

**IN THE INCOME TAX APPELLATE TRIBUNAL,
BANGALORE BENCH 'B'**

**BEFORE SHRI N BARATHVAJA SANKAR, VICE RESIDENT
AND
SMT. P MADHAVI DEVI, JUDICIAL MEMBER**

ITA No.1368/Bang/2010
(Asst. Year - 2006-07)

M/s Google India Pvt. Ltd., . Appellant

Vs.

The Dy. Commissioner of Income-tax,
Circle-11(3),
Bangalore. . Respondent

Appellant by : Shri Arvind Sonde, CA

Respondent by : Shri Farahat Hussain Qureshi

Date of Hearing : 18-09-2012

Date of Pronouncement : 19-10-2012

ORDER

SMT. P MADHAVI DEVI, JUDICIAL MEMBER

This appeal is filed by the assessee. The relevant assessment year is 2006-07. The appeal is directed against the assessment order passed in consonance with the order of the Dispute Resolution Panel at Bangalore dated 20.09.2010. The appeal arises out of the

assessment completed u/s 144C(5) r.w.s 144C(8) of the Income-tax Act, 1961.

2. The assessee is aggrieved by the assessment order passed in consonance with the order of the DRP making transfer pricing adjustment u/s 92CA of the Income-tax Act.

3. The brief facts of the case are that the assessee company is engaged in the business of software development services and information technology enabled services (ITES). As the assessee had entered into an international transactions with its associated enterprise, a reference u/s 92CA of the Act was made to the TPO for determining the arms length price of the said international transaction. The TPO vide order dated 28.10.2009 u/s 92CA of the Act, proposed adjustments towards software development services and IT enabled services. The AO taking due note of the adjustments proposed by the TPO, forwarded a draft assessment order to the assessee. The assessee raised objections to the draft assessment order before the DRP and after considering the same, the DRP confirmed the proposal of the assessing authority and assessment order was accordingly passed.

3. Aggrieved, the assessee is in appeal before us. The DRP confirmed the order of the assessing authority as far as the adjustment to the ALP towards IT enabled services is concerned but recommended that no adjustments are required to be done in respect of the international transactions relating to software development services segment.

4. Aggrieved by the adjustment made under the ITES segment, the assessee is in appeal before us. Though the assessee has raised as many as 19 grounds of appeal, the main grievance is against the transfer pricing adjustment and the comparables adopted by the TPO.

5. At the outset, the learned counsel for the assessee has drawn our attention to the order of the DRP dated 20.9.2010 relating to adjustment to be given for the under utilization of the capacity. He submitted that the DRP has clearly noted that the comparables have an average of 80% utilization levels as compared to the assessee which is at 58%. However, while computing the adjustment, at page 7 para 7, the DRP has taken the capacity under utilization of the comparable companies at 65%, which has resulted in the higher adjustment.

6. The learned DR also agreed that an error has been committed while making the adjustment under utilization of capacity of the comparables. As this is only a mistake apparent from record, we deem it fit and proper to direct the assessing authority to rectify the mistake by computing the correct adjustment in under utilizing capacity by taking the capacity utilization of the comparable companies at 80% instead of 65% mentioned in the order of the DRP.

7. As regards the other grounds of appeal, the assessee has stated that the assessee has charged its associated enterprises at cost + method, but for computing the arm's length price, the TNMM has been adopted. He submitted that the transfer pricing officer has rejected some of the comparables adopted by the assessee and after conducting his own search analysis has adopted certain other companies as comparables. He submitted that the assessee has raised objections to the adoption of the said comparables but however, the TPO, after brushing aside the assessee's objection, has proceeded to make the adjustment to the ALP. He submitted that some of companies which cannot be adopted as comparables for the TP study are as under:

(1) Asit C Mehta Financial Services Ltd.

(2) Goldstone Infratech Ltd.

