IN THE INCOME TAX APPELLATE TRIBUNAL
"**K** " Bench, Mumbai

BEFORE SHRI RAJENDRA SINGH, ACCOUNTANT MEMBER AND SHRI VIVEK VARMA, JUDICIAL MEMBER

ITA No.7140 /Mum/2012
(Assessment year: 2007-08)

Vodafone India Services P. Ltd. (Formerly 3Global Services P. Ltd.) Vodafone House, GR Floor Corporate Road Off S.G. Highway Prahlad Nagar, Ahmadabad Gujarat, Pin- 380051 Pan AAACZ1849D	Vs.	DCIT 3(3) Pratyakshkar Bhavan, Bandra Kurla Complex, Mumbai Pin - 400051
Appellant		**Respondent**

(ITA NO. 7097/Mum/2012).
Assessment year:- 2007-08

DCIT 3(3) Pratyakshkar Bhavan, Bandra Kurla Complex, Mumbai Pin – 400051	Vodafone India Service P. Ltd. (Formerly 3Global Services P. Ltd.) Vodafone House, GR Floor Corporate Road Off S.G. Highway Prahlad Nagar, Ahmadabad Gujarat, Pin- 380051 Pan AAACZ1849D
Appellant	**Respondent**

Assessee by: Shri Yogesh Thar
Department by:Shri Ajit Kumar Jain

Date of Hearing: 8/4/2013
Date of Pronouncement: 26 /4/2013

O R D E R

Per Rajendra Singh A.M.

These cross appeals are directed against the order dated 11.9.2012 of CIT (A) for the assessment year 2007-08. The disputes raised by the parties in these appeals relate to transfer pricing adjustment made by the Assessing Officer (AO) on account of international transactions entered into by the assessee with associated enterprise, (AE).

2. The facts in brief are that the assessee who was engaged in the business of providing voice based call centre services, had provided such services to its holding company i.e. Hutchison Call Centre Holding Limited for which the assessee had received payment of Rs. 2925441490 during the year. Since the assessee had entered into international transaction with an associate enterprise, the Assessing Officer called for the necessary information/details for application of transfer pricing provisions. The assessee conducted its transfer pricing study in which TNMM method was used for bench marking the international transaction. The assessee in the TP study identified 39 comparables out of which 9 companies were selected as per details given below:-

Sl No.	Name of the company	Operating Cost	PBIT	%of PBIT
1	Allsec Technologies Limited	88.60	24.79	27.98%
2	Ask Me Info Hub. Ltd.	2.98	0.01	0.34%
3	Godrej Upstream Ltd.	17.97	0.46	2.56%
4	NIIT Smartserve Ltd.	53.85	2.21	4.10%
5	Nipuna Services Ltd.	172.57	0.59	0.34%
6	Optimus Global Services ltd.	33.07	(1.42)	-4.29%
7	Transwork Information Services Ltd.	176.03	21.12	12.00%
8	Sparsh BPO Services Ltd.	81.70	5.76	7.05%
9	HTMT Global Solution Ltd.	253.16	12.32	4.87%
Arithmetic Mean				6.10%

3. The assessee submitted that the price charged by the assessee from the AE was cost plus 7% mark up. It was pointed out that margin on operating cost in case of comparables selected by it was 6.10%. The assessee also submitted that certain costs such as linked cost and equipment cost had been incurred by the AE on behalf of the assessee and therefore in case the adjustments were made in relation to such costs, the margin of the assessee on operating cost would be 15.16%. The TPO however conducted his own search and identified 25 comparables providing Information Technology Enabled Services (ITES) as per details given below:-

S. No.	Name of the Comparable Company	Turnover	NCP%
1	Accentia Technologies Ltd	16.57	38.26
2	Aditya Birla Minacs Worldwide Ltd.	197.06	11.98
3	Allsec Technologies Ltd.	113.28	27.31
4	Apex Knowledge Solutions Pvt. Ltd.	4.92	20.48
5	Appollo Healthstreet Ltd.	47.84	-13.55
6	Asit C. Mehta Financial Services Ltd.	6.09	24.21
7	Bodhtree Consulting Ltd. (Seg).	2.94	29.58
8	Caliber Point Business Solutions Ltd.	39.3	21.26
9	Cosmic Global Ltd.	4.28	12.4
10	Datamatic Financial services ltd. (Seg)	2.92	5.07
11	Eclerx Services Ltd.	86.12	103.72
12	Flextronics Software Systems Ltd. (Seg)	21.41	14.54
13	Genesys International Corporation Ltd.	19.17	13.53
14	HCL Comnet Systems & services Ltd.	260.18	44.99
15	ICRA Techno Analytics ltd. (Seg).	7.23	12.24
16	Informed Technologies India ltd.	4.08	35.56
17	Infosys BPO Ltd.	649.56	66.14
18	IServices India Pvt Ltd.	16.29	50.27
19	Maple Solutions Ltd.	12.21	34.05
20	Mold-Tek Technologies Ltd.	11.4	113.49
21	R. Systems International Ltd.	17.34	20.18
22	Spanco Ltd. (Seg)	35	25.81
23	Triton Corp Ltd.	53.37	34.93
24	Vishal Information Technologies Ltd.	30.6	51.19
25	Wipro Ltd. (Seg)	939.78	29.7
Arithmetic Mean			33.09%

4. In response to the new comparables selected by TPO, the assessee submitted that Allsec Technologies and Transwork Information Ltd., were already selected by assessee in its comparables. The assessee also submitted that Spanco was

comparable to the case of assessee. In respect of the other companies, it was submitted that quite a few of them were in the field of computer software and other companies which were in ITES/BPO segment were doing high end job, and therefore, these companies were not functionally comparable. The assessee referred to the comparative billing rates as per NASSCOM report 2003-04 as per which the billing rates in respect of high end services such as content development and knowledge process outsourcing (KPO),which were very high. In relation to Maple E solution Ltd., it was submitted that business operations of this company were controlled by Triton and, therefore, it was submitted that this company should be excluded on the ground of related party transactions. The assessee also requested for working capital adjustments and submitted that after making such adjustments, the margin in case of the assessee would be 8.86 after including Spanco limited which was comparable to the assessee. It was also submitted that in case the adjustment was made on account of cost incurred by the AE, the margin would be 17.04%. The Assessing Officer, however, did not accept the contentions raised. It was observed by him that transaction of Maple (E) Solution Ltd. with Triniton were only on capital account and, therefore, it will not have any impact on the revenue stream. As regards, Wipro it was pointed out that the assessee itself had selected it as one of the comparables in the last year. TPO also observed that the assessee had not pointed out functional differences with respect to the companies selected by TPO as the assessee had conceded that most of the companies were in the ITES sector. The main objection of the assessee was that these companies were rendering high end activities in which charges per hour was very high. The TPO further observed that in such cases of high end companies, employees cost will also be high and therefore margins would not be impacted much. In relation to the comparables selected by the assessee, TPO observed that M/s Optimus Global Services was incurring persistent losses for the last three years. The TPO therefore excluded this company from the list of comparable cases. TPO thus finally selected thirty one comparables, eight from the list of comparables selected by assessee and twenty three new comparable selected by him (excluding two common comparables) and computed the mean margin of these thirty one comparables at 25.25% as per details given below:-

1	Allsec Technologies Ltd.	27.98%
2	Ask Me Info Hub Ltd.	0.34%
3	Godrej Upstream Ltd.	2.56%
4	NIIT smartserve Ltd.	4.10%
5	Nipuna Services Ltd.	0.34%
6.	Transworks Information Services Ltd.	12.00%
7.	Sparsh BPO Services Ltd.	7.05%
8.	HTMT Global Solution Ltd.	4.87%
9	Accentual Technologies	38.26%
10	Apex Knowledge Solutions Pvt. Ltd.	12.83%
11	Apollo Healthcare Ltd.	-13.55%
12	Asit C. Mehta Financial Services Ltd.	24.21%
13	Caliber Point Business Solutions Ltd	21.26%
14	Cosmic Global Ltd.	12.40%
15	Datamatics Financial Services Ltd. (Seg).	5.07%
16	Exclerx Services Ltd.	90.43%
17	Flextronics Software Systems Ltd. (Seg)	14.54%
18	Genesys International Corporation Ltd.	13.35%
19	HCL Comnet Systems & Services Ltd.	44.99%
20	Informed Technologies India Ltd.	35.56%
21	IServices India Pvt. Ltd.	50.27%
22	Mold Tek Technlogies Ltd.	113.49%
23	R Systems International Ltd. (Seg).	20.18%
24	Spanco Ltd. (Seg.)	25.81%
25	Vishal Information Technologies Ltd.	51.19%
26	Bodhtree Consulting Ltd. (Seg).	29.58%
27	ICRA Techno Analytics Ltd. (Seg)	12.24%
28	Infosys BPO Ltd.	28.78%
29	Maple E Solutions Ltd.	34.05%
30	Triton Corp. Ltd.	34.93%
31	Wipro Ltd. (Seg).	29.70%
	Arithmetic Mean	25.25

5. The TPO accordingly made adjustment on account of transfer pricing at Rs. 502236923 on the basis of mean margin 25.25%. The Assessing Officer, thus, in the assessment order passed made an addition of Rs. 502236923 to the total income.

