financial years by using Operating Profit/Operating Costs (OP/OC) as the Profit Level Indicator (PLI). While the PLI methodology was not disputed, but the TPO required the assessee to compute the margin of the comparable concerns based on the financial data of the single financial year corresponding to the assessment year under consideration. Be that as it may, the TPO determined the arithmetic mean of margin of the four comparable concerns at 8.07% detailed as under :-

<i>Comparables</i>	<i>OP/OC</i>
Asahi India Glass Ltd.	1.01%
Gujarat Guardian Ltd.	24.65%
Hindusthan National Glass & Ind. Ltd.	-2.27%
U P Twiga Fiberglass Ltd.	8.88%
Arithmetic mean	8.07%

Insofar as assessee's margin is concerned, the same has been considered by the TPO at 2.62%, computed as under :-

<i>S. No</i>	<i>Particulars</i>	<i>Amount</i>
1.	Operating revenue (A)	361,44,01,311
2.	Operating Cost (B)	352,22,90,485
3.	Operating Profit (C)	9,21,10,826
4.	NCP Margin %	2.62%

Thus, the arithmetic mean of the margins of the comparables computed at 8.07% was compared with assessee's margin of 2.60%; and, since assessee's margin was beyond the  $\pm 3\%$  permissible variation, an adjustment of Rs.19,21,38,016/- was worked out which was required to be made to the stated value of the tested 'international transactions' aggregated under the manufacturing segment. The order passed by TPO u/s 92CA(3) of the Act dated 31-10-2016 determining an adjustment of Rs.19,21,38,016/- formed the basis for the Assessing Officer to propose an addition of the aforesaid sum in the draft assessment order dated 26-12-2016. The assessee raised varied objections against the above adjustment before the DRP, including an Additional Ground raised in the course of proceedings, which was to the effect that assessee's margin at 2.62% was wrongly computed by TPO by erroneously including an amount of Rs.9,06,80,292/- representing fixed assets written-off as a part of operating costs. All the Grounds raised by the assessee have been dismissed by the DRP, including the Additional Ground. Thus, an amount of Rs.19,21,38,016/- was added to the returned income in the final assessment order.

6. Before us, the assessee has urged various issues in Grounds no. 1.1 to 1.7 with respect to the adjustment of Rs.19,21,38,016/- made to the manufacturing segment, but at the threshold, a plea was raised with respect to Grounds of appeal no. 1.3 and 1.4. The two Grounds are with regard to Additional Ground of objection raised by the assessee before the DRP, which is to the effect that the amount of fixed assets written-off of Rs.9,06,80,292/- is not a part of its operating costs and the same cannot be considered to compute its margin for carrying out the comparability analysis with the margin of selected comparables. It has been canvassed before us that if the said aspect is decided in favour of the assessee,

it would result in deletion of the entire addition even if one is to go by the working of the margin of comparables as drawn by the TPO. In support of his submissions, the learned representative pointed out that so far as assessee is concerned, though the amount of fixed assets written-off of Rs.9,06,80,292/- was debited in the Profit & Loss Account, but while computing the income for the purposes of tax, the same has been added back and, for that matter, our attention has been drawn to the computation of total income annexed to the return of income. Secondly, on the point of law, it is sought to be made out that in the following cases different benches of the Tribunal have taken a view that the amount of fixed assets written-off could not be taken as part of the operating costs of the tested segment :—

- (i) *Thyssenkrupp Industries India (P.) Ltd. v. Addl. CIT* [\[2013\] 33 taxmann.com 107 \(Mumbai - Trib.\)](#); and,
- (ii) *Claas India (P.) Ltd. v. DCIT*, [IT Appeal No. 3883(Delhi) of 2010, dated 12-08-2015].

Supporting his argument further, the learned representative pointed out that, in fact, in the case of *Serial Innovations India (P.) Ltd. v. Dy. CIT* [\[2015\] 60 taxmann.com 406 \(Bangalore - Trib.\)](#) before the Bangalore Bench of the Tribunal, the working of the margins noted by the Bench showed that the TPO himself had not considered the fixed assets written-off as part of the operating cost. It has been pointed out that even otherwise, on the basis of established commercial principles, it could not be said that the charge to the Profit & Loss Account represented by 'fixed assets written-off was a part of 'operating costs'.

**7.** On the other hand, the ld. DR opposed the plea of the assessee by referring to the discussion made by the DRP. According to him, the DRP had brought out that the Additional objection raised by the assessee could not be entertained as it was raised at the fag end of the proceedings; that in the absence of details of the assets written-off, the claim could not be verified. The ld. DR also referred to an observation of the DRP that in the absence of the relevant details, it was not clear as to whether any depreciation on such assets was allowed in this year or not. For all the above reasons, the plea of the assessee has been opposed by the ld. DR.

