आयकर अपीलीय अधिकरण
मुंबई पीठ"के",मुंबई
श्री विकास अवस्थी, न्यायिक सदस्य एवं
श्री गगन गोयल, लेखाकार सदस्य के समक्ष
IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "K", MUMBAI
BEFORE SHRI VIKAS AWASTHY, JUDICIAL MEMBER &
SHRI GAGAN GOYAL, ACCOUNTANT MEMBER
आ.अ.सं.338/मुं/2014(नि.व.2009-10)
ITA NO.338/MUM/2014 (A.Y. 2009-10)

Fulford (India) Limited,
Platina Building, 8th Floor,
C-59, G-Block, Bandra Kurla Complex,
Bandra (East), Mumbai – 400 098
PAN: AAACF-1795-L ..... अपीलार्थी/Appellant

बनाम Vs.

Dy.Commissioner of Income Tax, Circle 2(1),
Room NO.561, 5th Floor,
Aaykar Bhavan, M.K.Road,
Mumbai – 400 020. ..... प्रतिवादी/Respondent

Assessee by : Shri P.J. Pardiwala, Sr. Advocate with
Shri Madhur Agrawal, Advocate
Revenue by : Dr. Yogesh Kamat, CIT-DR &
Shri Ujjwal Kumar Chavan, Sr.AR

सुनवाई की तिथि/ Date of hearing : 10/11/2023
घोषणा की तिथि/ Date of pronouncement : 06/02/2024

आदेश/ORDER

PER VIKAS AWASTHY, JM:

This appeal by the assessee is directed against the assessment order dated 13/12/2013 passed u/s. 143(3) r.w.s. 144C(13) of the Income Tax Act, 1961 [in short 'the Act'], for the Assessment Year 2009-10.

2. The facts of the case in brief are: The assessee/appellant is engaged in the business of manufacturing and distribution of Pharmaceutical Products in

India. The assessee is a subsidiary of Schering-Plough Corporation, USA. During the period relevant to the Assessment Year under appeal, the assessee entered into various international transactions with its Associated Enterprise(AE). During the course of assessment proceedings the Transfer Pricing Officer (TPO) made adjustment in respect of following international transactions:

Sl.No.	Description of international transaction	Adjustment made by TPO (Amount in Rs.)
1.	Import of Active Pharmaceutical Ingredients (APIs)	4,81,96,325
2	Import of Finished Drug Formulations (FDF)	15,75,53,000
	Total	20,57,49,325

The assessee filed objections before the Dispute Resolution Panel(DRP) assailing the adjustments but the same were rejected. Hence, the present appeal by the assessee.

3. The assessee in appeal has raised following two primary grounds assailing adjustments made in the impugned order.

(i) Re-computation of Arm's Length Price (ALP) of the international transactions in relation to import of Active Pharmaceutical Ingredients (APIs) – Adjustment of Rs.4,81,96,325/-.

(ii) Re-computation of ALP in relation to import of formulations – Adjustment Rs.15,75,53,000/-.

4. Shri P.J. Pardiwala appearing on behalf of the assessee submitted that the assessee is engaged in the business of manufacturing and distribution of pharmaceutical products in India. The assessee does not have its own

manufacturing facility, thus, the assessee engages third party for manufacturing of pharmaceutical products. The business of assessee can be divided in four segments, viz:

(i) Tolling: Import of APIs from AEs and converting the same into formulations by using services of third party viz. Gland Pharma.

(ii) Tolling: Import/purchases of APIs from third party (non-AE) and thereafter, converting the APIs into formulations using third party manufacturing facility under the supervision of the assessee.

(iii) Contract manufacturing: The assessee engages third party viz. Zyg Pharma and Encore Pharma to purchase the APIs from approved sellers of API, manufacture the formulations as per specifications given by the assessee, under supervision of the assessee and under the Brand name of assessee.

(iv) Distribution: In this segment the assessee purchases finished formulations from its AEs and distributes/sells the same in India. The assessee acts as a distributor of the formulations manufactured by its AEs.

The ld. Counsel for the assessee submits that in so far as segment (ii) and (iii) are concerned there is no dispute. The dispute is with respect to determination of arm's length pricing (ALP) in segment (i) and (iv).

