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Amicus Transfer Pricing Alert

Ahmedabad Tribunal prefers TNMM over CUP in Absence of Reliable Comparability Adjustments

July 30, 2025

Background:

Taxpayer was engaged in the business of manufacturing frozen french fries. It acquired potatoes from its Associated Enterprise ('AE'). As per the agreement between taxpayer and its AE, AE had to sell the potatoes at a cost-plus markup to taxpayer and only if there was surplus stock, AE could sell the potatoes to third parties.

Taxpayer applied CUP method for benchmarking the related party transaction in its Transfer Pricing Documentation. However, in the course of audit, taxpayer changed the method from CUP to TNMM citing economic and comparability arguments. The Transfer Pricing Officer ('TPO') still applied CUP method using internal comparables and made upward adjustment, without taking into account volume differences. Taxpayer appealed to Tax Tribunal to consider TNMM as the appropriate TP method.

Key Points of Tribunal's Ruling

Change in TP Method – Whether Permissible?:

- It is a settled position that the most appropriate method has to be selected and applied;
- If there is a mistake in application of the correct TP method, the same can be corrected to determine Arm's Length Price ('ALP');
- The methods prescribed and used are only means of achieving the object of ALP determination;
- Thus, selection of method is not binding if better suited method is found later on, provided the change in method is backed with economic justification.

Functional and Economic Differences: The Tribunal identified following differences in sale to third party and taxpayer, leading to difficulty in accurate comparability adjustments:

- **Volume of Transaction:** Taxpayer's sale to unrelated third party averaged to merely 1% of the volume sold to AE;
- **Product Differentiation:** Quality-wise data maintained showed that distinct potato grades were maintained & sold to third parties and AE;
- **Contractual Framework:** AE sold on cost-plus basis to Taxpayer, whereas third-party sales were discretionary and at market driven rates;
- **Functional Profile:** AE utilized potatoes for manufacturing French fries while unrelated third parties used it for varied commercial use.
- **Different Business Model:** The sale to Taxpayer followed B2B model while sale to third parties followed B2C model.

Relying on Indian Income Tax Rules[1], OECD Transfer Pricing Guidelines (2022)[2] and UN Practical Manual on Transfer Pricing for Developing Countries (2017)[3], he Tribunal ruled that reasonably accurate adjustments with respect to differences in volume of sales, product differentiation, etc. are essential under CUP method as it directly compares the price charged. Since TPO did not make accurate adjustments taking these factors into account (due to lack of data in public domain), CUP could not be considered as an appropriate method.

Further, taxpayer had provided benchmarking under TNMM which was not disputed by Revenue. So, TNMM was preferred to CUP in the present case.

Conclusion:

CUP method should not be applied mechanically when accurate comparability adjustments are not possible. Further, change in TP method is permissible if a better method is found later in the course of audit. There is no estoppel under Transfer Pricing Regulations and even if Taxpayer has chosen one method, another can be applied if same is justified under facts and circumstances of the case.

However, as a word of caution taxpayers are advised to maintain robust documentation and choose correct Transfer Pricing methods upfront and change methods only as last resort. A well-documented and consistent approach in Transfer Pricing is imperative for certainty and to avoid prolonged litigation with Revenue authorities.

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[1] Indian Income Tax Rules, 1962, Rule 10B(1)
[2] Para 2.19 & 2.20.
[3] Para 5.3.2.34.

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Amicus is legal and tax consulting firm with focus on corporate finance, re- structuring, private equity, international taxation, transfer pricing and goods and services tax. The Firm's tax team also represents clients in assessments and litigation including Tax Tribunal and Higher Courts.

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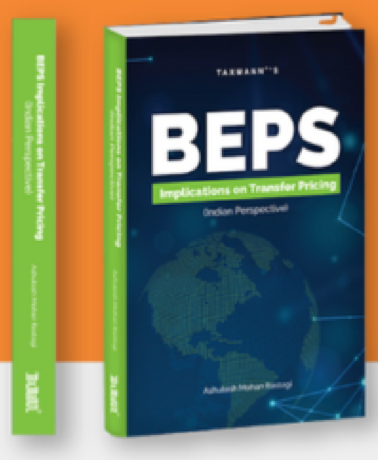

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