**8.** In reply, the learned representative pointed out that the Additional objection raised before the DRP does not require any additional/fresh evidence and that it was possible to decide the matter on the basis of available material on record. Further, it is pointed out that the Assessing Officer has himself not taken note of the amount of fixed assets written-off while computing the total income in the assessment order. In other words, according to the appellant, the said amount has not been taken as deduction while computing the income and, in this context, he referred to the 'business income' computed by the assessee in its computation of income at Rs.41,61,49,407/-, a copy of which is placed at page 25 of the Paper Book. It is explained that the aforesaid figure has formed the basis for the Assessing Officer to start the computation of income in para 17 of the assessment order. Therefore, in this manner, it is canvassed that once an amount has not been taken into consideration to arrive at 'business income', it could not be taken as part of operating costs for the purposes of computing the segmental margin of one of the segments. Insofar as the plea of ld. DR on depreciation is concerned, the learned representative pointed out that in this year, no depreciation has been claimed on such assets written-off.

**9.** We have carefully considered the rival submissions. In our view, the impugned sum cannot be construed as part of operating costs for the purpose of arriving at the margin of assessee's manufacturing segment. The said proposition is amply supported by the earlier decisions of our coordinate Benches in the case of *Thyssenkrupp Industries India (P.) Ltd. (supra)* as well as *Claas India (P.) Ltd. (supra)*. Moreover, factually speaking, it is quite clear that though the assessee had debited the fixed assets written-off of Rs.9,06,80,292/- in the Profit & Loss Account, but while computing income for the purposes of income-tax, the said amount has been added back and this aspect is also accepted in the

assessment order. In para 17 of the assessment order, the Assessing Officer while computing the total income under the normal provisions of the Act has started with the figure of Rs.41,61,49,407/-, which is the 'business income' computed by the assessee in its return after adding back the element of fixed assets written-off of Rs.9,06,80,292/-. This feature further strengthens the argument of the assessee that the impugned sum cannot be construed as a part of operating costs of the manufacturing segment for the purpose of carrying out comparability analysis in order to determine the ALP of the international transactions. In the course of hearing, it was also put across to the assessee as to whether similar treatment is also meted out in the case of the four comparable concerns whose arithmetic mean has been arrived at by the TPO at 8.07%. In response, the appellant had furnished a working of the margin of each of the four comparables to point out that even after considering the element of fixed assets written-off as non-operating costs in each of the four cases, the margin remains the same. The working so produced was also sought to be backed-up by the Annual Reports of the four comparable concerns, whose copies have also been placed in the Paper Book. On this aspect, there is no dispute.

**10.** Considering all these aspects, in our view, the DRP erred in not considering the Additional plea sought to be raised by the assessee. The DRP, in our view, wrongly noted that the new plea would require admission of any fresh evidence. In fact, all that is required to verify the Additional plea is the examination of the existing material available on the records of the Assessing Officer. Therefore, in our view, there was no justification on the part of the DRP not to admit such a plea. The other objections referred by the Id. DR before us are also not germane and, in any case, the same have been effectively met out by the learned representative before us. Thus, we find no merit in the stand of the Revenue to oppose the aforesaid Additional plea of the assessee.

**11.** As per the working submitted, if the element of fixed assets written-off of Rs.9,06,80,292/- is excluded from the operating costs, the reworked margin of the assessee would be as under :—

Sr. No.	Particulars	Amount
1.	Operative Revenue (A)	3,61,44,01,311
2.	Operating Cost (B) [Refer Note 1]	3,43,16,10,193
3.	Operating Profit (C) = (A) - (B)	18,27,91,118
4.	Cost plus Margin of Tested party (D)	5.33%

**12.** Thus, the margin of assessee's manufacturing segment is liable to be adopted at 5.33% as against 2.62% considered by the TPO. Once it is compared with the margin of the comparables adopted by the TPO at 8.07%, the difference, in our view, is within the variation of  $\pm 3\%$  permissible in terms of the second proviso to Sec. 92C(2) of the Act and, therefore, necessity of any adjustment to the stated value of international transactions is obviated. Therefore, on the basis of Grounds no. 1.3 and 1.4, the claim of assessee is allowed and the Assessing Officer is directed to delete the addition of Rs.19,21,38,016/- made to the returned income on account of transfer pricing adjustment. Pertinently, so far as the other pleas on this aspect raised by way of Grounds of appeal no. 1.1, 1.2, 1.5, 1.6 and 1.7 are concerned, they are rendered academic since assessee has already succeeded in seeking deletion of the addition in terms of Grounds 1.3 and 1.4 above and, therefore, they are not being adjudicated for the present.

**13.** Insofar as Ground of appeal no. 2 is concerned, the same relates to the claim of amortisation of premium paid for leasehold land of Rs.20,14,932/-. It is noticed that the Assessing Officer disallowed the claim by relying on the decision of the Special Bench of the Tribunal in the case of *Jt. CIT v. Mukund Ltd.* [2007] 106 ITD 231 (Mum.) as also the stand of the assessing authority in assessee's own case for the earlier assessment years. Before us, it was pointed out that the lead year of dispute on this aspect was Assessment Year 2001-02, wherein the Tribunal in assessee's own case vide ITA No. 8939/Mum/2004 dated 19-11-2008 decided the issue against the assessee. In Assessment Year 2004-05 also, vide ITA No. 461/Mum/2009 dated 16-03-2011 the said issue has been decided against the assessee. The learned representative for the assessee quite fairly conceded that the issue is liable to be decided against the assessee in view of the precedents in assessee's own case. Thus, on this aspect,

assessee fails and Ground of appeal no. 2 is dismissed.