6. The assessee disputed the decision of the Assessing Officer making adjustment on account of transfer pricing and raised several objections before CIT(A). The first objection was regarding applicability of transfer pricing provision in case of the assessee whose income was exempt u/s 10 A of the Income Tax Act. It was submitted that the assessee had no advantage in transferring profit to low tax jurisdiction as the income of the assessee was exempt. The assessee

placed reliance on the decision of Tribunal of Bangalore bench in case of Phillips Software Centre (P) Ltd. (26 SOT 226), in which it was held that in case the income of the assessee was exempt u/s10 A, the transfer pricing provision would not be applicable. The Assessing Officer, however, did not accept the contentions raised. It was observed by him that in case the assessee had entered into international transactions and the transfer pricing provisions were applicable, then adjustment had to made as per law and it was not necessary to go to intentions behind the regulations and the Assessing Officer was not required to prove that there was any manipulation by the assessee in shifting the profit outside India. CIT (A) also observed that decision of Bangalore Bench of Tribunal in case of Phillips Software Centre (P) Ltd. (Supra) had been stayed by Hon'ble High Court of Karnataka in ITA 49/2008, CIT(A), therefore, rejected the argument advanced by the assessee.

7. The assessee also objected to the exclusion of Optimus Global Services Ltd, the comparable selected by the assessee on account of losses. It was submitted that the said company had been set up in the year 2002 which was around the same time when the assessee company had been set up. It was pointed out that it was natural to make losses in the initial few years and that the company had made profit of Rs. 0.58 Lakh in assessment year 2008-09. The assessee referred to several decisions of Tribunal in support of the propositions that the comparables could not be excluded only on the ground of losses. CIT (A) however, did not accept the arguments advanced. It was observed by him that consistent losses could be only on account of some extraordinary factors and therefore, such losses could not be considered as incurred during normal course of business. CIT(A) also observed that for making comparison only the data for past two years could be considered as per rule and not the data of subsequent year, and therefore, profit made by the Optimus Global Services ltd. in assessment year 2008-09 was not relevant. CIT (A) accordingly upheld the order of Assessing Officer excluding the said comparable.

8. The assessee also raised objection to the four comparables selected by TPO on the ground that these were cases of exceptionally high profit margins as per details given below, reproduced from page 10 of CIT (A).

Sl. No.	Name of the Company	Operating Profit (%)
1.	Eclerx Services Ltd.	90.34%
2.	Iservices India Private Ltd.	50.27%
3.	Mold0tek Technologies Limited	113.49%
4.	Vishal Information Technologies Ltd.	51.19%

8.1 The assessee requested that the above exceptionally high profit cases should be excluded. The assessee placed reliance on several decisions of Tribunal in support of the said proposition. CIT (A) however, did not accept the contentions raised. It was observed by him that the high/low profit alone was not a **factor** for excluding the comparables and only in cases where such high/low profit was on account of factors affecting to the comparability of the companies, these cases could be excluded. CIT(A) placed reliance on the decision of Mumbai Bench of Tribunal in case of DCIT Vs. BP India Services (P) Ltd. in ITA 4425/Mum/2013. CIT (A), accordingly, rejected the plea of the assessee to exclude the above four comparables on the ground of high profit margin alone.

9. The assessee also raised objections on the ground of functional comparability. It was submitted that out of the twenty three companies selected by TPO, 21 were functionally not comparable with the assessee as they were not engaged in voice based call centre. These were providing high end services such as Knowledge Process Outsourcing (KPO), Software Development etc. It was argued that the assessee was operating in the lowest strata of various ITES services as the nature of work was similar to customer care centre. The assessee referred to the billing rates per hour given in the NASSCOM report in relation to different sections of ITES services to point out that there was steep difference in the billing

rate between the low end services and high end services. In this regard, the statistics from the NASSCOM strategic review 2005 was given as under;-

Sl. No.	Type of Service	Billing Rate per Hour
1	Customer Care	10-14$
2.	Payment services	12-15$
3.	Finance	12-15$
4	Admin	12-15$
5	Human Resource	15-17$
6	Content Development	18-24$
7	Knowledge Process Outsourcing ("KPO")	30-34$

9.1 The assessee further submitted that the candidates employed by the assessee were graduates/under graduates with English speaking skills as nature of work handled by them did not require any special skills like those possessed by software professionals, technical consultants, accountants etc. It was pointed out that ITES/BPO had a wide network of services such as high end services like content development, finance and account, HR etc, which required specialized skills. It was also pointed out that several companies selected by TPO were engaged in content development and knowledge process outsourcing and other high end segments and, therefore, these companies were functionally not comparable. The assessee placed reliance on some decisions of Tribunal in support of the plea that these companies were not comparable.

9.2 The CIT (A) after considering the submissions of assessee observed that the assessee had itself mentioned that several companies selected by the TPO were in ITES/BPO segment and therefore these were functionally comparable. CIT (A) also observed that the assessee had submitted functional details of the companies on the basis of the details available on the web site which was not correct as details only from audited accounts should be taken. After considering the details as per audited accounts, CIT (A) observed that in many cases functions of the company had been mentioned as computer software but in fact these were not in development of computer software. He referred to Accentia Technologies Ltd. which had most of the revenue from medical transcriptions and therefore it was not a software company. Similarly Apex Knowledge Solution Ltd. was engaged in contact management and not providing any computer software services. The assessee had mentioned that Genesys International Corporation Ltd. was providing computer software services but actually the company was helping in the management of information creation flow and analysis through information technology and therefore the function was similar to an ITES company. Other companies were operating in the field of BPO/KPO, Medical Transcription, whose functions were similar. CIT (A) further observed that though billing rate in case of high end ITES services was high, corresponding expenses on employees were also high and, therefore, it did not impact the margins much. Since, the functions of these companies were similar, CIT (A) observed that these could not be excluded.

10. CIT (A) accordingly rejected most of the functional objections raised by the assessee and agreed that only in six cases there were functional differences and therefore held that only these comparables should be excluded. The details of these six comparables and the reasons given by CIT (A) for exclusion are given below:-

Sl. No.	Name of the Company	Reasons for exclusion
1	Bodhtree Consulting Ltd. (Seg).	Company engaged mainly in software development and therefore functionally not comparable
2.	ICRA Techno Analytics Ltd. (Seg).	The company helps in identifying, designing, billing and maintaining solutions that are continually comparatible with business and technology strategies. The function are therefore not comparable to that of the assessee.
3.	Infosys BPO Ltd.	This company is an ITES/BPO company but it has grand value and incurs heavy marketing and selling expenses and cost on software package for own use and therefore not comparable.
4.	Wipro Ltd.	Reasons for exclusion are same as above.
5.	Triton Corp. Ltd.	The annual report of the company shows that the company was engaged in trading of ITES Peripherals and had incurred 14.07% of total expenses on account of purchases and

		disclosed inventory of stores in the financials. The company has single segment i.e. IT and ITES. There is no separate ITES segment, and, therefore, not comparable.
6.	Maple (E) Solutions Ltd.	This company was acquired by Triton Corp Ltd. w.e.f 1.1.2007. Therefore non comparable on the same ground on which Triton Corp Ltd. was excluded. Thus this company was also to be excluded from the comparables.

11. The assessee also pointed out errors in the margin of comparables computed by the TPO. It was pointed out that based on date available in the public domain, margins were found to be different than those computed by TPO on the basis of information obtained u/s 133 (6) in case of four companies i.e. Flextronics Software (Seg), HCL Comnet (Seg), Moldtek Technologies Ltd and R. Systems International ltd. It was pointed that in case correct margin was taken the mean margin of comparables would come to 29.26 against 30.75% computed by TPO.

11.1 CIT (A) after considering the submissions of the assessee directed the TPO to look into the margin computation given by assessee and rectify the same if required at the time of giving effect to the appellate order.

12. The assessee also requested that adjustment may be allowed on account of working capital and linked cost and other costs incurred by the AE on behalf of the assessee. It was pointed out that after making these adjustments, the margin in the case of assessee would come to 17.04%. The assessee pointed out that rule 10B (3) (ii) and Rule10 C (2)(e) permitted adjustment to eliminate material defects of the difference between the assessee and comparables. The assessee also referred to the decision of Tribunal in the assessee's own case in assessment year 2005-06 in which the same issue had been restored by the Tribunal to the file of Assessing Officer. CIT (A) however did not accept the contentions raised. He referred to the rule 10B (1) (e) (iii) as per which net profit margin of the comparable uncontrolled transaction is required to be adjusted to take into account the difference between the international transaction and the comparable uncontrolled transaction. CIT (A) observed that the assessee had not submitted any factual details in respect of the comparables indicating need for any such adjustment. It was also observed by him

that the assessee had not made any such adjustment in the transfer pricing study. The assessee made the claim only when the TPO proposed to exclude certain comparables or to include certain other comparables. Therefore CIT (A) held that claim could not be allowed now as held by the Tribunal in case of Symantec software sales (P) Ltd. As regards the reference by the assessee to the decision of the Tribunal in assessment years 2005-06 and 2006-07, CIT (A) observed that in these orders, ITAT had only set aside the issue and not allowed the claim to the assessee. CIT (A) also observed that no comparables were perfect without any difference or variation and to account for such difference standard deviation of +/- 5%, has been provided in the Act while computing the ALP. CIT (A), therefore, rejected the claim of the adjustment made by assessee.