IMPORT OF APIs FROM AEs:

5. The ld. Counsel for the assessee submits that in transfer pricing study the assessee has characterized its activities of tolling as 'Licensed Manufacturer', exposed to less than normal risk as compared to full fledged

manufacture. During the proceedings before the TPO the assessee re-characterized its status from 'Licensed Manufacturer' to 'Value Added Distributor' (VAD). The assessee to benchmark its transaction applied Transactional Net Margin Method (TNMM) as the most appropriate method for determining ALP of the international transaction for purchase of APIs from its AEs. The APIs is the active ingredient or the main ingredient of the formulations. The cost of conversion of APIs to formulations is miniscule and work of conversion of API to formulation is performed by an independent third party. The assessee has entered into an agreement with Gland Pharma for the process of conversion of API to formulations, for which Gland Pharma is remunerated at arm's length. The assessee only performs the functions of a distributor for marketing and selling formulations manufactured by third parties. The process of conversion of APIs into formulations is only a value addition performed by the assessee. Therefore, the assessee should be treated as VAD and compared to other distributors while applying TNMM.

5.1 Without prejudice, even if, the assessee is treated as manufacturer still TNMM is the most appropriate method for determination of the ALP. The ld. Counsel for the assessee submitted that in the process of tolling, the APIs risk is that of the AE and the assessee had minimal risk. In the process of manufacturing/conversion of APIs into formulation the quality control is maintained by the AE.

6. Assailing the findings of the TPO, the ld. Counsel for the assessee submitted that the TPO rejected TNMM as the most appropriate method for determination of ALP adopted by the assessee and instead, applied CUP as the most appropriate method. For applying CUP the TPO collected data from the Customs Data Base(TIPS) in respect of APIs:

(i) Dexchlorpheniramine Maleate

(ii) Mometasone

The TPO in exercise of his powers u/s. 133(6) of the Act selected Cipla Ltd. as comparable for Netilmicin. The TPO compared the rate in TIPS data based in respect of other two APIs which certain parties were also importing allegedly from outside India with the rates at which the assessee was purchasing the APIs from its AEs. The TPO also disregarded the submissions of the assessee that assessee is nothing more than a VAD for the purchase of APIs. The ld. Counsel for the assessee asserted that even if, assessee is treated as manufacturer CUP cannot be applied as most appropriate method over TNMM. He referred to the provisions of Rule 10B(2) of the Income Tax Rules, 1962[in short 'the Rules'] that provides the parameters for judging the international transactions with uncontrolled transactions. The ld. Counsel for the assessee further submitted that the information gathered by the TPO from TIPS data base does not have relevant information for applying CUP. TIPS data base does not give name of the parties to the transactions, the contractual terms with respect to the transactions, sample of the goods sold, etc. For determination of ALP one has to see uncontrolled transaction i.e. transaction between two unrelated parties. In the present case, information provided by the Revenue, lacks vital details viz:

(i) The transaction between related/unrelated party;

(ii) Terms of contract, payment terms, other relevant circumstances with respect to the contract rate.

FAR of the alleged unrelated transactions cannot be compared with the FAR of the assessee. The assessee vide its detailed submissions had brought these

facts before the TPO and the DRP, but, they failed to appreciate the submissions of the assessee.

6.1 . The ld.Counsel for the assessee placed reliance on the following decisions to contend that TIPS data base cannot be relied upon to apply CUP in the absence of relevant supporting information:

(i) Tilda Riceland Pvt. Ltd. vs. ACIT, 42 taxmann.com 400 (Del-Trib)

(ii) ACIT vs. Billion Wealth Minerals Pvt. Ltd, 90 taxmann.com 170(Mum.)

(iii) DCIT vs. UCB India Ltd., 70 taxmann.com 164 (Mum-Trib).

6.2 He further submitted that merely for the reason that the name of the product is same, i.e. Mometasone, it cannot be said that the products are comparable without actual comparability analysis of the products purchased by the assessee and products purchased by alleged independent third parties. The TPO while determining comparability of assessee's product with that of the independent third party has not examined the sample of the product purchased by third party. In the backdrop of these facts CUP cannot be applied as the most appropriate method . CUP require high degree of comparability of the products to determine ALP. In support of his submissions he placed reliance on the decision in the case of Merck Ltd. vs. DCIT, 148 ITD 513(Mum).

7. The ld.Counsel for the assessee submits that the observation of the TPO that the product purchased by third party as well as the assessee fulfils the quality standard provided by Indian Food and Drug Administration (FDA), therefore, the products are comparable is erroneous and incorrect. The APIs purchased by the assessee from AE not only meets the Indian FDA

requirements but also qualifies stringent requirement of European FDA. Whereas, in respect of third party no data is available to show that the purchased products fulfils European FDA requirements. The ld. Counsel for the assessee submits that even though the higher and stringent requirement may not be necessary for selling the drugs in India, the products procured by the assessee from AE are much superior in quality, hence, cannot be compared with the APIs that fail to qualify stringent tests by European FDA. There is no material available on record as to whether the drugs purchased by the third party fulfils Indian FDA requirements or the purchaser after purchasing the drugs carry out further processing on the APIs to make Indian FDA compliance. In the absence of such details and information CUP cannot be applied to determine ALP. Hence, it is not possible to make adjustment as provided in Rule 10B(1)(a) for differences if any, between the international transactions and uncontrolled transactions.

