

**आयकरअपीलीयअधिकरण, विशाखापटणमपीठ, विशाखापटणम**

IN THE INCOME TAX APPELLATE TRIBUNAL,  
VISAKHAPATNAM BENCH, VISAKHAPATNAM

**श्रीदुव्वुखारएलरेड्डी, न्यायिकसदस्यएवंश्रीएसबालाकृष्णन, लेखासदस्यकेसमक्ष**

BEFORE SHRI DUVVURU RL REDDY, HON'BLE JUDICIAL MEMBER &  
SHRI S BALAKRISHNAN, HON'BLE ACCOUNTANT MEMBER  
(Through Hybrid Hearing)

आयकरअपीलसं./ I.T.A. No.627/Viz/2018

(निर्धारणवर्ष/ Assessment Year : 2014-15)

Brandix Apparel India Private Vs. Assistant Commissioner of  
Limited, Income Tax,  
APSEZ, Pudimadaka Road, Circle-5(1),  
Atchutapuram Mandal, Visakhapatnam.  
Visakhapatnam – 530011.  
PAN: AACCB 6569 L

(अपीलार्थी/ Appellant)

(प्रत्यर्थी/ Respondent)

अपीलार्थीकीओरसे/ Assessee by

Sri Darpan Kriplani

प्रत्यर्थीकीओरसे/ Revenue by

Dr. Satyasai Rath, CIT-DR

सुनवाईकीतारीख/ Date of Hearing

03/01/2024

घोषणाकीतारीख/Date of

13/02/2024

Pronouncement

**ORDER**

**PER S. BALAKRISHNAN, Accountant Member :**

This appeal filed by the assessee against the final assessment order passed U/s. 143(3) r.w.s 144C of the Income Tax Act, 1961 [the Act] dated 29/10/2018.

2. Briefly stated the facts of the case are that the assessee is engaged in the provision of processing services in relation to manufacture of garments to the Brandix Group of companies. The assessee, M/s. Brandix Apparel India Private Limited (in short BAI) is compensated on a cost plus basis for such processing services. The assessee filed its return of income for the AY 2014-15 on 30/11/2014 admitting a total income of Rs. 3,80,09,800/-. Subsequently, the case was selected for scrutiny under CASS and notice U/s. 143(2) of the Act was issued on 8/9/2015 and served on the 21/9/2015. The assessee later filed a revised return of income on 31/3/2016 by claiming an exemption of Rs. 4,73,25,503/- U/s. 10AA of the Act and however, paid tax on book profits. Later on, notices U/s. 143(2) and 142(1) of the Act were issued on 12/7/2016. Further, notice U/s. 142(1) r.w.s 129 of the Act was issued on 25/10/2017 due to change in the incumbent. In response to the notices, the assessee's Authorized Representative appeared and submitted the documents called for as per the notice dt 25/10/2017. On perusal of the submissions made by the assessee's Representative, the Ld. AO noticed that the assessee has entered into an international transaction with its Associated Enterprises

[AEs] aggregating to Rs.268.19 Crs during the previous year relating to the AY 2014-15 as detailed below:

<b>Associated Enterprise</b>	<b>Nature of transaction</b>	<b>Amount (Rs)</b>
Brandix Essentials Limited	Fixed Assets	2,55,613
Brandix Essentials Limited	Purchase of Fixed Assets	59,59,880
Brandix Apparel Limited	Income from Processing Services	140,99,04,987
Brandix 13 PVT Ltd	Payment for services	1,01,672
Brandix Mauritius Holdings Ltd	Buy back of shares	42,14,93,000
Brandix Apparel Ltd	Recovery of expenses	93,76,528
Brandix Apparel Ltd	Recovery of expenses	66,96,55,903
Brandix Mauritius Holdings Ltd	Reimbursement of expartite	1,80,50,882
Brandix Essentials Ltd	Reimbursement of expenses	32,64,831
Brandix Apparel Ltd	Reimbursement of expenses	37,82,725
Brandix Intimate Apparel Ltd	Reimbursement of expenses	74,83,898
Brandix Apparel Ltd	Recovery of Pre-commencement	3,68,47,180
Brandix Apparel Ltd	Liability no longer required	9,91,13,198

3. Thereafter, the case was referred to the Ld. Transfer Pricing Officer, Hyderabad [TPO] after obtaining necessary approval from the Ld. Principal Commissioner of Income Tax-2, Visakhapatnam for determining the Arm's Length Price [ALP] U/s. 92CA(1) of the Act. The Ld TPO rejected the TP analysis and documentation of the assessee. The Ld. TPO carried out an independent search using Capitallineplus and Prowess databases by using the following filters:

(i)	Companies with Sales > 1 Crore
(ii)	Companies with Financial Year end 31/03/2014
(iii)	Companies with positive net worth
(iv)	Companies with diminishing revenue / persistent loss are rejected
(v)	Companies with extraordinary circumstances

	are rejected
(vi)	Companies with related party transactions less than 25%

The Ld. TPO using the above filters arrived at a different set of comparables and thereby the Arithmetic Mean of the Profit Level Indicator [PLI] of the comparables was computed as under:

S.No	Name of the Comparable	OR	OC	OP	OP/OC
1.	Maral Overseas Ltd	220453	194278	26175	13.47
2.	Kitex Garments Ltd	1595222544	1356526616	238695928	17.60
3.	SP Apparel Ltd	359959300	322750571	37208729	11.53
4.	Kewal Kiran Clothing Ltd	48835	42080	6754	16.05
5.	Sudar Industries Ltd	380818773	359408490	21410283	5.96
6.	Virat Industries Ltd	221778024	173896678	47881346	27.53
	Average				19.58

The Ld. TPO did not refute the TNMM as the most appropriate method [MAM]. The Ld. TPO issued a show-cause notice on 16/10/2017 asking the assessee as to why the additions as mentioned in the show-cause notice should not be made? In reply to the show cause notice, the assessee contended the comparability of the chosen comparables by the Ld. TPO for the following entities:

1. Maral Overseas Ltd
2. Kitex Garments Ltd
3. Kewal Kiran Clothing Ltd
4. Virat Industries Ltd

The main contention of the assessee is that the above comparables are in the business of manufacturing of garments and not in the processing services. The Ld. AR also objected to the Ld. TPO considering the outstanding receivables as international transaction and has applying the interest rate of 6.5% on the outstanding receivables by making an adjustment of Rs. 3,26,65,774/- in addition to the adjustment made on account of income from processing services for Rs. 27,35,22,396/-. The Ld. AO considering the upward adjustments made by the Ld. TPO passed a draft assessment order on 28/12/2017. Aggrieved by the draft assessment order, the assessee filed its objections before the Ld. Dispute Resolution Panel [DRP]. Before the Ld. DRP, the assessee made various submissions including objections were raised with respect to selection of comparables in relation to processing services and requested the Ld. DRP to exclude the companies which are functionally not comparable with that of the functions performed by the assessee. Further, the assessee also raised objections with respect to the notional

interest on overdue receivables before the Ld. DRP. Considering the submissions of the assessee, the Ld. DRP concluded that the assessee has performed all the activities relating to manufacturing functions such as procurement, warehousing, processing, packing & labeling and shipment. The Ld. DRP therefore by relying on the assessee's TP study report, rejected the plea of the assessee that it was a mere service provider and therefore it is functionally not comparable to manufacturer. Similarly, by relying on various judicial pronouncements, Ld. DRP directed the Ld. TPO to compute the interest on outstanding receivables thereby considering the outstanding receivables as international transaction as inserted by Finance Act, 2012 w.e.f 2002 and directed the Ld. TPO to allow a credit period of 30 days and compute the interest beyond the period of 30 days. The Ld. AO giving effect to the directions of the Ld. DRP passed the final assessment order on 29/10/2018 making the addition towards TP Adjustment of Rs. 28,14,06,365/-. Aggrieved by the final assessment order of the Ld. AO, the assessee is in appeal before us by raising the following grounds of appeal:

*"1. That the order of the Ld. ACIT, Circle-5(1), Visakhapatnam to the extent prejudicial to the appellant, is bad in law, contrary to the facts and circumstances of the case and is liable to be quashed.*

2. *The Ld. DRP erred in not appreciating that the order of the Ld. DCIT, TPO-2, Hyderabad passed U/s. 92CA of the Act is contrary to law and thus liable to be quashed.*

3. *That on the facts and in the circumstances of the case, the Ld. AO / TPO and the Ld. DRP erred in making an upward adjustment to the transfer price of the appellant's international transactions of Rs. 273,522,396 on account of imputation of notional interest on outstanding receivables.*

**Grounds for processing services:**

4. *On the facts and in the circumstances of the case and in law, with respect to adjustment to the transfer price of processing services the Ld. DRP / AO / TPO erred in*

4.1. *Rejecting the TP documents maintained by the appellant U/s. 92D of the Act in good faith and with due diligence.*