13. The assessee also claimed the benefit of +/- 5% deviation to the on sale price as provided in the *proviso* to section 92 C (2). The assessee referred to several decisions of Tribunal in support of the claim. CIT (A) however observed that the second *proviso* to section 92 C (2) was amended by the Finance Act 2009 to provide that the standard deviation can be allowed only if the arms length price was within the 5% of the transfer price. It was further clarified by the finance Act 2012 that the said amendment would apply to all assessments and re-assessments pending before the Assessing Officer as on 1.10.2009. Since in this case, the proceedings were pending before AO/TPO as on 1.10.2009 and the ALP determined by the AO exceeded the transfer price by more than 5%, CIT (A) did not allow the claim of the assessee.

14. The assessee further argued before CIT (A) that in TNMM method the net profit margin could be computed in relation to cost incurred, sales affected or asset employed as provided in the Rule 10B (1) (e) (i). It was submitted that though the assessee had computed the margin on the operating cost, it had requested the TPO compute the same on assets employed. It was pointed out that margin of the assessee on the basis of asset employed was 54.04% which was more than the margin of 47.76% of the comparables selected by TPO and margin of 11.37% of

the comparables selected by the assessee. It was, therefore, urged that in view of the higher margin on the asset employed, no adjustment was required to be made. After considering the submissions of the assessee. CIT (A) observed that the assessee was a service provider and ran the dedicated call centre which was being remunerated on cost plus basis by the AE. In case of cost plus remuneration, return on asset employed would not adequately capture all the costs associated with functions undertaken and risk assumed. CIT (A) also observed that in case of service industry, the main asset was human resource which was not reflected in the balance-sheet of the company. Therefore in computing return on asset employed the main asset cost will go out of consideration. CIT (A) thus held that PLI as return on asset employed was not suitable in this case and accordingly rejected the claim.

15 CIT (A) thus directed the Assessing Officer/TPO to re-compute the transfer pricing adjustment in the light of decision taken by him in relation to the comparables and the various claims made by the assessee. Aggrieved by the decision of the CIT (A), the assessee is in appeal before Tribunal objecting to the 15 comparables selected by TPO which had been upheld by CIT (A), exclusion of one comparable selected by the assessee and the rejection of other claims of the assessee on various issues, whereas the revenue is aggrieved by the decision of CIT(A) excluding the six comparables selected by the TPO.

16. We first deal with the various disputed raised by the assessee in the appeal. The first dispute is regarding the selection of comparables and the decision of CIT (A) to uphold the selection of 15 comparables selected by TPO and exclusion of one of the comparables selected by assessee i.e. Optimus Global Services Ltd. The learned AR submitted that 15 comparables selected by TPO and upheld by CIT (A) were operating in different segments of ITES and were not providing services similar to that of the assessee, which was running a voice based call centre. The comparables selected by TPO provided different services such as software services, geographical information service, medical transcription service, knowledge process outsourcing services etc., which were not comparable to the case of the assessee. It was pointed out that under Rule 10B (2) the comparability of international transaction with uncontrolled transaction has to be judged with the reference to

characteristics of the services rendered and the functions performed. Since the functions performed and the services rendered were different, these cases were not comparable. It was pointed out that some of the comparables were engaged in high end IT enabled services such as KPO, medical transcription, etc., requiring skilled employees and therefore, these were not comparable to the case of the assessee and should be excluded. It was also argued that certain comparables selected by the TPO had super normal profits and therefore these were not comparable and should be excluded. Reliance was placed on some decisions of the Tribunal in support of the plea. In regard to Optimus Global Services Limited., the comparables selected by the assessee which had been excluded by CIT (A), it was submitted that the said company was functionally comparable and had been set up around the same time when the assessee company was set up and therefore, it should not be excluded only on the ground of persistent losses. It was also pointed out that the said company had earned profit in the assessment year 2008-09

17. Learned CIT(DR) on the other hand submitted that the assessee was providing IT enabled services (ITES) as a call centre. It was pointed out that as per the details given by the assessee in para 9.3.1 at page 93 of the paper book. the assessee had made the search based on ITES. He also referred to the details given by the assessee in para 6 at page 181 of the paper book in which it was mentioned that the assessee belonged to ITES/BPO industry. The learned CIT (DR) also referred to NASSCOM's member directory a copy of which was placed on record as per which the assessee had been characterized as BPO/IT service company. Thus, the assessee was providing the ITES or Back Office Operation (BPO). He referred to the CBDT notification SO 890 (E) 26.9.2000 issued in connection with section 10 A and 10B in which IT enabled product or services were defined to mean:-

(i) Back office operation

(ii) Call centers

(iii) Content development or animation,

(iv) Data processing

(v) Engineering and design

(vi) Geographic Information System services.

(vii) Human Resource services.

(viii) Insurance claim processing.

(ix) Legal database

(x) Medical transcription

(xi) Payroll

(xii) Remote Maintenance

(xiii) Revenue Accounting

(xiv) Support Centers, and

(xv) Web site services."

17.1 The learned CIT (DR) argued that the services provided by the comparables selected by TPO fell in the category of ITES. It was pointed out that in a particular category of service no distinction can be made between high end and low end services as argued by learned AR as in TNMM method which the assessee had followed, standard of comparability was relatively relaxed and broad similarity of function was required. It was also submitted that the comparables selected by TPO broadly performed functions similar to that of the assessee and were part of ITES segments and therefore, these could not be rejected on the ground of high end activity. He referred to the decision of Hyderabad bench of Tribunal in case of Delloite Consultancy India (P) ltd. in ITA 1082/HYD/2010, in which the Tribunal held that " No two comparable companies could be replica of each other". Reference was also made to a decision of Delhi bench of Tribunal in case of ACTIS Advisors in ITA 122/Delhi/2011 in which it was held that it was quite difficult to get accurate comparables and in case the assessee wanted that IT enabled services should be further dissected, there will not be any end to it and it would be a very subjective exercise.

17.2 The learned CIT DR further submitted that even the comparables selected by the assessee were not engaged in activities which were exactly that of the assessee. He referred to the services performed by those comparables which has been given in table below to point out that the services being provided were not identical to that by the assessee:-

S. No.	Name of the Company	Remarks
1.	Allsec Technologies Ltd.	Call centre, customer services, HR and Payroll processing.
2.	Ask Me Infor Hubs	Telemarketing and customer support services
3	Godrej Upstream Ltd	Contact Center Solution in Travel Domain
4.	NIIT Smart Serve Ltd.	Insurance and financial services call centre, web/e-mail based support services, back office processing
5	Nipuna Services Limited	Contact center
6	Optimus Global Services Limited	Comprehensive Portfolio
7	Transwork information Services Ltd	Financial services, Telecom, Technology and hospitality, Call centre, order processing, claims processing, and loan/mortgage processing.
8	Sparsh BPO Services	Business to Business and Business to customer services
9	HTMT Global solutions	HTMT provides consultancy and development services covering business domain knowledge, technology and process in the domains of automotive, insurance, IT, Customer Services banking, finance and telecom

17.3 Learned CIT DR further submitted that high profit margin or low profit margin could not be the basis for exclusion of a particular comparable, if the comparable is functionally comparable to that of the assessee. He therefore, objected to the argument of learned AR to exclude the four comparables having very high profit margin starting from 50.27% to 101.77%. He placed reliance on the latest decision of Tribunal in case of Willis Processing Services India (P) Ltd. in ITA no4547/Mum/2012 for the assessment year 2007-08. The learned CIT (DR) also supported the decision of CIT (A) to exclude the persistent loss making comparable i.e. Optimus Global Services Ltd. He referred to the decision of Hyderabad bench of Tribunal in case of Brigade Global Services (P) Ltd. in which it was held that in case the company was incurring continuous loss year by year it should not be considered as comparable and following the said judgment, the Mumbai Bench of Tribunal in case of Goldman Sach (I) Securities (P) ltd. held that for excluding a comparable the persistent loss has to be for a period of three years. It was also submitted that there was no merit in the contention of the learned AR that age and formation of the company should also be criteria for comparability analysis as held by the Mumbai bench of Tribunal in case of FIRMENICH Aromatics (1) (P) Ltd. in ITA no. 2056/Mum/2006. As regards the argument of the Learned AR that said company had a profit in assessment year 2008-09, it was submitted that for making comparability analysis, data of subsequent year could not be considered under the rules.

