

TNMM is most appropriate method for determining ALP of agency and marketing support services rendered to AE

Summary – The Delhi ITAT in a recent case of Marubeni India (P.) Ltd., (the Assessee) held that where assessee was engaged in providing agency and marketing support services to its AE, TNMM was most appropriate method for determining ALP of said international transactions entered into with AE.

Facts

- The assessee was a wholly owned subsidiary of Japan ('MCJ'), Japan. The assessee liaised between various business departments of MCJ group companies and their suppliers/customers in India.
- The assessee selected Transactional Net Margin Method (TNMM) as the most appropriate method with the Profit Level Indicator (PLI) of OP/OC. Profit rate of 16.87 per cent was declared by the assessee in respect of its international transactions with the same PLI of OP/OC of certain unrelated comparables at 13.81 per cent on the basis of multiple years data. On this basis, the assessee claimed that its international transactions were at arm's length price (ALP) falling within ± 5 per cent range.
- The TPO opined that the assessee developed several unique intangibles at its own cost which were profitably used by the AEs without compensating the assessee *qua* costs incurred on the development of such intangibles. He further held that the assessee was performing several critical and crucial functions on behalf of its AEs.
- In such backdrop of facts, the TPO came to hold that the assessee was not adequately compensated by its AEs and the Profit split Method (PSM) was required to be applied for determining the ALP of the international transactions under this segment.
- On the basis of PSM, TPO made certain addition to assessee's ALP.
- The DRP set aside assessee's objections.
- On appeal:

Held

- It can be seen from records that whereas the responsibilities of AEs extend to Contracting, pricing, sourcing, scheduling, procuring, inventory management, logistics, marketing, credit management, quality and compliance of global laws etc.; the responsibilities of the customer, vendors from India extend to Contracting, pricing, scheduling, negotiating, inventory etc. As opposed to these two sets of persons, namely, the AEs and the buyers/sellers from India, the assessee is acting as a mediator between them who is responsible for supplying marketing information, liaising with vendor and coordination.

- This material on record amply shows that the risk of the assessee in mediating between its AEs on one hand and suppliers/purchasers from India on the other, is limited and minimal with least capital employed. This is in sharp contrast to the findings returned by the TPO that the assessee was performing all the crucial and critical functions on behalf of the AEs.
- Despite the fact that this chart was placed before the TPO, he did not controvert any of the facts stated in it, but proceeded to record whimsical contrary observations to the effect that the assessee undertook all the critical functions of its AEs without spelling any further details as to which specific functions were performed by the assessee.
- There is no elaboration of any such critical functions except for the mention of the fact that the assessee was also engaged in arranging for feasibility studies, industry analysis, and project evaluation for potential projects identified by its AEs.
- Turning to such observations of the TPO that the assessee was also engaged in arranging for feasibility studies etc. for its AEs, it is found that this finding is incorrect. Definitely, the assessee was engaged in arranging for feasibility studies, industry analysis and project evaluation but such activities were done for non-AEs. It can be seen from the assessee's profit & loss account that the assessee's trading turnover to the non AEs is to the tune of Rs. 40.64 crore. Apart from that, the assessee also received service income of Rs. 5.14 crore in addition to commission income of Rs. 35.39 crore.
- From the details furnished by the assessee, it can be seen that out of total revenue of Rs. 81.71 crore, the receipts from AEs stand at Rs. 36.30 crore as against Rs. 45.13 crore from non-AEs, being the unrelated parties. The assessee has placed some material on record to demonstrate that no feasibility study etc. was conducted for the AEs, which position has not been repelled on behalf of the Revenue.
- Thus it is clear that the assessee was not arranging any feasibility studies/industry analysis and project evaluation for potential projects identified by its AEs. Rather, this activity was done for unrelated parties. The role of the assessee in the extant international transactions was basically confined to acting as a mediator between its AEs and buyers/sellers in India and also supplying marketing information to the AEs which could help them in taking their business decisions as to which item could be purchased or sold by them with reference to the macro opinion of Indian market made available by the assessee.
- This activity was done by sending certain articles or newspaper cuttings or other data from India with a view to help the AEs in indentifying the areas in which they could undertaken transactions. It is the case of the assessee that it was adequately compensated with a fixed fee from its AEs for extending such market support activities, which amount is part of the total revenue of Rs. 32.18 crore.
- The role of the assessee on this count is no more than sending such information. It was only for the AEs to take business decisions about any purchases or sales to be actually made by them to or from India. The Tribunal is unable to find any critical functions carried out by the assessee or any