8. These two companies have abnormally high profit margin. He submitted that Asit C Mehta has shown phenomenal increase in profits by 1,195% and the revenues for the financial year 2005 has increased by 363% as compared to financial year 2005. He submitted that in the case of Goldstone Infratech Ltd., there are abnormal fluctuations as compared to financial year 2005-06. In the year 2005, the revenue was 31%, while in the year 2006 decline in the Revenue was 16%, while the profit earned during 2005 was -69% as compared to the profit growth of 38% in 2006. Thus, according to him, these companies have to be excluded from the list of comparables as they are abnormally higher margin companies. In support of its contention that the abnormally higher margin companies are to be excluded from the list of comparables for the purpose of TP study, the learned counsel for the assessee has placed reliance upon the following decisions :

- 1) Abode Systems Pvt. Ltd., in ITA No.5043/Del/2010

- 2) SAP Labs India Pvt. Ltd., in ITA No.398, 418/Bang/2008
- 3) Teva India Pvt. Ltd., in ITA No.5707/MUM/2010
- 4) Saunary Jewels Pvt. Ltd., in ITA No.5758/Mum/2007
- 5) Sapient Corporation Pvt. Ltd., in ITA No.5263/Del/2010
- 6) M/s Genisys Integrating Systems (I) Pvt. Ltd., in ITA No.5263/Del/2010

9. The next comparable, the assessee has objected to is (3) Vishal Information Technology Ltd. The objection of the assessee is that the employee cost of this company is less than 25%. The learned counsel for the assessee submitted that the IT enabled services are basically dependent upon the human resources and, therefore, any company with employee cost less than 25% can not be compared with an IT enabled services company. He submitted that in the case of Maersk Global Services Centre (I) Pvt. Ltd., case of Vishal Information Technology has been considered and was directed to be excluded. He submitted that the TPO has himself held that employee cost filter is very much applicable and through Vishal Information Technologies Ltd. having outsourced some of its services and having employee cost of 25% cannot be considered as a comparable. He has also drawn our

attention to the TPO's order, wherein the employee cost filter was considered for the purpose of software development services but has not been considered for the IT enabled services. He submitted that the TPO has to adopt the same yardstick for the purpose of TP adjustment for both the ITS and TTES company. In support of its contention that the employee cost is important factor/ filter and has to be considered for the purposes of making transfer pricing adjustment, he placed reliance upon the following decisions :

- 1) Avaya India Pvt. Ltd., in ITA No.5150/Del/2010
- 2) Colt Technologies Services Ind. Pvt. Ltd., in ITA No.4370/Del/2010
- 3) Sapient Corporation Services India Pvt. Ltd., in ITA No.5263/Del/2010

10. The next comparable company, the assessee objecting to is (4) Apex Knowledge Solution Pvt. Ltd. According to the learned counsel for the assessee, the assessee company is in the pure business of ITES, while Apex Knowledge Solution Pvt. Ltd., is functionally different, as it is engaged in providing value added E-publishing, GIS and knowledge based services. He submitted that this company operates in four business segments i.e E-publishing solutions,

business solutions, engineering solutions and customer care solutions and segmental data of these segments is not available. Therefore, according to the learned counsel for the assessee, this company has to be excluded from the list of comparables. In respect of this contention, he placed reliance upon the following decisions :

- 1) Quark Systems Pvt. Ltd., in [2010-TIOL-31-ITAT-CHD-SB]
- 2) CRM Services India (P). Ltd., in ITA No.4068 of 2009 and 4796 of 2010)
- 3) Aztec Software, (SB 107 ITD 141)
- 4) Moser Baer India Ltd., 316 ITR 1
- 5) Mentor Graphics Pvt. Ltd., in ITA No.1969/D/2006
- 6) Egain Communication Pvt. Ltd., in ITA No.1685/PN/2007

12. The Fifth comparable company which the assessee objects to is (5) Datamatics Financial Services Ltd. The objection of the assessee is that the company does not qualify the revenue filter considered by the learned TPO himself, according to which the company not deriving 75% or more of its revenue from ITES activity is to be rejected from comparables. As regards last comparable which the assessee seeks to be excluded is (6) Allsec Technologies Ltd. According to the learned

counsel for the assessee, Allec Technologies Ltd., has been experiencing extra ordinary events. During the financial year 2005-06, Allsec had gone for a IPO during the relevant previous year and also the company had entered into a share purchase agreement with shareholder of B2K Corporation Pvt. Ltd., which is engaged in the business of inbound and outbound voice, email chat services and information technology services. Therefore, due to these extra ordinary events, the profits of the said company are not ascertainable and, therefore, the company has to be excluded.

13. The leaned DR on the other hand supported the orders of the authorities below and submitted that the assessee had been given ample opportunity of raising the objections before the TPO and the DRP and the authorities have considered the objections of the assessee before passing the order. Thus, according to him, the assessment order is to be confirmed.