18. The details of functions of the 15 comparables of the TPO accepted by CIT (A) as given by the learned AR and the arguments of the department as to why the decision of CIT (A) should be uphold as summarized in the table below:-

Sl. No.	Name of the Company	Functional Difference Pointed out by the AR	Arguments of the Revenue
1	Accentia Technologies Limited	Computer Software, Medical Transcription Billing and Coding and Software Sales	The Profit and Lost Account and the Schedule of Revenue is attached which shows that almost 67% of the revenue of the company is from medical Transcription and Billing and Coding which are ITES activities. Medical Transcription is ITES as per notification no. 890 dated 26.9.2000
2	Apex Knowledge Solutions Ltd.	Computer Software-database creation services	Annual report of the company shows that the revenue is generated from export of software and related activity Schedule 12 shows exports of software and related ITES activities. There are no segmental available
3	Apollo Healthcare Ltd.	Medical Transcription-Medical BPO	Medical Transcription is ITES as per notification No. 890 dated 26.9.2000
			In Willis Processing Services India Pvt. Limited in Para No.25 this company was excluded by the ITAT for the reason that there are related

			party transactions of 81% in this company
4	Asit C Mehta (Nucleus Netsoft)	ITES/Portfolio Management Services and Investment	The annual report of the company shows that the income is from ITES Content development is ITES as per notification no. 890 dated 26.09.2000.
5	Caliber Point Business Solutions ltd.	Computer Software-business process management	Annual report of the company shows that segmental accounts are available and BPO segment's results can be used for the purpose of comparison.
6	Cosmic Global Ltd	Translation Charges-Medical Transcription and consultancy services and Accounts BPO	The annual report of the company shows that the company is deriving income from medical transcription, Translation charges and BPO
			Medical Transcription is ITES as per notification No. 890 ated 26.09.2000 **However the translation charges are not covered in notification No. 890 dated 26.09.2000.**
7	Datamatics Finacial Services Ltd. (Seg).	ITES/BPO-ITES in the field of financial accounting services and internet based research services as per the information collected by the TPO u/s133 (6)	Annual report of the company shows that it is deriving income from Processing and Printing and export of ITES. There are no segmental results available so the margins of ITES cannot be computed.
8	Eclerx Services Ltd.	(i). ITES/BPO-BPO Services	The annual report of the company shows that it is engaged in BPO services.
		(ii) High Profit Margin	**Rely on the discussion in Para No. 34 of Willis Processing Services India Pvt. Ltd in which it was decided that a company cannot be excluded on the basis of high or low margin.**
9	Genesys International Corporation Ltd.	Computer-Software Geographical Information Services	The annual report of this company shows that it is deriving income from GIS activities which is an ITES activity as per Notification No. 890 dated 26.09.2000. Accepted as comparable by ITAT in Willis Processing Services India Pvt. Ltd.
10	HCL Comnet (seg)	Telephonic Communication and	The annual report of this company shows there are segmental results

		ITES-comprising data centre management services, end user computing services, networking services & tools & process consulting services	available for ITES segment which can be used for the purpose of comparison.
11	Informed Technologies India Ltd.	ITES/BPO-KPO services	The annual report of the company shows that the revenue is derived from BPO activities. There is no reference in the annual accounts of the KPO activities.
12	I Services India Pvt. Ltd.	(i). ITES/BPO-BPO unit providing back office services. Further as per the information u/s 133 (6) of the Act for AY 2008-09 and AY 2009-10 the company is engaged in providing remote data services and GIS.	The information collected by the TPO for subsequent year cannot be used for the current financial year since the functional profile of the company might change. GIS activities is an ITES activity as per notification no. 890 dated 26.09.2000.
		(ii) High Profit margin company	**Rely on discussion in para No. 34 of Willis Processing Services India Pvt. Ltd. in which it was decided that a company cannot be excluded on the basis of high or low margin.**
13	Mold Tek Technologies Limited	ITES/BPO-KPO Division	The annual report shows that the company has segmental accounts which can be used for the purpose of comparison. In the case of **Willis Processing Services India Pvt. Ltd it is held on page 48 (para 34.5) that KPO is a term given to the branch of BPO**
		High Profit Margin	**Rely on discussion in Para no. 34 of Willis Processing Services India Pvt. Ltd in which it was decided that a company cannot be excluded on the basis of high or low margin.**
14	R.Systems	ITES/BPO-sale of	In the annual report the BPO

	International Ltd. (Seg.)	software products and software development services	segment is available and the same can be used for the comparison.
15	Vishal Information Technologies Limited	i. ITES-BPO-Digital Library and Print on Demand	The annual report of the company shows that the income of this company is derived from ITES activities.
		ii High Profit margin company	**Rely on discussion in Para No. 34 Willis Processing Services India Pvt. Limited in which it was decided that a company cannot be excluded on the basis of high or low margin.**

19. The learned AR for the assessee in the reply to the arguments advanced by the learned CIT (DR), submitted that reliance on the classification of IT enabled services in the CBDT notification no.890890 dated 26.9.2000 was misplaced as the said notification was in relation to claim of exemption u/s 10A and 10 B and referred to both products and services and, therefore, these could not be applied only to services. Moreover, the comparability had to be decided on the basis of characteristics of services rendered and functions performed which was not so in all the cases in the list. He referred to engineering and design services, GIS, and content development and animation appearing in the list to point out that these were totally different services involving skilled professionals, which was not so in case of call centre. It was also pointed out that if one were to go by the definition of ITES as per the notification, KPOs and BPOs which did not appear in the list have to be excluded. It was therefore urged that said classification was of no relevance to the issue under consideration. As regards the decision of ITAT in case of Actis Advisors (P) Ltd. (*Supra)* referred to by learned CIT DR, it was submitted that facts of the case were different as the nature of service was consultancy and advisory. In that case neither assessee nor TPO had gone into the horizontal or vertical functional line within the IT enabled services. It was under these circumstances that the Tribunal held that comparable could not be rejected as it was operating in a different line but in the same sector. The learned AR also referred to the decision of Tribunal in case of ITO Vs. CRM services (P) Ltd. (14 Taxmann.com 96) in which it was held that comparables which are non voice

based BPO should not be compared with voice based BPO. It was pointed out that the said decision of Tribunal had not been brought to the notice of Tribunal in case of Actis Advisor (P) Ltd. *(Supra).* In regard to reliance placed by the learned CIT (DR) on the decision of Tribunal in case Willis Processing Services India (P) ltd. *(Supra),* it was submitted that loss or extreme profit case should be further examined for such extreme results and they can be excluded if these are on account of difference in characteristics of services rendered or functions performed. It was also pointed out that in case of Willis Processing Services India (P). Ltd. *(Supra),* comparables of HCL Comnet Services Ltd. and R.System International Ltd. had been excluded by the Tribunal on the ground of related party transactions.

19.1 The learned AR further submitted that extraordinary profit in case of Mold Tek Technologies was because in that case KPO division had been rendering engineering services to high rise buildings as was clear from the annual report of the company placed on record and, therefore, the case was not comparable to that of the call centre. Similarly, Eclerx Services Ltd. which had shown extraordinary profit had tremendous goodwill among the customers which was nothing but the asset employed, even if the same was not recorded in the books. Moreover, Eclerx Services Ltd. was operating in the field of KPO which was different from call centre activity as was clear from the activities of the company given in the annual report placed on record. In case of Vishal Information Technologies Ltd. having very high margin it was pointed out that the tTribunal in case of Capital IQ information systems (P) Ltd. in ITA no. 1961/HYD/2011 for assessment year 2007-08 noted that this company outsourced its work to 3rd parties and, therefore, it had different model. Moreover, the said company had employed 75 seats (utilized 60 seats) as was clear from the order in case of Willis Processing Services India (P) Ltd. (*Supra)* whereas the assessee had 2840 seats. It was pointed out that number of seats was nothing but asset employed and, therefore, because of huge difference in asset employed, the company should be excluded. He also referred to the decision of Tribunal in case of Mersk Global Services Ltd ITA/3774/Mum/11 in which it was held that the company running on its own account cannot be compared to the company that was outsourcing work. It was therefore, submitted that this case was also not comparable. In relation to I Services India (P) Ltd. it was submitted that thought the profit in this year was 50.28% the profit in the next year was 9.66% which showed that there was something extraordinary this year resulting into high profit and therefore it should be excluded. Reliance was placed on the decision of Tribunal in case of Actis Advisors *(Supra).*

19.2. In regard to exclusion of comparables on account of extraordinary events like merger, demerger, amalgamation, it was submitted that Tribunal in case of Capital IQ *(Supra)* clearly held that in such cases comparable has to be excluded. The Tribunal in case of Willis Processing Services India (P) Ltd (*Supra)* had taken the same view but held that in case, because of the merger/demerger, the company become functionally different then it should be excluded. It was pointed out that in addition to functional difference, factors like synergies of operation, change of management, operational efficiencies etc are also to be considered. It was pointed out that this aspect had not been examined and, therefore, it was requested that the case of Accentia Technologies and Mold Tek Technologies should be set aside to AO for examination of these aspects.

19.3 In regard to the submission of learned DR that even activities of comparables selected by the assessee were not exactly the same, the learned AR referring to the relevant portion of annual reports of the companies, pointed out that these companies were largely in the call centre business either exclusively or pre-dominantly. It was pointed out that the other activities listed by the Learned DR may be only incidental activities. The learned AR however admitted that the annual report was not clear on the exact nature of services rendered in case of Transwork Information Services Ltd. However, the assessee being in the same business was aware that the nature of business of the said company was pre-dominantly call centre and other activities were only incidental. In case of NIIT Smart Serve, the learned AR referred to the relevant portion of the annual report to point out the party had operations both in Back Office and Voice processing. It was thus, argued that the comparables selected by the assessee were largely in the same business in which the assessee itself was placed.

20. We have perused the records and considered the rival contentions carefully. The dispute is regarding selection of comparables for bench marking the international transaction entered into by the assessee. The assessee had selected 9 comparables as unrelated parties for comparing the transaction in case of the assessee. The AO further selected 23 more comparables out of which 2 comparables i.e. Spanco and Flextronics (Seg.) were accepted by the assessee as comparable and the 21 comparables were disputed by the assessee. Out of these 21 cases, CIT (A) has accepted the claim of the assessee in six cases holding that these cases are not comparable to the case of the assessee on different grounds. The remaining 15 comparables selected by the TPO have been upheld by the CIT (A) as comparables to the case of assessee The assessee has disputed the said order of CIT (A).