4.2. *Rejecting the comparability analysis carried out by the assessee in TP documentation and in conducting a fresh comparability analysis for processing services.*

4.3. *Not providing any methodical search process during the course of assessment proceedings based on which the comparability analysis was undertaken by the Ld. TPO and accordingly, cherry picking the most favourable companies while arriving at the arm's length mark-up.*

4.4. *Using data, which was not contemporaneous and which was not available in the public domain at the time of preparing the TP documentation.*

4.5. *Not considering the multiple year / prior year data of comparable companies while determining the arm's length price in relation to the appellant's international transactions with its AEs.*

4.6. *Characterizing the appellant as in entrepreneur undertaking manufacturing activities, where in fact, the appellant is a low risk captive service provider undertaking processing services for its AEs.*

4.7. *Including companies that are functionally different from the operational profile of the appellant.*

4.8. *Excluding the companies selected by the appellant in its TP documentation without providing any cogent reasons for exclusion.*

4.9. *Not considering liabilities no longer required written back as operating in nature while computing the mark-up of the appellant.*

4.10. *Not considering certain expense such as provision for doubtful debts, provision for warranties, provision of doubtful deposits, and miscellaneous expenditure written off, as operating in nature on the premise that these are not the routine operating costs in determining the operating mark-up of the comparable companies.*

4.11. *Considering foreign exchange loss as operating in nature while determining the mark-up on cost of the appellant.*

4.12. *Not providing appropriate adjustments towards material difference between the operational profile of comparable companies and the appellant.*

**Grounds for imputation of notional interest outstanding receivables.**

5. *On facts and in the circumstances of the case, the Ld. DRP/AO/TPO erred in:*

5.1. *Considering overdue receivables from AEs as an international transaction under the provisions of section 92B of the Act.*

5.2. *Without prejudice to ground no. 5.1 above, ignoring the fact that the appellant does not pay interest to the AEs in relation to outstanding payable to AEs.*

5.3. *Without prejudice to Ground Nos. 5.1 & 5.2 above imputing interest using SBI term deposit rate instead of LIBOR.*

6. *That the Ld AO erred in levying interest U/s. 234B & 234C of the Act."*



4. At the outset, the Ld. Authorized Representative [AR] argued that the assessee is a job work service provider and does not manufacture goods which is evident from the fact that the assessee is not holding any inventories. It was further submitted by the Ld. AR that the assessee's source of income is "income from processing services" for Rs. 140,99,04,987/-. The Ld. AR vehemently objected to the three comparables viz., (i) Kitex Garments Ltd, (ii) Kewal Kiran Clothing Ltd and (iii) Virat Industries Ltd by stating that these three companies are manufacturers of garments and are not engaged in processing services. In fact the Ld AR submitted that these comparables outsource processing services and incurs huge processing expenses. It was submitted that therefore these companies are not comparable to the assessee-company and hence required to be excluded. The Ld. AR also in his written submissions stated that from the annual reports of M/s. Kewal Kiran Clothing Ltd in Note 2.15 discloses that it holds huge inventories for the purpose of manufacturing activities. Similarly, the Ld. AR also referred to Note 2.25 wherein M/s. Kewal Kiran Clothing Limited has paid huge processing charges of Rs. 1,866.46 lakhs. The Ld. AR also referred to the fact that M/s. Kewal Kiran Clothing Limited manufactures "Killer" brand materials for sale. Similarly, the Ld.

AR also referred to the financial statement of M/s. Kitex Garments Limited wherein under "corporate information" it is mentioned that the company is engaged in the manufacturing of fabric and readymade garments. Further, the Ld. AR also referred to Note-22 wherein M/s. Kitex Garments Limited has paid an amount of Rs. 12,09,77,618/- as processing charges. The Ld. AR also argued that similar information is stated in the case of M/s. Virat Industries Limited wherein this company has also paid the processing charges of Rs. 1,34,26,071/- as mentioned in Note 26 of the financial statements. The Ld. AR therefore pleaded that all the three companies outsourced the processing of the finished goods and has paid for the manufacturing of branded garments. It was further submitted that in the instant case, the assessee is not engaged in manufacturing of branded garments but only processes garments as per the specifications of the customers under the directions of the parent company viz., Brandix Apparel Company, Sri Lanka, (in short referred as BAL). The Ld. AR therefore pleaded that the three comparables may be removed from the calculation of Arithmetic Mean of the PLI with that of the assessee.