8. The ld.Counsel for the assessee submitted that the Tribunal in ITA No.6154/Mum/2011 in assessee's appeal for Assessment Year 2003-04 had held CUP as most appropriate method, however, the said decision of the Tribunal would not be applicable to the facts of the present case as in the said assessment year, the Tribunal was concerned with the issue of whether cost plus method or CUP, which is the most appropriate method. In the given facts, the Tribunal held that for determining ALP of APIs, cost + method cannot be applied and upheld CUP as the most appropriate method. The Tribunal after having held the CUP as the most appropriate method remanded the matter back to the TPO for giving the information to the assessee to make submissions with respect to comparability of comparable product and FAR of the

comparable transactions. TNMM was never under consideration as the most appropriate method before the Tribunal

9. Per contra, Dr. Yogesh Kamat representing the Department vehemently supported the order of TPO and the directions of the DRP. The ld. Departmental Representative submits that the assessee has changed its stand in the proceedings before the TPO to re-characterize its transactions as Licensed Manufacturer to VAD without there being any cogent reason. He pointed that the assessee has tried to re-characterize its role as VAD in order to avoid application of CUP as the most appropriate method. The TPO in the order has pointed that conversion of APIs into Finished Drug Formulations(FDF) is not a simple value addition but is highly technical process. The running cost of conversion may be low, the basic profile and activity of the assessee is that of manufacturer. In value addition, features or services to an existing product are added and then resold. The assessee in the present case is not doing any value addition but is manufacturing FDF using APIs procured from AEs. The assessee is a Licensed Manufacturer, who is getting FDF manufactured from third parties using their manufacturing facility for which Toll Agreement has been entered. Further excise duty paid during manufacturing of the FDF indicates that the assessee is not VAD. The Ld. Departmental Representative pointed that the intent of the assessee to re-characterize its role as VAD is to wriggle out of transfer pricing adjustment. It is an after though. If , the assessee is held to be VAD the price of the APIs would then be determined by using Market Back approach. The assessee by claiming itself to be distributor wants that it resells the products purchased from the AEs, meaning thereby that the AE is the manufacturer and the assessee is simply a distributor of the FDFs. Whereas, the assessee in the

present case is not merely a distributor but is also engaged in manufacturing activities of conversion of APIs into FDF.

10. The Ld. Departmental Representative further submits that adjustment while applying CUP is an accepted norm. To support this argument he placed reliance on the decision in the case of Serdia Pharmaceuticals (India) Ltd. vs. CIT, 147 ITD 156(Mum) and Merck Ltd. vs. DCIT, 148 ITD 513. As regards argument of the ld.Counsel for the assessee in respect of generic vs. patent APIs, the Ld. Departmental Representative submits that quality and performance of both the APIs would meet the minimum standards as specified under the Drugs and Cosmetics Act, 1940. Once the API qualifies minimum standards there is no difference between generic and patented API. He further submitted that patents do not last for ever. Once patent on an API expires or is not valid in particular geographical location, any pharmaceutical company can manufacture and sell API. The API then becomes generic in nature. However, the company manufacturing such API has to maintain same quality and performance standards as maintained by the brand.

10.1 On selection of comparable from TIPS data base, he submitted that there is no bar in selecting comparable from TIPS. To support his contentions he placed reliance on the decision in the case of Cargill Foods (India) Ltd. vs. DCIT, 57 taxmann.com 330 (Pune). He further submitted that the view taken in the aforesaid decision by the Tribunal has been upheld by Hon'ble Delhi High Court in the case of CIT vs. Cargill Foods (India) Ltd. in ITA 157/2016 decided on 19/02/2016. With regard to objection of assessee that TIPS data base does not have the names of the parties to the transaction, ld. Departmental Representative pointed that the TPO has used TIPS data base to determine ALP in respect of import of API- Mometasone and Dexchlorpheniramine

Maleate. One of the parties in TIPS data base for import of Mometasone is Sun Pharmaceuticals Ltd. For comparison of Netilmicine Sulphate, the TPO has collected information from Cipla Ltd. Both the aforesaid companies are leading Pharma Companies. As regards assessee's objection on adjustment if any required, he submitted that the issue can be restored to the Assessing Officer to make necessary adjustments.

11. On application of CUP as most appropriate method the Ld. Departmental Representative submitted that in Assessment Year 2003-04 in assessee's own case the Tribunal held CUP as the most appropriate method to benchmark the transactions relating to import of APIs. The Tribunal restored the matter to the file of Assessing Officer to re-examine, if any, adjustment is required to be made for difference in terms of contract, quantity sold or purchased, nature of market (retail or wholesale), credit period allowed, delivery terms, foreign currency risk, etc. which might affect the price in the open market. He further place reliance on the decision in the case of Serdia Pharmaceuticals vs. ACIT, 147 ITD 156 to contend that the Tribunal applied CUP over TNMM to benchmark international transactions relating to import of APIs.