20.1 The assessee has followed TNMM method for making the transfer pricing adjustment in relation to the international transaction entered into by the assessee. Therefore, the arithmetic mean of the margins of the comparables is required to be compared with that of the assessee for the purpose of making TP adjustment. The selection of comparables is important, which must be operating in the same field in order to insure that accurate adjustment as provided under the law is made. The assessee is providing IT enabled services as call centre about which there is no dispute. The assessee conducted the search for companies engaged in ITES which is clear from the note submitted by the assessee before the TPO on TP study in para 3.3.1 at page 193 of the paper book. In para 6 of the note at page 181 of paper book, the assessee has mentioned that it belongs to ITES/BPO industry. The learned DR has also placed on record the NASSCOM member directory, in the relevant portion of which the assessee has been described as ITES/BPO company. It is thus clear that the assessee is providing ITES/BPO services. The case of the assessee that ITES/BPO industry is divided into several segments and, therefore, assessee had selected only those companies which were pre-dominantly engaged in call centre business. It has also been submitted that ITES/BPO industry has several segments starting from low segment such Call centre, Customer Care to high end segments such as KPO, content development etc. in which there is wide variation in the billing rates. NASSCOM report on billing rate for different segments has been placed on record. It has thus, been argued that high end services are not comparable to the case of the assessee.

20.2 The comparability of transaction or the selection of comparables in our view has to be examined in terms of the rules framed in this regard. The Rule 10B (2) provides that the comparability of international transaction with uncontrolled transactions has among other things to be judged with the reference to characteristics of services provided, functions performed, asset employed and risk assumed. It has therefore to be insured that functions of the comparables and characteristics of services rendered are similar. Viewed from this angle, we find that all companies which are in ITES segment are providing similar services and difference is in the internal working which is reflected through difference in qualifications and skills of the employees. In all these cases employees are the main assets who are providing various services using Information Technology (IT). The main difference is the skills/qualification of the employees engaged who are providing the services. The employees are the main assets of these companies and therefore, the difference is mainly in the assets employed. Therefore, we have to examine whether difference in the skill/qualification of the employees or their payment structure is going to affect the comparability in any significant manner. TNMM method is tolerant to minor differences and, therefore, even if there are some differences unless they materially affect the margin, the comparables could not be excluded. This is clearly provided in the Rule 10 B (3) as per which an uncontrolled transaction has to be taken as comparable to the international transaction if none of the differences between the transactions compared or the enterprises entering into such transactions are likely to materially affect the price charged, cost incurred or profit earned and even if there are material differences, the uncontrolled transaction can still be considered as comparable if reasonably accurate adjustments could be made by eliminating the material affects of such differences.

20.3 In this case as we have pointed out earlier that difference in various segments i.e. low end to high end in ITES services is mainly on account of differences in the skill/qualification and pay structure of employees and, therefore, the main point to be considered is whether such differences between employees is going to materially affect the margin of the comparables. The learned AR for the assessee has placed before us the NASSCOM report showing billing rates in different segments of the ITES sector to point out that there is wide variation between low end and high end segments. However only on the basis of billing rates no conclusion could be drawn that margins in different segments of ITES services is also different. This is because if the billing rate is high in the high end services, the cost of the employees who are highly qualified/skilled also goes up steeply and, therefore, the margins are not much affected. Infact, no evidence has been produced before us to show that margins in the high end segments of ITES services is high compared to low end services. Therefore, we are unable to accept the argument advanced by learned AR that the comparables belonging to high end segments such as content development, KPO, Medical Transcription etc. should be excluded from the comparability list on this ground alone. In fact, this view is supported by the latest decision of Mumbai bench of Tribunal in case of M/s Willis Processing Services India (P) Ltd. in ITA no. 4544/Mum/2012 for assessment year 2007-08 dated 1.3.2013 in which the Tribunal after considering the various submissions and decisions of Tribunal relied upon by the assessee held that KPO was a term given to a branch of BPO in which apart from processing data, knowledge is also applied. The Tribunal therefore, held that the KPO could not be excluded from the comparability list. The Tribunal in the case of Actis Advisors (P) Ltd.(*Supra)* have also held that any further dissections of ITES will not be proper as it would be a very subjective exercise. Even in the case of CRM services (P) Ltd (Supra) on which the assessee has relied, there is no finding that margin in case of high end segment of ITES is higher.

20.4 We also note that even in the case of comparables selected by the assessee details of which have been given in para 3 of the order earlier, there is wide fluctuation in the margins of the companies; the lowest margin i.e. 0.34% in case of Ask Me Info Hub Ltd. and the highest margin as 27.98% in case of Allsec Technologies Ltd. Obviously the cases selected by the assessee are not identical otherwise there would not have been so wide variation Excluding the highest margin and the loss case, the average margin of other comparables of the assessee comes to only 4.5% which is 1/6th of the highest margin. Compared to this, the average margin of the comparables of the TPO is within two times the highest margin in case of the assessee. Thus, if the comparables with 1/6th of the highest margin are acceptable to the assessee then, there is no reason for the assessee to be aggrieved with the comparables of TPO where average margin is within twice the highest margin, case selected by the assessee. The objection of the assessee will be valid only if there is material to show that high margin in case of high end services is because of nature of activities. But as it has been pointed out earlier, no such material had been produced. Therefore, we reject the argument advanced based on low end/high end services in the ITES activities.

21 With broad proposition laid down above we may now proceed to deal with the comparables individually to find out if they are suitable for comparison;-

21.1 ACCENTIA TECHNOLOGIES LTD.

This comparable has been objected to by the assessee on the ground of functional differences. It has been pointed out that in addition to Medical Transcription and Billing and Coding, this company is also involved in software sales. The learned DR has placed on record the profit and loss account of the company for the relevant year which shows that out of total revenue of Rs. 50.2 Crore a sum of Rs. 9.6 Crore is from sale of software and revenue from Medical Transcription is 32.1 Crore, which is about 67%of total revenue. There is no segment wise result available in case of Medical Transcription and billing and coding. It is not known by how much the margin is affected by trading in software. Therefore in our view this company could not be considered as a good comparable. We therefore hold that this company has to be excluded.

21.2 APEX KNOWLEDGE SOLUTIONA LTD.

The assessee has objected to the selection of this comparable on the ground that it is engaged in computer software and data base creation services. The annual report of the company for the relevant year has been placed on record which shows that entire revenue has been generated from export of software and related ITES activities. There is no segment wise result available for ITES activity. This company had also been excluded by the Tribunal in case of Willis Processing Services India (P) Ltd.*(Supra)*. We therefore, hold that this company is not a good comparable and has to be excluded.

21.3 <u>APPOLO HELATH LTD.</u>

This company is also providing IT enabled services. The objection of the assessee is on the ground that the services provided are in the high end segment of ITES i.e. Medical transcription and Medical BPO. In our view, as held earlier, on this ground alone the comparable could not be excluded. However, it has been brought to our notice that 81% of the transactions in case of the company are with related parties. With such high RPT, this comparable could not be considered as a good comparable. This comparable had also been considered by Tribunal in case of Willis Processing Services India (P) Ltd. *(Supra)* and had been excluded on this ground. We therefore, hold that this comparable has to be excluded.

21.4. <u>ASIT C. MEHTA (NUCLEUS NET SOFT).</u>

The assessee has objected the selection of this comparable on the ground that it is engaged in portfolio management services also, in addition of ITES. The learned DR has placed on record the annual report of the company which shows that the assessee is in the field of content development which is an ITES. It is also to be noted that almost entire revenue i.e. Rs. 6.09 crore is from ITES and only a sum of Rs. 23.26 lakh is from portfolio management service which is insignificant which in our view will not have much impact on the margins. Content development is a high end service but as held earlier on this ground alone it cannot be excluded. As there is no material to show that in case of high end services in ITES industry margins are higher than those in low segment.

21.5 CALIBER POINT BUSINESS SOLUTIONS LTD.

The assessee has argued that company is not comparable as it is engaged in business process management and other activities. The learned DR has placed on record the annual report of the company which shows that segmental accounts are available in case of BPO segment. The AO/TPO have taken the entire revenue for the purpose of comparison which in our view will not be appropriate. We therefore, direct that the results of only BPO segment have to be considered for the purpose of comparability and subject to the above, the inclusion of this comparable is upheld. Argument based on high segment as held earlier has to be rejected.

21.6 COSMIC GLOBAL LTD.

The assessee has objected to the inclusion of this comparable on the ground that the company is not comparable as it is mainly engaged in translation business in addition to medical transcription, accounts BPO and consultancy. The learned DR has placed on record the annual report of the company which shows that the main revenue i.e. 4.05 crore is from translation business where as revenue from medical transcription is only 9.72 lakh and from BPO at Rs. 12.41 lakh. The translation business is not comparable to the case of the assessee. Therefore, in our view, this company has to be excluded from the list of comparables. We accordingly direct the Assessing Officer to exclude this comparable.

21.7 DATAMATIC FINANCIAL SERVICES LTD. (SEG).

The assessee has objected to this comparable on the ground that functions are different. The perusal of annual report of the company placed on record shows that this company is deriving substantial revenue from processing and printing and export of ITES. About 50% of the revenue is from printing services. The segment wise result from ITES services is not available. Therefore in our view, this company could not be considered as a good comparable and accordingly we direct the AO to exclude this company from the list of comparables.