5. Countering the arguments of the Ld. AR, the Ld. DR argued that from the analysis of the P & L Account, it is seen that the net book profit declared by the assessee is equivalent to the other income. Further, the Ld. DR also referred to the agreement between the Brandix Apparel India Pvt Limited and Brandix Apparel Limited, Sri Lanka wherein it was stated that the assessee is a "contract manufacturer". Further, the Ld. DR also referred to the TP study of the assessee wherein it was mentioned that a large scale manufacturing facilities was established in Brandix India SEZ, Visakhapatnam and argued that the assessee maintains huge assets which are required for process of the manufacturing activities. The Ld. DR also referred to a flow diagram submitted in page 108 wherein the significant functions performed by BAI states that the assessee is engaged in procurement, warehousing, processing, packing & labeling and shipment. The Ld. DR also submitted that the assessee directly supplies to the end customers and not to BAL.

6. Objecting to the arguments of the Ld. DR, the Ld. AR submitted that the agreement between the BAI and BAL as per clause-2 is with respect to supply of services only. The Ld. AR also reiterated that the assessee does not carry any inventory

and the procurement is funded by BAL, and BAI does not bear the risk for the manufactured goods. The Ld. AR also referred to the revenues of Kewal Kiran Clothing Limited and also referred to the segment reporting furnished by Kewal Kiran Clothing Limited wherein it can be seen that it is engaged in earning revenues from various segments. The Ld. AR reiterated that the assessee is engaged only in one segment i.e., processing services. The Ld. AR also submitted that similarly Kitex Garments Ltd and Virat Industries Ltd were also engaged in various activities and also cannot be compared with the assessee-company. The Ld. AR also once again pleaded that since the said three companies are functionally different from the operational profile of the assessee-company, these companies are to be excluded from the comparables. Further, the Ld. DR submitted that as per the annual report of Kewal Kiran Clothing Limited it has not provided the segmental information as it has not crossed the threshold limit as prescribed under Accounting Standard-17 [AS] of the Institute of Chartered Accountants of India [ICAI] and hence not provided the same.

7. We have considered the rival contentions and perused the material available on record and the written submissions made by the assessee.

8. **Grounds No. 1 and 2 are general in nature** and therefore they need no adjudication.

9. **Ground No.3** relates to the upward adjustment made by the Ld. TPO / AO for which specific grounds have been raised vide Grounds No. 4 and 5 and accordingly it has been adjudicated.

10. **Grounds No. 4.1 to 4.8** relate to the selection of comparables by the Ld. TPO wherein the plea of the assessee is that the objections of the assessee in the selection of comparables by Ld TPO, were not considered by the Ld. DRP. On this issue, the main contention of the Ld. AR is that the assessee in its TP document submitted before us has determined the ALP of the Tested Party based on the combined results of Search-1 and Search-2 and has arrived at the following comparables and computed the arithmetic mean accordingly:

SI No	Name of the Company	Data Source	Average NPI
1.	Sudar Industries Ltd	P	13.53%
2.	Suryakiran International Ltd	P	4.86%
3.	Caprolactam Chemicals Ltd	P	3.45%

4.	Laurel Organics Ltd	P	11.90%
5.	Sampre nutritions Ltd	P	8.04%
6.	Spice Islands Apparels Ltd - Garment	P-Seg	-0.25%
7.	Superhouse Ltd - Textile Garments	P-Seg	8.83%
8.	Suryavanshi Spinning Mills Ltd - Garments	P-Seg	11.95%
9.	Anup Malleables Ltd	P-Seg	8.35%
10.	Khator Fibre & Fabrics Ltd - processing	P-Seg	11.99%
11.	Maral Overseas Ltd - Textile Made-ups	P-Seg	8.06%
12.	Maxwell Industries Ltd - Hosiery & Others	P-Seg	5.11%
	<b>Mean</b>		<b>7.98%</b>
	<b>Median</b>		<b>8.21%</b>
	<b>Lower Quartile</b>		<b>8.04%</b>
	<b>Upper Quartile</b>		<b>8.83%</b>

The contention of the assessee in Ground No.4.8 is with respect to rejection of the TP documentation by the Ld. TPO without assigning any cogent reasons. From the order of the Ld. TPO, we find that the Ld. TPO has generally mentioned that the search process made by the assessee in the TP document is not in conformity with the TP regulations and also the choice of filters selected by the assessee resulted in selection of inappropriate comparables. However, the Ld. TPO did not elaborate on the inappropriate filters adopted by the assessee. We also find that the Ld. TPO has made an independent search using Capitallineplus and Prowess databases by adopting the following filters:

(i)	Companies with Sales > 1 Crore
(ii)	Companies with Financial Year end 31/03/2014
(iii)	Companies with positive networth
(iv)	Companies with diminishing revenue / persistent loss are rejected
(v)	Companies with extraordinary circumstances are rejected
(vi)	Companies with related party transactions less than 25%

The Ld. AO thus arrived at the following comparables thereby computed the OP/OC as detailed below:

S.No	Name of the Comparable	OR	OC	OP	OP/OC
1.	Maral Overseas Ltd	220453	194278	26175	13.47
2.	Kitex Garments Ltd	1595222544	1356526616	238695928	17.60
3.	SP Apparel Ltd	359959300	322750571	37208729	11.53
4.	Kewal Kiran Clothing Ltd	48835	42080	6754	16.05
5.	Sudar Industries Ltd	380818773	359408490	21410283	5.96
6.	Virat Industries Ltd	221778024	173896678	47881346	27.53
	Average				19.58

The objection of the assessee is with respect to inclusion of the following comparables which were functionally considered as comparables by the Ld TPO with that of the assessee whereas according to assessee, which are in fact not comparable viz., (i) Kitex Garments Ltd, (ii) Kewal Kiran Clothing Ltd and (iii) Virat Industries Ltd. The assessee also vide in its grounds of appeal pleaded to reject the above three comparables as they are functionally different from that of the operational profile of the assessee-company.

**(i) Comparable of Kitex Garments Ltd:**

From the submissions of the assessee-company and on going through the annual report filed by the Ld. AR, we find that Kitex Garments Limited is engaged in manufacturing of fabrics and export its fabrics and sells to domestic customers directly. Further, from Note-22 of the annual report, we find that Kitex Garments Limited has incurred processing charges wherein the contention of the Ld. AR is that Kitex Garments Limited has sub-contracted the work to other entities like that of the assessee. We find from the annual report (page 40) that Kitex Garments Limited is engaged in manufacture of fabric and readymade garments and exports the same. Thus in our opinion, Kitex Garments Limited is engaged in the manufacturing process whereas the assessee is engaged in the business of processing of garments thereby leading to the conclusion that the operations of Kitex Garments Limited are functionally different from that of the assessee-company. We therefore direct the Ld. TPO to exclude Kitex Garments Limited from the list of comparables for the aforesaid reasons.



**(ii)Comparable of Kewal Kiran Clothing Ltd:**

From the annual report submitted by the assessee we find that Kewal Kiran Clothing Limited is the owner of brands such as "Killer" and operating in a different operating model by holding huge inventories. Further, we find that Kewal Kiran Clothing Limited is also engaged in the business of manufacturing and marketing of apparels and trading of lifestyle accessories and generating power from Wind Mills. Further, Kewal Kiran Clothing Limited is also engaged in branding and advertising activities under its brand name "Killer". This leads to the conclusion that Kewal Kiran Clothing Limited is engaged in a diversified activities and deriving income from various kinds of operations whereas the assessee is engaged only in one activity i.e., processing services. Further, we also find from the annual report Kewal Kiran Clothing Limited has incurred huge processing charges by sub-contracting the work to other entities such as the assessee-company. We therefore are of the opinion that Kewal Kiran Clothing Limited is functionally different from that of the operations of the assessee and hence it cannot be considered as a comparable for the computation of ALP of the assessee and

thereby directing the Ld. TPO to exclude Kewal Kiran Clothing Limited from the list of comparables for the aforesaid reasons.

**(iii) Comparable of Virat Industries Ltd:**

From the annual report submitted by the assessee, it is found that Virat Industries Limited focuses on manufacturing of socks from yarn whereas the assessee is engaged in processing of garments from fabrics. Similar to the above two entities viz., Kitex Garments Limited and Kewal Kiran Clothing Limited, Virat Industries Limited also holds huge inventories and fully engaged in the manufacturing of garments. We also find that Virat Industries Limited has also engaged in sub-contracting the processing works to job-workers such as the assessee-company. Therefore, in our opinion, Virat Industries Limited is functionally different from that of the assessee-company and cannot be considered as a comparable for the computation of ALP with that of the assessee-company for the aforesaid reasons. Accordingly, we hereby direct the Ld. AO to exclude Virat Industries Limited from the list of comparables. Thus, Grounds No. 4.1 to 4.8 raised by the assessee are allowed.