12. The Ld. Departmental Representative pointed that the high price charged by the AE on APIs is on account of AMP expenses and not the quality. He 2further submits that cheaper in rate does not mean lower in quality. He reiterated the findings of TPO to support CUP as the most appropriate method.

13. Rebutting the submissions made by Ld. Departmental Representative, the ld.Counsel for the assessee submits that TPO while applying CUP as the most appropriate method to benchmark the transaction has failed to consider the fact that APIs purchased by the assessee not only qualify parameters fixed

by the Indian Drug Authority but has qualified higher parameters fixed by the European countries, therefore, the APIs purchased by the assessee cannot be treated as comparable to those purchased by the independent third party. The ld.Counsel for the assessee reiterated that merely because both the products fulfill minimum standards, the products cannot be comparable when one product is of higher standard. With regard to patent drug being similar to generic drug he submitted that the same can be established or considered if the sample of the product from third party is available to compare with sample of APIs purchased by the assessee. In the present case no such comparison was carried out by the TPO.

13.1 With regard to Department's reliance on the decision in the case of Serdia Pharmaceuticals (supra), the ld.Counsel for the assessee submitted that the Tribunal in the case of Serdia Pharmaceuticals (India) Ltd. (supra) had placed reliance on the decision in the case of Glaxo Smith Kline 2008 TCC 324 by Tax Court of Canada. The decision of Tax Court of Canada has been reversed by Federal Court of Canada and the decision of Federal Court has been approved by the Supreme Court of Canada. Hence, no reliance can be placed on the decision of Tribunal. He further pointed that the decision in the case of Serdia Pharmaceuticals (India) Ltd. (supra) has been distinguished by the Tribunal in the case of Gulbrandsen Chemicals Vs. DCIT, ITA Nos.760&874(Ahd) of 2012 and DCIT Vs. Dishman Pharmaceuticals & Chemicals Ltd., ITA Nos.1388&1511 (Ahd) of 2016.

13.2 Without prejudice to the primary submissions the ld.Counsel for the assessee submitted that if, CUP is held as the most appropriate method to benchmark the transaction then the matter may be remitted back to the TPO to determine comparability of the products.

14. We have heard the submissions made by rivals sides, examined the orders of authorities below and have considered the documents & judgements on which reliance has been placed by the respective sides. The first contention of the assessee is that the assessee be treated as VAD instead of "Licensed Manufacturer" as has been classified by the assessee in TP study report. The assessee for the first time in submissions before the TPO seeks to reclassify it self as VAD. The assessee purchased following APIs from its overseas AEs:

(i) Netilmicin Sulphate

(ii) Dexchlorpheniramine Maleate

(iii) Mometasone

After processing of the same converts it into FDF in the manufacturing unit of Gland Pharma for sale in Indian market. As per assessee's own assertions, procurement of APIs and maintain quality control during Toll manufacturing is the responsibility of the assessee. Thus, the assessee is associated with the manufacturing process right from the beginning i.e. from procurement of APIs till manufacturing of FDF. The assessee uses manufacturing facility i.e. machines and manpower of the Toll manufacturer (i.e. Gland Pharma) to process APIs into FDF as the assessee does not have its own manufacturing unit. As is emanating from the impugned orders, the assessee has entered into an agreement with Gland Pharma for Toll manufacturing, APIs procurement by the assessee from AEs as well as non-AEs. The assessee in proceedings before the TPO has only sought to re-characterize its status as 'Licensed Manufacturer' to VAD qua the APIs procured from AEs. The assessee is not seeking re-characterization in respect of second segment i.e. procurement of APIs from non-AEs and manufacturing of FDFs through Toll manufacturer, though the manner of operation in both the segments is same, except for source of procurement of APIs. Taking into consideration the facts, we are

unable to accept the plea of assessee to re-characterize assessee 'Value Added Distributor'. We find no infirmity in the findings of TPO/DRP on the issue, hence, the first plea of assessee is rejected.