21.8. ECLERX SERVICES LTD.

This company is engaged in the BPO business which is an IT enabled service. The learned AR for the assessee has argued against the company on the ground of super profit margins, which according to him makes the company non comparable. He has placed reliance on the decision of the Tribunal in case of Capital IQ Information System India in ITA no. ITA/1961/HYD/11. In the said order, the Tribunal held that super normal profit cases should be excluded as not comparable. However as pointed by the learned DR the same comparable was considered in the latest decision of the Tribunal in case of Willis Processing Services India (P) Ltd (Supra) in which the Tribunal after considering the decision in case of Capital IQ *(Supra)* held that the comparable could not be excluded only on the ground of high profit margin. The Tribunal observed that inclusion or exclusion of a comparable could not be decided on the basis of factors other than the factors specified in Rule 10B which does not include the margin or loss. Similarly, as held earlier high end or low end segment of ITES could also not be a ground for exclusion or inclusion of a comparable. It has also been argued that the company had high goodwill with customers which is an asset which gave better margins. No doubt good will is an asset which can bring more customers and can increase turnover but as we have discussed in the subsequent part of this order (para 24.3.3), there is no linear relationship between margin and turnover and that the concept of economy of scale is not relevant in case of service companies. The argument thus, has no merit and has to be rejected. Therefore, in our view, this comparable has to be included and accordingly we uphold its selection.

21.9. <u>GENESYS INTERNATIONAL CORPORATION LTD.</u>

The assessee has objected to the selection of this comparable on the ground that it is engaged in high end ITES services i.e. Geographical Information Service (GIS). As we have held earlier, only on the ground of high end or low end segment, comparable could not be excluded or included. GIS is an IT enabled service. The entire revenue of the company as per the annual report placed on record is from GIS activities. We also note that the Tribunal in case of Willis Processing Services India (P) Ltd. *(Supra)* has accepted this company as a good comparable. We therefore uphold the inclusion of this company.

21.10 <u>HCL COMNET SYSTEMS & SERVICES LTD</u>.

The assessee has objected to this company on the ground that it is engaged in activities different from that of the assessee i.e. telephone communication in addition to ITES. The learned DR has placed on record the annual report of the company to point out that segment wise result for ITES is available, which has been used by the TPO for the purpose of comparison. The Learned AR for the assessee however, pointed out that company had related party transaction up to 21.52% and on this ground this company had been excluded in case of Willis Processing Services India (P) Ltd. (*Supra).* We agree that related party transaction affect the comparability and in case of high RPT the company could not be really considered as independent unrelated party. In case of Willis Processing Services India (P) Ltd. *(Supra)* the Tribunal held that related party transaction can be accepted only up to 15%. We therefore accept the plea of the assessee to exclude this comparable.

21.11 <u>INFORMED TECHNOLOGIES INDIA LTD</u>.

The assessee has objected to this comparable on the ground that it is engaged in high end ITES segment i.e. KPO. The Learned DR, however, placed on record the annual report of the company to point out that revenue is derived from BPO activities and there is no reference to KPO activities in the annual accounts. We also find from perusal of accounts that BPO is only reportable segment and the entire revenue is from BPO activities. We have also held earlier that a comparable could not be excluded only on the ground of high end /low end activities. Therefore, we uphold the selection of this company as a comparable.

21.12. I SERVICES INDIA PVT. LTD.

The assessee has objected to the inclusion of this company on the ground that it has a BPO unit providing back office operation. It has also been submitted that as per the information provided u/s 133 (6) for assessment year 2008-09 and 09-10, the company is also engaged in the business of providing remote data entry services and GIS. The learned DR has pointed out that the subsequent year report could not considered for the purpose of comparability as the activity could change in the subsequent year. Moreover, GIS is an IT enabled service. In our view the annual, accounts of the current year i.e. assessment year 2007-08 are required to be seen to find out whether in the relevant year, the assessee was providing services as comparable to the case of assessee. The learned AR has also raised objection on the ground of high profit margin. We have held earlier that a company could not be excluded only on the ground of high profit margins. The same view has also been taken in case of Willis Processing Services India (P) Ltd. *(Supra)*. It has been pointed out that the margin in the immediate succeeding year year was only 9.66% which showed that the margin this year was exceptional. We do not find the argument convincing. It is clear from the rules that for the purpose of comparability, data of current year and upto past two years in certain circumstances can only be considered and not the data of the subsequent year. It has not been shown before us that profit this year was exceptionally high compared to last year due to some extraordinary factor, which affected the comparability. The argument raised is therefore rejected. With these observations we direct the TPO/AO to verify the actual activities of the company from the annual account of the relevant year and include the same if it is found to be engaged in ITES activities.

21.13 MOLD TEK TECHNOLOGY LTD.

The company has a separate IT division in which it is providing Knowledge process outsourcing (KPO) services for which segmental results are available and which had been compared by the TPO with the case of the assessee. The assessee has objected to this comparable on the ground that it is working in the high end segment of ITES which involves highly skilled employees and, therefore, is not comparable to the assessee. Objections have also been raised on the ground of very high profit margin of the assessee. Learned AR has referred to the annual report of the company placed on record in which it has been pointed out that the assessee during the year started engineering services to high rise buildings for clients in US and Canada which offered excellent growth prospects. It was pointed out profit during the year of KPO division registered an increase of 260% compared to the 204% rise in the turnover. We find that the margins have slightly improved this year and there is nothing extraordinary about it. We have already examined both the aspect i.e. offer of high end ITES services and super normal profit and have held that on these grounds alone, a company could not be held as not comparable. We also find that this company had also been considered by the Tribunal in case of Willis Processing Services India (P) Ltd in which all the aspects were considered and the Tribunal held that the IT division of the company was in the nature of KPO which was operating in the ITES segment and has therefore to be considered as comparable to the case of the assessee. The Tribunal also rejected the ground of super normal profit for excluding the comparable. It was also noted that this company had been found to be a good comparable by the Tribunal in case of Actis Advisors (P) Ltd. *(Supra).* The Tribunal also noted the argument advanced on the ground of merger during the year as recorded by the Tribunal in case of Capital IQ Information (Supra). The Tribunal held that only on the ground of merger/amalgamation the comparable could not be excluded unless it was held that the resulting company was functionally different. The Tribunal restored the merger aspect to the AO/TPO for verification and for fresh decision. Facts in this year are identical. Therefore following the decision of Tribunal in case of Willis Processing Services India (P) Ltd (Supra), it is held that the company is a good comparable subject to the verification of merger aspect and its impact on functional comparability.

21.14. R SYSTEMS INTERNATIONAL LTD. (SEG.)

The assessee has objected to the inclusion of this comparable on the ground that the company is engaged in sale of software products and in software development services which are functionally different and, therefore, not comparable to the assessee company. However, before us, the learned CIT (DR) has placed on record the relevant portion of the annual report of the company which shows that the assessee has also a BPO division for which segmental results are available. The TPO has also taken only BPO segment for the purpose of comparability. We have already held that the company could not be excluded only on the ground of high end services. Therefore, following our decision in earlier part of this order, we hold that this company has to be included as a good comparable and accordingly uphold the order of CIT (A) on this point.

21.15. VISHAL INFORMATION TECHNOLOGIES LTD.

The assessee has objected to the inclusion of this comparable on the ground that the company is engaged in high end BPO services and other functions such as digital library and print on demand. It has also been argued that the company should be excluded on the ground of high profit margin and high turnover as the assessee had 2840 seats compared to 75 seats held by that company. The learned CIT (DR) has however placed on record the annual report of the company for the relevant year which shows that it is a 100% ITES company. The learned CIT (DR) pointed out that digitizing the books was an IT enabled service and so was the print on demand, which was the reason for classifying the company as an ITES company in the annual report. We agree that being an ITES company, it is comparable to the case of the assessee. However, as we have held earlier, supernormal profit or high margin is not a valid ground for exclusion of a comparable. As regards the high number of seats it will mean more employees and more turnover, but as we have discussed in subsequent part of this order at para (24.3.3), there is no linear relationship between margin and turnover and that the concept of economy of scale is not relevant to the service companies. Following the reasoning given therein, we reject the arguments advanced. The learned AR for the assessee, has also sought exclusion of the company on the ground of substantial outsourcing of work. We find that this argument has already been considered by the Tribunal in case of Willis Processing Services India (P) Ltd (Supra). In that case, the Tribunal had considered the argument of the learned DR that the company had seating capacity of 75 out of which 60 had been utilized by the company and, therefore, it was pointed out that the argument that the company was outsourcing work was not correct. The Tribunal further noted the argument of the learned AR that the said information which had been obtained by the learned DR u/s 133 (6) was not addressed to the TPO. The Tribunal, therefore, restored the issue of outsourcing to AO/TPO for fresh examination of relevant facts. The facts in the present case are identical we, therefore, restore the issue of outsourcing to AO/TPO for fresh examination and order after hearing the assessee.