11. With respect to **Ground No 4.9** regarding liabilities no longer required written back whether it has to be treated as operating income or non-operating income while computing the mark-up of the assessee, the Ld. AR relied on the judgment of the Hon'ble Bombay High Court in the case of Pr. CIT-4 vs. Tetra Pak India Pvt Ltd in Income Tax Appeal No. 876 of 2018. The Ld. AR referred to para 8 of the said decision of the Bombay High Court which is extracted herein below:

*"8. As regard the credit to profit and loss account on account of liabilities written back amounting to Rs. 6,15,59,011/- the details of the liabilities written back were made available to CIT(A) as well as ITAT. Both, on facts, and having considered those details, have come to conclusion accepting the Assessee's contention that those liabilities belong to earlier years and are directly relatable to the regular business operations of the assessee and since these liabilities were no longer payable to business creditors should be allowed to be written back in the AY under consideration and the same was rightly offered to tax as business income U/s. 41(1) of the Act. Therefore, on facts it was accepted that these liabilities written back were arising out of normal business operations and hence form part of operating income of the assessee."*

The Ld. AR therefore submitted that the AE waived the air freight charges relatable to regular business operations of the assessee, and hence the assessee has written back the liability as no longer payable. Further, the Ld. AR submitted that the details of these expenditure which was allowed as operating expenditure in the earlier years was also submitted before the Ld. AO. The Ld AR

pleaded that since it was treated as operating expenditure in the earlier years, the liability for such expenditure which was created in earlier years and written back in the current assessment year and therefore should be treated as an operating income. Countering the arguments of the Ld. AR, the Ld. DR submitted that the issue before the Hon'ble Bombay High Court is factually different because as per 4-B of the substantial question of law raised before the Hon'ble Bombay High Court is with respect to whether this item represents provisions made in the earlier years which has been reversed in AY 2002-03 and do not constitute income from the operations of the assessee. The Ld. DR therefore submitted that it was provision of two earlier years and not an expenditure which was reversed and therefore the case relied on by the assessee is factually different from the present facts of the assessee's case.

12. We have heard the rival contentions. The assessee has incurred air freight expenses for which liability which was created in the books of accounts in the prior years has been written off during the impugned assessment year, since it is no longer considered as a liability in the books of accounts of the assessee. In this connection, the assessee has also submitted

the waiver letter issued by Brandix Apparels Limited, Sri Lanka which is enclosed in page 44 of the paper book. These air freight expenses when incurred in the prior years wherein it was included in the operating cost of the assessee. However, the Ld. TPO has considered it as non-operating when this liability has been written back in the impugned assessment year. Reliance placed by the assessee in the case of Pr. CIT vs. Tetra Pak India Ltd (supra) wherein in para 8 of its order, the Hon'ble Bombay High Court has held as follows:

*"8. As regard the credit to profit and loss account on account of liabilities written back amounting to Rs. 6,15,59,011/- the details of the liabilities written back were made available to CIT(A) as well as ITAT. Both, on facts, and having considered those details, have come to conclusion accepting the Assessee's contention that those **liabilities belong to earlier years and are directly relatable to the regular business operations of the assessee and since these liabilities were no longer payable to business creditors should be allowed to be written back in the AY under consideration and the same was rightly offered to tax as business income U/s. 41(1) of the Act.** Therefore, on facts it was accepted that these liabilities written back were arising out of normal business operations and hence form part of operating income of the assessee."*

The argument of the Ld DR could not be accepted for the reason that in accounting principles that a liability in the form of provision shall be created in the books of accounts in the year of accrual of expenses until the actual payment is made. Since this

liability was waived off by BAL, it was written back and considered as income in the impugned AY. Respectfully following the ratio laid down by the Hon'ble Bombay High Court in the case of Pr. CIT vs. Tetra Pak India Ltd (supra), we direct the Ld. AO to include the liabilities written back in the impugned assessment year as operating income.

13. With respect to **Ground No. 4.10** the Ld. AR contended that these expenditure were considered as operating expenditure in the previous years and thereby similarly when these expenses are being written off in the subsequent years as no longer payable it has to be considered as operating income in the year in which it has been written off. The Ld DR relied on the orders of Revenue authorities.