15. The next objection of the assessee is that since TPO has selected comparables from TIPS data base, where information regarding comparables is not completely available i.e. deficit with respect to quality, etc. the comparable so selected would not be ideal for applying CUP method. The assessee in support of its submissions has place reliance on the decision in the case of Tilda Riceland Pvt. Ltd.(supra). We find that the Tribunal in Tilda Riceland Pvt. Ltd.(supra), wherein the assessee had selected the comparable from the TIPS data base and the TPO had rejected the comparable on the ground that said comparable is unreliable, rejected objections of the TPO. The Tribunal held that information available in TIPS data base is available in the public domain and is reliable. The observations of the Tribunal in the case of Tilda Riceland Pvt. Ltd.(supra) on the issue are as under:

> *"11. We have noted that the information inputs given by the Tips Software, on the facts of this case, are inputs with regard to the information publicly available with the customs department at the different ports. These inputs are not the independent 'quotes', as referred to by the TPO, but only compilation of the data available in public domain.* ***In our considered view, the Transfer Pricing Officer was clearly in error in rejecting these inputs on the ground that such information is not covered by Rule 10D(3) for the simple reason that Rule 10D(3) is only illustrative in nature and it merely describes the information,*** *required to be maintained by the assessee under section 92D, "shall be supported by authentic documents, which .may include the following (i.e. documents specified therein)". The logic employed by the Transfer Pricing Officer is that since databases compiled by private entities is not included in rule 10 D(3), such' databases cannot be relied upon by the assessee. This logic is clearly fallacious inasmuch as an item not being included in illustrative list of required documents does not take outside the ambit of 'acceptable document' for the required purposes. In any event, all that Tips Software does is to collect the data, compile the same in easy to refer format and make it available to he end-user of such data online (www.tipsexim.com) or on electronic media, but* ***this data, nonetheless, is Public data maintained by the customs department at various ports. It was also open to the Transfer Pricing Officer to, if he had any doubts, call for further information from this database supplier and examine authenticity of the data so furnished.*** *Yet,*

instead of doing so, he summarily rejected the data as unreliable on a technical ground which, as we have seen above, is not tenable in law."

Hence, the aforesaid decision in fact supports the case of Revenue and is contrary to the arguments raised by the assessee. The assessee has also placed reliance on the decision in the case of Billion Wealth Minerals Pvt. Ltd.(supra). We find that the Tribunal in the said case has distinguished the decision in Tilda Raceland Pvt. Ltd.(supra), as the facts in the case of Billion Wealth Minerals Pvt. Ltd.(supra) were at peculiar and at variance. Hence, the findings of the Tribunal in the said case were specific to the facts of that particular case. The Tribunal again in the case of Dow Chemical International (P) Ltd. vs. ITO, 141 taxmann.com 68 (Mumbai) held that TIPS data can be used to determine ALP under CUP method. Thus, we are of the considered view that the objection raised by the assessee with regard to use of TIPS data base for selection of comparables is unfounded. However, while using TIPS data base reasonable adjustment qua quality, etc. can be allowed.

16. The Tribunal in the case of Merck Ltd.vs. DCIT(supra) has also considered the issue regarding quality of products affecting comparability of the transaction. The Co-ordinate Bench held that since no independent evidence were produced before the Lower Authorities to show quality of assessee's product during the course of assessment proceedings and additional evidence being filed before the Tribunal in the form of quality certificate admitted the additional evidence and restored the issue back to the file of CIT(A) for fresh order, after examining the additional evidence. In the instant case, the assessee has vehemently argued that the APIs procured by the assessee are higher in price because of superior quality. Neither before the TPO nor before the DRP any comparative analysis of the quality of the APIs imported by the assessee and the comparable selected by the TPO was available. Hence,

we are of the considered view that reasonable adjustment with regard to quality of the comparables can be allowed to the assessee.

17. The next grievance of the assessee in respect of TP adjustment under Licensed manufacturing segment is that the assessee has applied TNMM as the most appropriate method to benchmark its transaction of import of APIs from the AEs. The TPO rejected the same and applied CUP as the most appropriate method to determine the ALP of APIs from the AEs. The primary objection of the assessee in application of CUP is selection of comparable by the TPO from TIPS data base. The contention of the assessee is that TIPS data base does not have relevant information for applying CUP method. CUP is direct method to bench mark international transaction. The essential conditions for adopting CUP as most appropriate method are:-

(i) Availability of comparable uncontrolled transaction where none of the differences between such uncontrolled comparable and the controlled transactions under testing affect the price in the open market.

(ii) Reasonable accurate adjustment to eliminate material differences, if any.