**14.** In Ground of appeal no. 3, the dispute pertains to depreciation of Rs.20,75,940/- disallowed by the Assessing Officer out of total depreciation claim of Rs.21,83,10,119/-. The facts relevant to the partial disallowance of depreciation are as follows. It was noted by the Assessing Officer that in Assessment Year 2006-07, depreciation in respect of 'addition to fixed assets' of that year was disallowed since assessee had failed to produce supporting documents for verification. The Assessing Officer also noted that appeal of the assessee against the denial of depreciation for Assessment Year 2006-07 was also dismissed by the CIT(A) and further appeal of the assessee was pending before the Tribunal. Considering the consequential effect of the disallowance made in Assessment Year 2006-07, the Assessing Officer scaled down the depreciation claimed in this year by a sum of Rs.20,75,940/-, which is sought to be assailed by the assessee before us.

**15.** Before us, the learned representative has not disputed the fact that the disallowance of depreciation made in Assessment Year 2006-07 continues to hold. The only point made out by the assessee is that the consequential denial of depreciation to the extent of 'addition made to fixed assets in Assessment Year 2006-07' has not been made in Assessment Years 2007-08 and 2008-09 and, therefore, the impugned disallowance was not merited in this year too.

**16.** On the other hand, the Id. DR appearing for the Revenue has defended the action of the Assessing Officer.

**17.** Having considered the rival stands, in our view, the lead year of dispute is Assessment Year 2006-07. In Assessment Year 2006-07, the depreciation in respect of 'addition to fixed assets' made in that year has not been allowed by the income-tax authorities and the said position continues to prevail till now. In this view of the matter, in our view, the Assessing Officer made no mistake in giving consequential effect and scaling down assessee's claim for depreciation in this year. We are inclined to uphold the stand of the Assessing Officer with a caveat that if the position of assessee's claim of depreciation for Assessment Year 2006-07 is altered by any higher authority in favour of the assessee, the consequential relief be allowed to the assessee in the instant assessment year also. With these remarks, we hereby affirm the ultimate decision of the Assessing Officer and accordingly, assessee fails on this aspect.

**18.** Insofar as Ground of appeal no. 4 is concerned, the same relates to assessee's claim of depreciation @ 60% on computer software as against 25% allowed by the Assessing Officer.

**19.** Insofar as the factual aspects are concerned, the learned representative pointed out that expenditure on computer software in question related to SAP software and that the income-tax authorities erred in allowing depreciation @ 25%. In support, reliance has been placed on the judgment of the Hon'ble Bombay High Court in the case of *CIT v. Saraswat Infotech Ltd.* ITA(L) No. 1243 of 2012 dated 15-01-2013, wherein depreciation on computer software has been held to be allowable @ 60%. Considering the judgment of the Hon'ble Bombay High Court in the case of *Saraswat Infotech Ltd.* (*supra*), we hereby allow assessee's claim of depreciation @ 60% on computer software. Thus, on this aspect, assessee succeeds.

**20.** The last Ground in this appeal is with regard to disallowance of Provisions for legal and professional fee of Rs.93,50,000/- and Power and fuel expenditure of Rs.47,62,500/-. In this context, the relevant discussion contained in para 10.4 of the assessment order reveals that the Provision for expenses, included Provision for legal and professional expenses of Rs.93,50,000/- and Power and fuel expense of Rs.47,62,500/-. It is further noted by the Assessing Officer that in the absence of any basis of estimation of the above Provisions, it could not be proved that the corresponding services have been received by the assessee during the year under consideration. Thus, in the absence of supporting evidence, the Assessing

Officer also doubted the genuineness of the claim and finally, he has disallowed the same u/s 37(1) of the Act.

**21.** Before us, the only plea raised by the assessee is that the aforesaid Provisions have been made in the books of account on an estimated basis pending the receipt of actual bills, which were received by the assessee in the subsequent financial year. The learned representative also pointed out that it is only on the receipt of the bills in the subsequent year that assessee has deducted the requisite tax at source and made the payments to the vendors/parties. In this background, the only point sought to be canvassed is to the effect that in the subsequent year, the Assessing Officer be directed to allow the claim of the assessee.

**22.** In our considered opinion, insofar as the case made out by the Assessing Officer to disallow the impugned Provision of expenses is concerned, the same is fair and proper as nothing cogent has been led by the assessee to counter the findings contained in para 10.4 of the assessment order. Thus, the disallowance made by the Assessing Officer u/s 37(1) of the Act is hereby affirmed. Insofar as assessee's plea for considering the claim in the subsequent year is concerned, the same be considered by the Assessing Officer in accordance with law as and when the claim is put forth by the assessee before him. Thus, we hereby affirm the said addition and accordingly, assessee fails on this aspect.

**23.** Resultantly, appeal of the assessee is partly allowed, as above.

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\*In favour of assessee.