14. We have heard the rival contentions. The assessee has raised the issue that the Ld. TPO has not considered certain expenses such as provision for doubtful debts, provisions for warranties, provision of doubtful deposits and miscellaneous expenditure written off as operating in nature. The submission of the Ld. AR that due to political instability in Visakhapatnam arising out of the agitations due to bifurcation of the separate state of Telangana, the assessee was forced to incur certain

expenditure to minimize the impact of the agitations on the work output of the processing unit. However, the Ld. Revenue Authorities rejected the contention of the Ld. AR stating that the assessee has not furnished any details of the expenses before the Ld. TPO. We therefore direct the assessee to produce the details of expenditure incurred by the assessee which was considered as extraordinary to the Ld. TPO / AO. We direct the Ld. AO / TPO to provide one more opportunity to the assessee for submission of the details of expenditure and decide the allowability in accordance with law. Accordingly, this ground raised by the assessee is allowed for statistical purposes.

15. The Ld. AR also argued with respect to **Ground No.4.11** that the foreign exchange loss is non-operating in nature in the determination of the mark-up on cost of the assessee. Countering the arguments of the Ld. AR, the Ld. DR referred to the Ld. TPO order wherein it is observed as a transaction loss and not a hedging loss and hence it has to be considered as a operating in nature. The Ld DR placed reliance in the case of NVH India Auto Parts P Ltd vs DCIT [156 taxman.com 330 (Chennai Trib)] and Phoenix Comtrade P Ltd vs DCIT [149 taxman.com 389 (Mumbai

Trib)] wherein it was held that Foreign exchange loss is operating in nature.

16. We have heard the rival contentions. The Ld. AR's submission was that the foreign exchange loss was considered as operating in nature, whereas the Ld. TPO has stated in his order that the foreign exchange loss should be considered as non-operating. The Ld. TPO in para 11(d) of the order passed U/s. 92CA(3) has observed as under:

*"11(d). Hence, foreign exchange fluctuations on account of hedging cannot be considered as an operating item and thus the taxpayer contention cannot be accepted."*

Thus, the Ld. TPO has observed that the foreign exchange fluctuations on account of hedging operations cannot be considered as operating item. However, in the instant case we find that the assessee has not engaged in hedging activities and foreign exchange loss is a transactional loss and in our opinion it should be considered as an operating cost for mark-up purposes. Further there is also merit in the argument of the Ld DR wherein the ratio laid in the cases NVH India Auto Parts P Ltd (supra) and Phoenix Comtrade P Ltd (supra) was emphasised. Therefore, we



find no infirmity in the order of the Ld. Revenue Authorities and accordingly, this ground raised by the assessee is dismissed.

17. With respect to **Ground No. 4.12**, the assessee has pleaded that material difference providing appropriate adjustments in the working capital between the assessee and the comparable companies selected by the Ld. TPO was not considered by the Ld. DRP. Per contra, the Ld. DR relied on the order of the Ld. DRP.

18. We have heard both the sides and perused the material available on record as well as the orders of the Ld. Revenue Authorities on the issue. From the directions of the Ld. DRP in para 2.5.1, it is observed that the Ld. DRP has held that the assessee has not demonstrated with any data or information and the impact of difference on the pricing, cost and profits. Even before us, the Ld. AR has not provided any documents regarding the working capital adjustments. Following the principles of natural justice, in order to provide one more opportunity to the assessee, we hereby direct the Ld. AO / TPO to consider the impact of working capital adjustments of the assessee company and appropriate material differences with that of the comparable companies and decide on this issue accordingly. We also direct the assessee to submit necessary documentation to the Ld. AO /

TPO on this issue. Accordingly, this ground raised by the assessee is allowed for statistical purposes.

19. With respect to **Ground No.5** on the computation of the notional interest on outstanding receivables, the contention of the Ld. AR that outstanding receivables cannot be considered as an international transaction and therefore no adjustment can be made with respect to the notional interest on the outstanding receivables. The Ld. DR submitted that this Bench of the Tribunal in the case of Devi Sea Foods limited (supra) vide para-7 of its order, the Tribunal has held that receivables is included under the definition of international transaction consequent to the amendments made by the Finance Act, 2012 w.e.f 01.04.2002 and hence it is an international transaction.