22. OPTIMUS GLOBAL SERVICES LTD.

This comparable had been selected by the assessee. However, both the TPO and CIT (A) have excluded this comparable on the ground that the company was incurring persistent losses for last three years. The argument of the assessee for inclusion of this comparable was that this company was engaged in the same business of call centre and had been set up in the year 2002 which was around the same time the assessee company started business. It has been argued that losses in the business in the initial years is quite normal and it has also been pointed out that in the next assessment year i.e. assessment year 2008-09, the company has started making profit. We have carefully considered the various aspects of the matter. We have already held in earlier part of this order that only loss or super normal profit could not be the sole ground for exclusion of a particular comparable unless there are some factors such as abnormal business conditions which affected the functioning of the company. However, in case, a company is making continuous losses year after year, it definitely reflects some abnormal circumstances and, therefore, the Tribunal in case of Brigade Global Services (P) Ltd. ltd. ITA (1484/HYD/2010) held that the company could not be considered as comparable as it was incurring continuous losses year after year. The Tribunal in case of Goldman Sach (I) Securities (P) Ltd. (Supra) have also held that in case a company had persistent losses for a period of three year it has to be excluded. In the present case the company has been incurring losses for the last three years. The argument of the learned AR that in subsequent year the assessee company had a profit could not be accepted as for the purpose of comparability only the results of current year or up to past two years could be considered and not the results of subsequent year. The learned CIT (DR) has also brought to our notice the decision of Tribunal in case of FIRMENICH Aromatics (I) (P) Ltd. in ITA no. 2056/Mum/06 in which it has been held that age and formation of the company could not be the criteria for the purpose of making comparative analysis. Therefore, considering the various decisions of Tribunal (Supra) and facts of the case, we are convinced that this company which has persistent losses for the last three years has to be excluded. The order of CIT (A) is, therefore, upheld on this point.

23. **Comparables of TPO excluded by CIT (A)**

As pointed out earlier, out of 23 new comparables selected by TPO, 2 comparables had been accepted by the assessee and out of the remaining 21, 15 comparables have been accepted by CIT (A) which have already been dealt with. The 6 comparables which have been excluded by CIT (A) are as under:-

Sl. No.	Name of the Company	Margin
1.	Bodhtree Consulting Ltd. (Seg).	29.58%
2.	ICRA Techno Analytics ltd. (Seg).	12.24%
3.	Infosys BPO Ltd.	28.78%
4.	Wipro Ltd. (Seg)	29.70%
5.	Maple Solutions Ltd.	34.05%
6.	Triton Corp Ltd.	34.93%

24. We take up each company separately for examination and analysis with a view to decide its comparability to the case of the assessee

24.1 BODHTREE CONSULTING LTD. (SEG.)

The TPO had selected the company as an ITES company holding it comparable to the case of assessee CIT (A) held that the company was engaged in software business and therefore functionally not comparable and has thus excluded it. The learned CIT (DR) has placed some fresh materials before us, which has been collected by the revenue u/s 133(6) of the IT Act. The information gathered shows that the assessee in addition to developing software, is also engaged in data cleansing services, the segmental results for which are available which is an ITES activity. The learned AR for the assessee pointed out that there is some element of software development also involved in providing such services. We find that this issue had come up for consideration by the Tribunal in case of Willis Processing Services India (P) Ltd. in which the Tribunal restored the issue to the file of AO/TPO for examination of material collected u/s133 (6) of IT Act. Therefore, following the decision of the Tribunal (Supra) we restore this issue to the file of AO/TPO for fresh decision after considering the fresh material and after hearing the assessee.

24.1 ICRA TECHNO ANALYTICS LTD. (SEG.)22

The assessee has objected to the inclusion of this comparable on the ground that the company was into software business and is also engaged in high end ITES segment. CIT (A) has accepted the argument of the assessee and excluded this comparable. The annual report of the company has been placed on record before us by the learned CIT (DR) which shows that the company is dealing in computer software, software development, consultancy and training. We also find that this company had been considered by the Tribunal in case of Willis Processing Services India (P) Ltd. (Supra) in which the Tribunal noted that the company had 23.86% related party transactions. The Tribunal in the said case held that any company having related party transactions more than 15% has to be excluded as comparable. Therefore, following the decision of Tribunal in case of Willis Processing Services India (P) Ltd. (Supra), the exclusion of this comparable by the CIT (A) is held valid.

24.3 INFOSYS BPO LTD.

The company is engaged in BPO business which is an ITES activity. The assessee has objected to the inclusion of this company on the ground that the company had high brand value and incurred heavy expenditure on marketing and selling expenses and on acquisition of software package for its own use. CIT (A) has accepted the objections of the assessee and excluded this comparable. The learned CIT (DR) has argued that the arguments advanced by the assessee had been considered by the Tribunal in case of Actis Advisors (P) Ltd. in ITA no. 5277/Del/2011 and had not been accepted. The learned AR, however, pointed out that brand was a valuable asset which as per rules is one of the factors for deciding the comparability. It was pointed out that this aspect had not been considered by the Tribunal in case of Actis Advisors (P) Ltd. (Supra). Besides, it has also been argued that the companies in the high end BPO segment of ITES on which ground also the company shall be excluded. It has been further argued that in the TP study the assessee had considered only the companies whose turn over was up to Rs. 500 Crore, whereas the turnover of the assessee is 649.57 Crore. It has therefore been argued that the company should also be excluded on the ground of high turnover. Reliance has been placed on some decisions of Tribunal in support of the turnover filter. It was also brought to our notice that the issue whether turnover could be the basis of exclusion of a comparable has been referred to the special bench recently. However, both the parties agreed that the comparability of the company may be decided on the basis of existing decisions.

24.3.1 The learned DR on the other hand submitted that high margin or turnover could not be the basis for inclusion of the comparables. It was pointed out that the issue of turnover has been examined in detail recently by the Tribunal in case of Willis Processing Services India (P) Ltd. (Supra) as well as in the case of Capgemini India (P) Ltd. in ITA no. 7861/M/2011 and not accepted.

24.3.2 We have carefully considered the various aspects of the issue and the rival arguments advanced by both the parties. We have already held that high end services in ITES sector could not be the basis for exclusion of comparables. Similarly, we have also not found the arguments based on high margin convincing for the reason given earlier. The argument of the learned AR based on brand value and high marketing /selling expenses had been examined in detail by the Tribunal in case of Actis Advisors (P) Ltd. (Supra). The Tribunal noted that high marketing expenses did create marketing intangibles such as brand. But it was not necessary that it always resulted into high margin. The Tribunal in that case noted the finding of TPO that 95% of the revenue of Infosys came from repeat business which showed that marketing intangibles did not help Infosys to get any better business. The Tribunal also accepted the finding of TPO that marketing intangibles may be helpful in getting better business but the same may not be applicable in the case of service industries like ITES. The department in that case had placed on record some instances in which companies with much lower marketing expenses had shown much higher margin. The Tribunal therefore, concluded that marketing intangibles such as brand could not be considered as a factor for raising the margin in a particular case. Brand is an asset which can bring in more business and can give more turnover but there is no evidence to show that it results in higher margin. Brand is no doubt an asset which is a relevant factor for deciding comparability but in the absence of any concrete material to show that it raises the margin, the argument based on branding cannot be accepted. We therefore, follow the decision of Tribunal (Supra) and reject the arguments advanced based on high marketing expenses and branding.

24.3.3. The argument based on turnover has also been examined in detail by the Tribunal in case of Willis Processing Services India (P) Ltd. (Supra) and in case of Capgemini India (P) Ltd. (Supra) and not found acceptable. In that case material in the form of graph and chart had been placed by the department before the Tribunal to point out that there was no linear relationship between turnover and margin and it was pointed out that in many cases with rise in turnover the margin came down. The Tribunal in both the cases referred to above also noted the argument based on concept of economy scale and held that it was relevant to manufacturing concerns and not applicable to service companies. The Tribunal in case of Capgemeni India (P) Ltd. (Supra) noted that employees in service companies were not doubt, valuable assets which have to be considered as a factor for comparability. The Tribunal observed that the assets employed had two dimensions i.e. quantity and quality, more employees would mean more turnover but there was linear relationship between margin and turnover. As regard the quality of employees, the Tribunal noted that this would depend upon the nature of projects and employee cost being more in case of more skilled manpower, it will not result into higher margins. Therefore following the decisions of Tribunal (Supra), we reject the argument advanced for exclusion of Infosys BPO Ltd. and accordingly hold that this has to be accepted as a good comparable.

24.4 **<u>WHIPRO LTD. (SEG.)</u>**

The case of Wipro Ltd. which has been excluded by CIT (A) is identical to the case of Infosys BPO Ltd. with only difference that turnover in case of Wipro Ltd. is 939.78 whereas in case of Infosys BPO Ltd. the turnover is 649.57. The argument advanced by the assessee for exclusion of this comparable is the same as advanced in the case of Infosys BPO Ltd. Therefore, for the same reasons given in case of Infosys BPO Ltd. we reject the argument advanced and uphold the inclusion of this comparable by Assessing Officer/TPO.

24.5 <u>Maple (E) Solutions</u>

This company is in the call centre business. A copy of the annual report placed on record by learned CIT (DR) shows that call centre revenue is 12.21 crore and sale of software is only Rs. 9000/- which is negligible. Therefore, almost whole of the revenue is from call centre. CIT (A) has excluded this comparable on the ground that it has related party transactions. CIT (A) also noted that this company became subsidiary of triton w.e.f 1.1.2007. Since, CIT (A) had excluded Triton ltd and therefore held that this company should also be excluded on this ground. The Leanred CIT (DR) pointed out, referring to the details given in the annual report of the company, that there were three related parties but there were no transactions with those parties on revenue account and the transaction were only on account of loan etc. These factual details placed on record have not been controverted by the learned AR. Therefore, this company could not be excluded on the ground of RPT. We also note that this company had become a subsidiary of triton w.e.f 1.1.2007. There was no merger or amalgamation of the two companies. The subsidiary company remains an independent company till it is merged. Therefore argument advanced by the learned AR on the ground of merger could not be accepted. Further, even if there was merger, as held by the Tribunal in case of Willis Processing Services India (P) Ltd. (Supra), only on the ground of merger, the comparable could not be excluded. It has to be examined if there are functional differences arising on account of merger. In this case, both the companies are in the same line of business and, therefore, even if they had merged, it will not impact the comparability. It has been argued that merger and amalgamation gives the benefit of synergies and operational efficiencies which increases the margin. It may however be pointed out that after merger it takes sometime for rationalization of workforce etc. and, therefore, effects of synergies etc. cannot be seen in the first year of merger or amalgamation. Facts of each case has to be examined carefully to find out whether merger has resulted into synergies and high margin. No such material has been produced before us. However as pointed out earlier there is also no material to show that this company had merged with Triton Corp. Ltd in the relevant year. We accordingly, reject the argument raised based on merger. We are therefore, unable to accept the order of CIT (A) excluding this comparable and therefore the order is set aside and this company is included as a comparable.