significant risks assumed by the assessee by using its tangibles and unique intangibles in the transactions with AEs.

- On a specific query from the Bench, the revenue could not draw its attention towards any material to corroborate the findings recorded by the TPO in this regard which are contrary to what has been put forth before on behalf of the assessee with the relevant material.
- When the position is so that the assessee simply supplied some information to the AEs and acted as a mediator between its AEs and Indian enterprises in the transactions arranged independently between themselves, one fails to comprehend as to how the assessee can be characterized as assuming higher risk or using its highly valued intangibles. The specific submissions made before the TPO in the context of role played by the assessee as consisting of agency services and rendering managerial support services to the limited extent of providing necessary information in facilitating the AEs in taking decisions, has not been rebutted by the TPO.
- Instead, he *suo motu* visualized certain human chain and valuable intangibles of the assessee used in the international transactions without first proving their very existence with the assessee. Apart from repeatedly reiterating that the valuable intangibles which has benefited the group as a whole, the TPO has not substantiated his conclusion with any material.
- Considering the entirety of the facts and circumstances prevailing in the present case, the findings returned by the TPO - the assessee assuming substantial risks; doing critical functions for its AEs; and allowing the user of its highly valued intangibles to such AEs - are all in air without any bedrock.
- Now comes the question that if the PSM is not to be applied and there are, in fact, international transactions of provision of agency and marketing support services to the AEs amounting to Rs. 32.18 crore, then how to determine the ALP? The mere fact that PSM is not applicable to the facts of the present case does not mean that the applicability of Chapter X or the Act is ruled out. In such a situation, the ALP of the international transactions is required to be determined with another suitable method.
- It can be seen from the assessee's transfer pricing study that it selected TNMM as the most appropriate method and computed its PLI at 16.87 per cent. Certain comparables were chosen and on the basis of multiple years data, whose mean of OP/OC was computed at 13.81 per cent. There is force in the view adopted by the TPO that the multiple years data cannot be used, which proposition has not been disputed even by the assessee.
- It can be noticed from the TPO's order that he proceeded with the alternative approach on the penultimate page of his order by choosing nine comparables with the arithmetic mean margin of 43.12 per cent. However, such alternative approach was dropped in view of the decision of the Delhi Tribunal in *Li & Fung India (P.) Ltd. v. CIT* [2014] 361 ITR 85/223 Taxman 368/[2013] 40 taxmann.com 300 for applying the PSM. It shows that both the assessee as well as the TPO in alternative approach adopted TNMM for determining the ALP of the international transactions.
- The TNMM is the most appropriate method in the present set of circumstances. The assessee submitted that the exercise done by the TPO in pursuing the alternative approach was done at the

back of the assessee and no information was given as to which were the comparables and how their arithmetic mean margin was computed. There is no reference to the names of such comparables in the TPO's order. It is noticed that the TPO embarked upon the PSM throughout the length and breadth of his order. The alternative approach of TNMM was not given any serious consideration. Even there is no discussion about the comparables chosen by the assessee and how they were acceptable or not.

- Under such circumstances, the ends of justice would meet adequately if the impugned order is set aside and the matter is restored to the TPO/Assessing Officer for a fresh determination of the ALP of the disputed international transactions of 'provision of agency and marketing support services'.