20. We have heard the arguments. This Bench of the Tribunal in the case of Devi Sea Foods limited (supra) vide para-7 of its order, the Tribunal has held as follows:

*"7. We have heard the rival submissions and perused the material available on record and the orders of the Authorities below. Admitted facts are that the assessee sells to both the AEs non-AE where the AE being the major debtor. There is no dispute with regard to the fact that receivables is included under the definition of international transaction consequent to the amendments made by the Finance Act, 2012 w.e.f 01.04.2002. Therefore we are of the considered view that there is no merit in the argument of Ld AR that receivables is not an international transaction. "*

We therefore following the same ratio, reject the arguments of the Ld. AR that outstanding receivable is not an international transaction. Having said so, the issue is whether separate adjustment is required to be made in respect of receivables, the contention of the Ld. AR is that the average realization period is only 79.63 days which is within the industry standards and hence notional interest should not be imputed. The notional interest is charged by the Ld. AO based on the SBI Term Deposit Rate has adopted 6.50% on the outstanding receivables beyond a period of 30 days as directed by Ld DRP. The Ld. AR also pleaded the working capital adjustment shall also be undertaken for the companies selected as comparables by the Ld. TPO. The Ld. DR submitted that the Ld. TPO has taken lowest rate for the application of interest on outstanding receivables from the website of SBI Term Deposit Rates for the term under consideration. The Ld. DR also referred to page 364 of the paper book wherein the assessee in the computation of share valuation has adopted a discount rate of 15.58%. The Ld. DR also referred to page 472 of the paper book wherein the assessee's basis for interest payable is one month LIBOR + 3.5% on the ECBs obtained by them. He therefore pleaded that the Ld. TPO has

rightly considered the rate and hence needs to be upheld. Countering the arguments of the Ld. DR, the Ld. AR submitted that when TNM method is used, no adjustment can be made with respect to notional interest of outstanding receivables as it is already subsumed in the computation of ALP under TNM method. On this issue the Ld AR relied on the case of Devi Sea Foods (supra) and pleaded that the same ratio be applied.

21. We have heard the rival contentions. We find that from the directions of the Ld. DRP that the assessee has not demonstrated the working capital adjustments before the Ld. Revenue Authorities while determining the ALP under TNM method both for the Tested Party and the comparables. In the case of Devi Seafoods Ltd (supra) this Bench has taken the following view:

*When TNM method is considered as the most appropriate method, which was also not disputed by Revenue, the net margin thereunder would take care of such notional interest cost. It was further explained by Ld.AR that the impact of the delay in collection of receivables would have a bearing on the working capital of the assessee. We find that these working capital adjustments on the ALP has been already factored in its pricing / profitability vis-à-vis that of its comparables. We therefore are of the considered view that any further adjustment to the margin of the assessee on the outstanding receivables cannot be justified and no separate upward adjustment on outstanding export receivables is required and therefore we direct the Ld.AO to delete the upward adjustment made towards overdue receivables from AE. We therefore allow this ground raised by the assessee.*

22. We hereby direct the Ld. AO / TPO to examine and consider the appropriate adjustments arising out of the working capital differences in the computation of the ALP. The assessee is also directed to submit the working relating to working capital adjustments of the assessee company. Following the principle of consistency if the working capital adjustments on the ALP has been already factored in its pricing / profitability vis-à-vis that of its comparables further adjustment to the margin of the assessee on the outstanding receivables cannot be justified and no separate upward adjustment on outstanding receivables is required, since TNM method is considered as the most appropriate method, which was also not disputed by Revenue, the net margin thereunder would take care of such notional interest cost. Accordingly, this ground raised by the assessee is allowed for statistical purposes.

23. **Ground No.6** is with respect to interest U/s. 234B and C which are **consequential in nature and therefore needs no adjudication.**

24. In the result, appeal of the assessee is partly allowed for statistical purposes as indicated herein above.

Pronounced in the open Court on 13<sup>th</sup> February, 2024.

Sd/-

(दुव्वुळार.एलरेड्डी)

(DUVVURU RL REDDY)

न्यायिकसदस्य/JUDICIAL MEMBER

Sd/-

(एसबालाकृष्णन)

(S.BALAKRISHNAN)

लेखासदस्य/ACCOUNTANT MEMBER

Dated :13.02.2024

OKK - SPS

आदेशकीप्रतिलिपिअग्रेषित/Copy of the order forwarded to:-

1. निर्धारिती/ The Assessee-Brandix Apparel India Private Limited, APSEZ, Pudimadaka Road, Atchutapuram Mandal, Visakhapatnam – 530011.
2. राजस्व/The Revenue –Assistant Commissioner of Income Tax, Circle-5(1), Visakhapatnam.
3. The Principal Commissioner of Income Tax,
4. आयकरआयुक्त (अपील)/ The Commissioner of Income Tax
5. विभागीयप्रतिनिधि, आयकरअपीलीयअधिकरण, विशाखापटणम/ DR,ITAT, Visakhapatnam
6. गार्डफ़ाईल / Guard file

आदेशानुसार / BY ORDER

Sr. Private Secretary  
ITAT, Visakhapatnam