<u>24.6 Triton Corp. Ltd.</u>

This company which had been selected by the TPO as comparable has been excluded by CIT (A) on the ground that the assessee was engaged in high end service of ITES segment i.e. KPO. CIT (A) has also observed that the company was trading in IT peripherals and there were no segmental results available. Amalgamation/restructuring has also been cited as a reason for excluding the comparable. The learned CIT (DR) has placed on record the annual report of the company for the relevant year which shows call centre revenue of Rs. 47.50 Crore and revenue from support services at Rs. 5.54

Lakh. The income from trading in IT peripherals is Rs. 5.80 Crore. It is therefore, clear that the company is predominantly in the call centre business. The revenue from trading in IT peripherals is small at about 11% which in our view will not have much impact on the margin. It is also clear from the fact that the margin in case of Triton Corp. Ltd is 34.93% which is almost similar to the margin in case of Maple (E) Solutions Ltd. which is wholly in call centre business, which shows that trading in IT peripherals has not impacted the margin. No details of merger/amalgamation as mentioned by CIT (A) has been placed before us to show that it has impacted the comparability. We therefore do not agree with CIT (A) for excluding this comparable, Accordingly, we set aside the order of CIT (A) on this point and include this case in the list of comparables.

25 The assessee has also disputed the decision of CIT (A) to reject the claim of the assessee that no TP adjustment could be made as income of the assessee was exempt u/s 10A of the IT Act. The assessee has placed reliance on the decision of Bangalore Bench of Tribunal in case of Phillips Software Centre (P) Ltd. (Supra) in which it has been held that in case the income of the assessee was exempt transfer pricing provisions could not be applied. The learned CIT (DR) has, however, pointed that said decision of Tribunal has been stayed by Hon'ble High Court of Karnataka in ITA No. 49/2008. Therefore, the argument based on decision of Bangalore Bench of Tribunal can not be accepted. The argument of the learned AR is that the purpose of the transfer pricing provisions is to ensure that the companies do not transfer profit to low tax jurisdiction through related parties for reducing tax. In the present case, it has been pointed out that the income of the assessee was exempt and, therefore, there was no tax avoidance in transferring the profit to low tax jurisdiction. The argument of the learned AR is however not convincing. The law has to be applied as enacted. There is no provision in the transfer pricing regulations, that for applying the said provisions revenue has to prove tax avoidance. Once there is a international transaction, ALP has to be computed with respect to similar transaction with unrelated party as per

the method prescribed and the adjustment has to be made on the basis of ALP. The revenue is not further required to prove that there is tax avoidance. This view is also supported by the decision of Tribunal in case of 24/7 Customer . Com (P) Ltd. in ITA no 227/Mum/2010 and the decision of special bench of Tribunal in Aztech Software Technology Ltd. (107 ITD 141). We therefore see no merit in the arguments advanced by learned AR and accordingly confirm the order of CIT (A) on this point.

26 The assessee has also raised dispute regarding method of margin computation for the purpose of comparability. The assessee had computed the margin on operating cost which has also been followed by Assessing Officer/TPO. The assessee has, however pointed out that under the provision of Rule 10 B(1) (e) (i) the margin could be computed in relation to cost incurred, or sales affected, or asset employed. It has therefore been argued that the assessee has the option to compute the margin on the basis of return on asset employed (ROA) or on capital employed (ROCA). It has been pointed out that on this basis margin of the assessee is higher than mean margin of comparables selected by the TPO and also higher than the mean margin of the comparables selected by the assessee. This argument has not been accepted by CIT (A) aggrieved by which the assessee is in appeal before Tribunal.

26.1 The learned CIT(DR) has referred to the OECD transfer pricing provision para (2.97) as per which return on asset or capital employed can be an appropriate basis only in cases where assets are a better indicator of the value added by the tested party. The method is therefore, suited to certain manufacturing or other asset intensive activities. He also referred to United Nations Practical Manual on transfer pricing provision para (6.3.7.3) in which it has been mentioned that ROCA/ROA are typically used for manufacturing activities. He has also placed reliance on the decision of Delhi bench of Tribunal in case of Johnson Matthey India Pvt. Ltd. in ITA No.344/Del/2010 in which the Tribunal observed that PLI selected should be appropriate to the transactions under consideration. The assessee in that case was engaged in the manufacturing of Automobile exhaust catalyst and making import of raw materials from its AE. The Tribunal held that the return on capital employed was not an appropriate PLI in the case. The learned AR on the other hand submitted that even the call centre activity is not possible without sophisticated equipments such as computers and telecommunication systems. Therefore, it has been argued that like manufacturing organization, it also has to employ plant and machinery for carrying out services efficiently. Therefore, ROCA/ROA should be employed for the purpose of margin computation.

26.2 We have perused the records and considered the rival contentions carefully. The dispute is regarding method of computation of margin for the purpose of comparability. The OECD as well as United Nations practical manual provide that ROCA/ROA are suitable for manufacturing and other capital or asset intensive industries. The assessee is in the service sector which is not capital asset incentive. No doubt in every sector there is some use of equipments and other assets but the same cannot be said to be as capital intensive as in case of manufacturing concerns. Moreover, in case of service companies, main asset is employees which is not reflected in the balance sheet and, therefore, ROCA/ROA in our view will not be an appropriate method for the purpose of computation of margin. We accordingly, do not see any infirmity in the order of CIT (A) rejecting ROCA/ROA as PLI. The order of CIT (A) is accordingly held on this point.

27. Working capital adjustment and adjustment on account of other costs:

The assessee has requested for adjustment on account of working capital. It has been submitted that the assessee was receiving money in advance whereas in other cases receivable may be pending for a longtime which affect the sale price as well as the margin. It has therefore, been requested that working capital adjustment may be allowed. The learned CIT (DR) on the other hand submitted that in case working capital adjustment was considered appropriate, the adjustment may be made as per the OECD guidelines and not as per the method adopted by the assessee. In other words the adjustments should be made in relation to both the payables and receivables.

27.1 We have perused the records and considered matter carefully. Under the provisions of Rule 10B (2) (d) the comparability has to be judged with respect to various factors such as marketing conditions, geographical locations, cost of labour and capital in the market, Accounts receivable/payable affect the cost of working capital. The more accounts receivable would mean more capital blocked with debtors which may also mean higher sale prices. Therefore, in our view it will be appropriate to make working capital adjustment to improve the comparability. Further we agree with the submissions of learned CIT (DR) that while making the working capital adjustment guidelines framed by OECD must be followed. We therefore, do not uphold the order of CIT (A) rejecting the working capital adjustment. The issue therefore, is restored to the file of AO/TPO for working out the working capital adjustment as per OECD guidelines and after allowing the opportunity of hearing to the assessee.

27.2 As regards the adjustment claim by the assessee on account of linked cost and other cost incurred by the AE on behalf of the assessee, it has been argued by the learned AR that in case the AE had not incurred the cost, the assessee will have to incur it and the margin in that case may have been different. The learned CIT (DR), on the other hand submitted that the assessee was following "cost + 7% mark up". Therefore in case the cost had been incurred by the assessee, it would have charged the AE at "cost + 7% mark up' and it will have no impact on the margin. We have considered the matter carefully. We agree with the submission of learned CIT (DR) that adjustment on account of linked cost and other cost incurred by the AE on behalf of the assessee is not justified as margins are unaffected in case these costs were incurred by the assessee. The claim is rejected and order of CIT(A) on this point is upheld.

28 **<u>The benefit of +/ - 5% deviation in the computation of margin.</u>**

The assessee has requested for the benefit of +/ - 5% deviation in the margin under the proviso to section 92 C (2) This has not been allowed by AO/TPO, which has been upheld by CIT (A). It has been pointed out by the revenue that the proviso to section 92 C(2) was amended by the Finance Act 2009 to provide that the standard deviation could be allowed only when the sale price was within 5% of transfer price. It has also been clarified by the Finance Act 2012 that the said amendment would apply to all assessments/reassessments pending before Assessing Officer as on 1.10.2009. In this case proceedings were pending before AO/TPO as on 1.10.2009. Therefore, the assessee is not entitled to the benefit of **+/-** 5% as the ALP determined has exceeded the transfer price by more than 5%. We therefore see no infirmity in the order of CIT (A) in rejecting the claim and the same is therefore upheld.

29. In the result both the appeals are partly allowed.

Order pronounced in the open court on 26th April 2013

Sd/-	Sd/-
(VIVEK VARMA)	(RAJENDRA SINGH)
JUDICIAL MEMBER	ACCOUNTANT MEMBER

.

Mumbai, dated 26th April, 2013.

Sunil Kumar, Sr. P.S.