18. We find that in Assessment Year 2003-04 the Tribunal in ITA No.6154/Mum/2011 has considered the issue of most appropriate method applicable to the similar transaction, the Co-ordinate Bench after examining the issue threadbare came to the conclusion that CUP is the most appropriate method for benchmarking the transaction for purchase of Netilmicine by the assessee vis-à-vis the APIs procured by Cipla Ltd and Mometasone Furoate by the appellant vis-à-vis Ranbaxy Laboratories Ltd. We find that the same very

APIs are subject matter of TP adjustment in the impugned assessment year. The assessee had tried to distinguish the aforesaid decision on the ground that in Assessment Year 2003-04 assessee had benchmarked the transaction by applying cost plus method. The Tribunal was considering CUP vis-à-vis cost plus method as the most appropriate method. TNMM was not under consideration before the Tribunal. In the instant Assessment Year the assessee has applied TNMM as the most appropriate method. The provisions of section 92C of the Act requires to compute ALP by following the most appropriate method. Once the Tribunal holds that CUP is the most appropriate method to benchmark a particular transaction without there being any change in the facts and nature of transaction, now it cannot be argued that CUP is not the most appropriate method. The assessee has not brought before us any material to show difference in the nature of transaction or variation in the terms and conditions for import of APIs from the AEs in the impugned assessment year. For the sake of completeness the relevant extract of the order by the Tribunal in ITA No.6154/Mum/2011 (supra) is reproduced herein below:

> *"7.5 The CUP method compares the price charged for goods, property or services transferred between related parties (controlled transaction) to the price charged for similar goods, property or services transferred between independent third parties (comparable controlled transaction) in comparable circumstances and conditions.*
>
> *We have narrated here-in-before the case laws relied on by the Ld. counsels and Ld. DR. We find that similar issue arose before the Tribunal in the case of Serdia Pharmaceuticals (India) (P.) Ltd. (supra) and Merck Ltd. (supra).*
>
> *Serdia is engaged in secondary manufacturing process in the sense it does import the active pharmaceutical ingredients, puts them in a delivery mechanism by combining them with excipients, and thus produce the FDF, i.e. finished dosage form, for consumption by the end user. The Tribunal dismissed the appeal of the assessee and confirmed the validity of CUP method followed by TPO for benchmarking the APIs imported by the assessee. In the above case, the Tribunal observed as under:*
>
> > *"The TPO noted that while Indapamide was imported by assessee's competitor from Italy at the price of Rs 40,375 per kg , the assessee had imported by the same, from its AE, at the price of Rs 1,89,456 per kg. The TPO*

further noted that while the assessee had imported Trimetazidine from its Servier Egypt at the price of Rs 52,546 per kg, the same drug was sold by other vendors at much lower rates of Rs 8,150 per kg (Nivedita Chemicals Pvt Ltd), Rs 8,625 per kg (Sharon Pharmachem Limited), Rs 10,558 per kg (Orion) and Rs 11,000 per kg (Trichem).

As visualized from the above, the rates of the drugs imported by Serdia(India) from its AEs were 5-6 times more than that purchased by the third parties.

In Merck Ltd. (supra), the assessee imported API from its AE for manufacture of medicine. The method adopted by the TPO is CUP method. DRP directed to make appropriate adjustment for quality difference between imported goods and comparable goods. On facts, product imported by assessee was superior to locally manufactured API. The TPO had himself allowed a quality adjustment @ 10% in subsequent year. The Tribunal confirmed CUP method and held that it was appropriate to adopt quality adjustment @ 10% in the that assessment year as well.

Facts being nearly identical, respectfully following the orders of the Co-ordinate Bench in Serdia Pharmaceuticals (India) (P.) Ltd. (supra) and Merck Ltd. (supra), we hold that CUP is the most appropriate method in the instant case.

However, adjustments under CUP method need to be examined by the AO/TPO for the reason that under the CUP method adjustments can be made for differences such as differences in the terms of contract, quantity sold or purchased, nature of market (retail or wholesale), credit period allowed, delivery terms, foreign currency risks etc. which might affect the price in the open market.

7.6 Accordingly, we hold that the TPO/AO has rightly adopted the CUP as the most appropriate method in the instant case with regard to Netilmicin by the appellant vis-à-vis Cipla Ltd and Mometasone Furoate by the appellant vis-à-vis Ranbaxy Laboratories Ltd. However, as observed above by us adjustments under the CUP method need to be reexamined by the AO. Therefore, we restore the matter to the file of the AO to re-examine that under the CUP method adjustments can be made for differences such as differences in the terms of contract, quantity sold or purchased, nature of market (retail or wholesale), credit period allowed, delivery terms, foreign currency risks etc. which might affect the price in the open market. We direct the appellant to file the relevant documents/evidence before the AO. Needless to say the AO would give the relevant information and reasonable opportunity of being heard to the appellant before finalizing the order.

We also want to make it clear that all the cases relied on by both the sides have been duly taken into consideration while deciding the matter. The omission of reference to some of such cases in the order is either due to their irrelevance or to ease the order from the burden of the repetitive ratio decidendi laid down in such decisions.