14. Having heard both the parties and having considered the rival contentions, we find that the only dispute before us is with regard to the comparables adopted by the TPO. The assessee vide its TP study had arrived at four comparable companies, out of which three have

been rejected by the TPO as not comparable. Thereafter, the TPO after conducting his own search from the available data base provided arrived at certain other comparables and after calling for assessee's objections has adopted the final list of comparables. The assessee has accepted some of the comparables adopted by the TPO while it raised objections to the others. The assessee's objection regarding two companies (1) Asit C Mehta Financial Services Ltd., and (2) Goldstone Infratech Ltd., is on the issue of abnormally higher margin. In our view, this objection is justified on the basis of various decisions of the Tribunal wherein it has been held that super profit making companies have to be excluded from the list of comparable before making transfer pricing adjustment. In the case before us, only these two companies showing profit of more than 100% as compared to the other comparables taken by the TPO. In view of the decisions of the Co-ordinate Benches of the Tribunal, we direct the AO to exclude these two companies from the list of comparables for the purpose of making the transfer pricing adjustment.

15. As regards the issue of (8) Vishal Information Technologies Ltd., we find that, it is adopted by the TPO. The DRP held that Vishal Information Technologies has outsourced its call centre work

and, therefore, the employee cost is less than 25% as is the common practice among other ITES services. The TPO as well as the DRP have recorded that in the ITES sector, employees filter of less than 25% alone is not applicable for the reason that in addition to the ample costs, the commission costs are also important. When company has outsourced its ITES services, it cannot be said that its business results would be comparable to any other ITES service provider rendering the services entirely on its own. In such circumstances, the net margins of the two comparables cannot be on the same basis. The decisions relied upon by the learned counsel for the assessee also held that the employee cost filter is important filter to be adopted for the purpose of computing ALP. In the case of Maersk Global Services Centre (India) Pvt. Ltd., in ITA No.3774/M/2011, the Tribunal at Mumbai has held that Vishal Information Technologies Ltd. has to be excluded from the list of comparables of ITES company as it has outsourced its services. In view of the same, we direct the AO to exclude this company also from the list of comparables.

16. As far as (4) Apex Knowledge Solutions Pvt. Ltd., is concerned, we find that the assessee had taken objections before the

TPO that it is functionally different, as it provides services such as E-publishing knowledge based services etc. But TPO has rejected the objection on the ground the assessee has not considered the verticals or functional lines during the search process conducted by it and, therefore, it is not proper to make any objection on this basis now. We are not able to agree with the finding of the TPO as confirmed by the DRP on this issue. Merely because, the assessee itself has not considered the said filter while making its TP study; it cannot be said that it cannot raise such an objection before the TPO. It is the TPO who has adopted this company as comparable. On such adoption, the assessee has every right to raise the objections as regards the functional differences between the assessee and comparable. It is the bounden duty of the TPO to consider the said objections in accordance with law. As brought out by the assessee, the assessee is in the IT enabled services, whereas the said company Apex Knowledge Salutation Pvt. Ltd., is in the business of E-publishing which cannot be said to be in the same line of business. The functional differences are likely to affect the profit marking capacity of both the companies. In view of the same, we are of the opinion that this company is also to be excluded from the list of comparables. As regards the other two comparables i.e (5) Datamatics Financial

Services Ltd. and (6) Allsec Technologies Ltd., we find that merely because there were extraordinary events during the financial year, without demonstrating as to how these extraordinary events have influenced the profit margin of the company, they cannot be excluded from the list of comparables, but the adjustments for such extraordinary events have to be made to the profits of the companies to bring them on par with the assessee before comparing them with the assessee. Therefore, we remand this issue to the file of the AO to consider the adjustments to be made to these two comparables before arriving at the ALP. Needless to mention that the assessee shall be given a fair opportunity of hearing.

17. In the result, the assessee's appeal is allowed for statistical purposes.

Order pronounced in the open court on **19th Oct, 2012.**

(N BARAT HVAJA SANKAR)
VICE PRESIDENT

(P MADHAVI DEVI)
JUDICIAL MEMBER

Vms.

Bangalore

Dated : 19/10/2012

Copy to :

1. The Assessee
2. The Revenue
3. The CIT concerned.
4. The CIT(A) concerned.
5. DR
6. GF

By order

Sr. Private Secretary, ITAT, Bangalore.