Thus the 1st ground of appeal is partly allowed for statistical purposes"

The Co-ordinate Bench while adjudicating the issue has taken into consideration the decisions rendered in the case of Serdia Pharmaceuticals (P) Ltd. (supra) as well as in the case of Merck Ltd.(supra). We see no reason to take a different view in accepting CUP as the most appropriate method for benchmarking the transaction in the impugned assessment year. Following the decision of Co-ordinate Bench in assessee's own case in Assessment Year 2003-04, ground No.1 of appeal is partly allowed in similar terms.

19. In the result, ground No.1 of the appeal is partly allowed.

DISTRIBUTION – IMPORT OF FORMULATIONS (FDF):

20. The ld.Counsel for the assessee submits that the second segment in which the TPO has made adjustment relates to the distribution of FDF.. He submitted that in transfer pricing study inadvertently the assessee has combined two segments i.e. Contract Manufacturing and Distribution of formulations imported from AE. The assessee applied TNMM as the most appropriate method to determine the ALP of the international transactions for purchase of formulations from AE. The assessee compared itself with other distributors to bench mark the transaction. In proceedings before the TPO, the assessee submitted 'Contract manufacturing' and 'Distribution' are two different segments. The functional profile of these segments are completely at variance. Merely for the reason that the assessee in Transfer Pricing Study Report erred in treating distribution segment and contract manufacturing segment as single activity it would not mean the error cannot be rectified, subsequently. Explaining the activities in the two segments he submitted that, in distribution segment the AE purchases finished formulations from its AE,

which are manufactured by the AE under its own brand. The said formulations are purchased by the assessee for sale in India.

Whereas, in Contract manufacturing segment, the assessee entered into a Contract Manufacturing Agreement with Zyg Pharma and Encore Healthcare, collectively known as 3PManufactuers for which the assessee has the license to manufacture the formulations using SP trademarks. Under the arrangement APIs are purchased by 3P manufacturers from third party (non-AE) suppliers and converts into FDFs based on the technology specifications and trademark provided by the assessee. The finished formulations are then sold by the 3P manufacturers to the assessee. The assessee is acting as manufacturer and not distributor. The payment is made to 3P manufacturer which is aggregate of cost of raw material, packing material, cost of conversion from API to FDF plus 10% margin on the total cost. The ld. Counsel for the assessee referred to Purchase Agreement dated 21/12/2007 between the assessee and Zyg Pharma Pvt. Ltd. The ld. Counsel for the assessee pointed that as per Agreement Zyg Pharma Pvt. Ltd. would manufacture products for assessee in accordance with regulatory requirements. He further referred to Technical Agreement on contract manufacturing at page 424 to 459 of the paper book. The ld. Counsel for the assessee submitted that similar arrangement has been entered with Encore Health Pvt.Ltd. The agreement is at page 403 to 423 of the paper book.

The ld. Counsel for the assessee to further buttress his arguments distinguishing manufacturing segment and distribution segment pointed that in Distribution, the product liability is of the AE being manufacturer of the FDF. Whereas, in case of manufacturing segment the products are manufactured by the 3P manufacturer at the direction and supervision of assessee.

21. On the other hand the learned Departmental Representative vehemently supporting the order of TPO submitted that assessee in Transfer Pricing study report had itself clubbed the segment of distribution of sale of FDFs procured from AE and formulations manufactured by Zyg Pharma and Encore Pharma. The assessee in proceedings before the TPO for the first time raised an argument for segregating Distribution segment and Manufacturing segment. He further submits that the points of difference as highlighted by the assessee are merely for name sake. On going through FAR it can be seen that in both segments function, assets and risk are almost the same. The only difference assessee between the two sub segments is that the assessee is following Market Back approach in purchase of FDF from AE and to Zyg Pharma it is giving cost plus. However, the assessee could not give any basis of Market Back theory. In both these sub segments the Assessee is purchasing finished goods and selling them in the market through its common network. He further argued that the other difference assessee could point was type of products, therapeutic area and promotion of expenses, the said difference is not of much relevance. As the expenses have been allocated in the ratio of sales. The assessee does not have any document to support how much extra expenditure has been incurred on promotion and marketing of products as it is promoting the brand value of the AE as all intangibles are owned by the AE.

The learned departmental representative further submitted that the TPO after examining the new agreements between the assessee and Zyg/Encore came to the conclusion that except for change in the nomenclature of the parties from ‘distributor’ to ‘buyer’ and from ‘manufacturer’ to ‘seller’ no substantial change in the terms and conditions of the old agreements and the new agreements is visible. One change in the agreements is, that the price

which was to be agreed between the parties has been now ex-factory price plus 110%, which is the premium to be paid as per DPCO norms. There is hardly any substantive difference in FAR analysis because of the new agreement, except that in earlier agreement there was clear mention that the assessee is a 'distributor' which has now been changed to 'Purchaser'.
The learned departmental representative vehemently supporting the impugned order prayed for dismissing ground number 2 of appeal.

22. We have heard the submissions made by rival sides in respect of ground number 2. It is an undisputed fact that. The Assessee in Transfer Pricing Study report has clubbed both the segments i.e. distribution segment and contract manufacturing segment. The assessee is now seeking segregation of both the segments.

We find that under distribution segment, the assessee is importing Formulations from AE for distribution in Indian market. The said formulations are manufactured by the AE under its own Brand Name. The product liability is that of AE as FDFs are manufactured by the AE. Whereas, under license manufacturing segment, the assessee enters into agreement with Zyg Pharma and Encore Pharma for manufacturing of FDFs. The APIs are purchased from third party suppliers and converted into FDFs based on the technology, specifications and trademark provided by the assessee. Under this sub segment the assessee is getting FDFs manufactured using manufacturing facility – machine and manpower of the third parties (Zyg and Encore). The assessee has entered into fresh agreements with Zyg Pharma and Encore. The agreement dated 21/12/2007 with Zyg Pharma effective from 01/1/2008 is at

page 379 of the paper book. After examining the terms and conditions of the agreement, the salient points of agreement are culled out as under:

- Zyg (seller) shall manufacture the product as required by the assessee (buyer) in accordance with manufacturing and quality assurance procedures specifications given by the assessee;
- Zyg assures that the products manufactured conforms to quality standards and specifications of the assessee;
- Zyg to keep secrete and confidential the standards and specifications shared by the assessee;
- Zyg to manufacture products under trademarks/brand specified by the assessee;
- Zyg not to use trademark/brand of the assessee or infringe/impair, right title or interest in the said mark of assessee;
- In case the assessee subsequently finds that the products do not conform to the standard and specifications or statutory requirements pertaining to the manufacturing of the products, Zyg was liable to reimburse the cost of the product paid by the assessee;
- Zyg on delivery of products was required to provide assessee, protocols assay and other manufacturing and quality assurance records;
- Zyg not to sell or deal with products manufactured for assessee, however, Zyg was not precluded to manufacture and sell the products not covered under the agreement;
- Zyg not the agent of assessee;
- The assessee to have minimum annual volume commitment with Zyg. In case of shortfall, the assessee to compensate Zyg.

From analyses of the above terms and conditions of the agreement between the parties, it is evident that under manufacturing segment the role of assessee is much more than that of a distributor. The obligations of the manufacturer i.e. Zyg and the contract manufacturer i.e. the assessee are defined.

It would be relevant to mention here that under Distribution segment the assessee is purchasing FDFs from its AE for sale in India, whereas, in Contract Manufacturing the assessee is transacting with non-AEs.

23. Taking into consideration the facts and terms and conditions of the Agreement we are of considered view that segregation of Contract Manufacturing activity and Distribution is fair and reasonable. Merely for the reason that the assessee committed error in TP study to merge the two distinct segments under one head would not mean that the error cannot be rectified, subsequently. Since, the TPO has not examined the transaction after segregation of the two segments, we deem it appropriate to restore this issue to AO/TPO for fresh examination of Distribution segment after segregation. The ground no. 2 of appeal is thus allowed pro tanto for statistical purpose.

24. In the result, appeal of assessee is partly allowed for statistical purpose.

Order pronounced in the open court on Tuesday the 06th day of February, 2024.

Sd./-	Sd./-
(GAGAN GOYAL)	(VIKAS AWASTHY)
लेखाकार सदस्य/ACCOUNTANT MEMBER	न्यायिक सदस्य/JUDICIAL MEMBER

मुंबई/ Mumbai, दिनांक/Dated: 06/02/2024

Vm, Sr. PS(O/S)

प्रतिलिपि अग्रेषितCopy of the Order forwarded to :

1. अपीलार्थी/The Appellant ,
2. प्रतिवादी/ The Respondent.
3. The PCIT
4. विभागीय प्रतिनिधि, आय.अपी.अधि., मुबंई/DR, ITAT, Mumbai
5. गार्ड फाइल/Guard file.

BY ORDER,

//True Copy//

(Dy./Asstt.Registrar),ITAT, Mumbai

	Details	Date	Initials	Designation
1	Draft dictated on			Sr.PS/PS
2	Draft Placed before author			Sr.PS/PS
3	Draft proposed & placed before the Second Member			JM/AM
4	Draft discussed/approved by Second Member			JM/AM
5.	Approved Draft comes to the Sr.PS/PS			Sr.PS/PS
6.	Kept for pronouncement on			Sr.PS/PS
7.	File sent to the Bench Clerk			Sr.PS/PS
8	Date on which the file goes to the Head clerk			
9	Date of Dispatch of order			