आयकर अपीलीय अधिकरण "के" न्यायपीठ मुंबई में।

IN THE INCOME TAX APPELLATE TRIBUNAL MUMBAI BENCH "K", MUMBAI

श्री बी. आर. बास्करन, लेखा सदस्य एवं
श्री अमित शुक्ला, न्यायिक सदस्य के समक्ष ।

BEFORE SHRI B R BASKARAN, ACCOUNTANT MEMBER AND SHRI AMIT SHUKLA, JUDICIAL MEMBER

ITA No. : 7099/Mum/2012

(Assessment year: 2008-09)

Capgemini India Private Limited, Plant 2, Block A, Godrej IT Park, Godrej & Boyce Compound, LBS Marg, Vikhroli (East), Mumbai -400 079 स्थयी लेखा सं.:PAN: **AAACZ 1421 B**	**Vs**	Income Tax Officer –Range 10(2), Room No. 432, Aayakar Bhavan, M K Road, Mumbai -400 020
अपीलार्थी (Appellant)		प्रत्यर्थी (Respondent)
Appellant by	:	Shri M P Lohia/ Shri Lokesh Gupta
Respondent by	:	Shri N K Chand

सुनवाई की तारीख /Date of Hearing : 11-09-2015

घोषणा की तारीख /Date of Pronouncement : 10-12-2015

आदेश
ORDER

अमित शुक्ला, न्या. स.:

PER AMIT SHUKLA, AM:

The aforesaid appeal has been filed by the assessee against final assessment order dated 30th October, 2012 passed in pursuance of direction given by the Dispute Resolution Panel (DRP) vide order dated 26.09.2012 under section 144C(1) for the assessment year 2008-09. The assessee has raised as much as 15 grounds of appeal challenging the various additions on account of transfer pricing adjustments of Rs.149,22,84,130/- and certain other disallowance and additions made under other corporate heads.

2. At the outset, the Ld. Counsel Shri M P Lohia submitted that, so far as ground no. 1 is concerned, the same is general in nature and ground no. 2, 3, 4 and 9 are not pressed accordingly, these grounds are treated as dismissed being not pressed. Effective

issue raised vide ground no. 5 to 8 is on account of transfer pricing adjustment Rs.149,22,84,130/-, which are being taken up first.

3. The brief facts *qua* the issue of transfer pricing adjustment are that assessee, Capgemini India Pvt. Ltd. is an Indian Company owned substantially by Capgemini US LLC, a company incorporated in USA. The assessee company is engaged in the business of providing software development & export services mainly to its Associated Enterprises (AEs) i.e. Capgemini Group Companies and third parties. The main service line of the assessee company includes, software technology services; IT outsourcing services; and customizes service software development services. During the relevant assessment year, the assessee has reported following international transactions with its AEs in the Form 3CEB:-

Nature of International Transaction	**Amount(Rs)**	**Method Applied**
Software Programming Services	*15,58,46,96,950*	*Transaction Net Margin Method ('TNMM')*
Payment for service' fees	*28,25,500*	*TNMM*
Licensing of intellectual Property	*87,83,495*	*Comparable Un-controlled Price Method ('CUP')*
Business development support costs	*27,39,300*	*TNMM*
Marketing support fee	*38,77,281*	*TNMM*
Allocation of various costs to CG India	*29,81,31,795*	*Not Applicable*
Reimbursement of expenses incurred by various Capgemini entities on behalf of Assessee	*17,43,96,814*	*Not Applicable*
Reimbursement of expenses incurred By Various Capgemini entities on behalf of Assessee	*2,18,95,43,752*	*Not Applicable*
Payment of training charges to Capgemini group entity	*1,85,38,031*	*TNMM*
Purchase of software and e-training licences from overseas third party vendor under globally negotiated contract	*15,76,246*	*TNMM*

For the purpose of establishing the arm's length price of the international transactions with its AEs, the assessee had undertaken a transfer pricing study after analyzing the FAR analysis vis a vis the selected comparables. For the software

program service, which is the subject matter of transfer pricing dispute here, the assessee had categorized itself as a 'risk mitigated captive delivery centre' and selected itself as a tested party. Considering the FAR analysis, transactional net margin method (TNMM) was determined as the most appropriate method (MAM) to benchmark the ALP. The assessee used operating profit to operating cost (OP/OC) as the Profit Level Indicator (PLI). The assessee's PLI for the relevant assessment year was worked out to **12.79%**. In the transfer pricing study report, the assessee selected 21 comparables having weighted average margin based on 3 years data at 13.78%. Later on, at the stage of the transfer pricing proceedings, the assessee on the basis of single year data of the same set of comparables, worked out the average arithmetic mean at 10.39%. From such a profit margin, the assessee sought marketing adjustment of 0.9% and risk adjustment of 6.50%. The comparables selected by the assessee along with their margin were as under:-

Sr. No.	**Name of Company**	**Operating profits on operating costs for FY 2007-08 (%)**
1	Akshay Software Technologies Limited	7.30%
2	Aztecsoft Limited	6.31%
3	Goldstone Technologies Limited	27.03%
4	Helios & Matheson Information Technology Limited	36.05%
5	Indium Software (India) Limited	-0.57%
6	Infosys Technologies Limited	NC
7	K P I T Cummins Infosystems Limited (Consolidated)	12.36%
8	Lanco Global Systems Limited	26.26%
9	Larsen & Toubro Infotech Limited	17.54%
10	Maars Software International Limited (Segmental)	7.93%
11	Meistar Information Technologies Limited	NC
12	Mindtree Limited (Segmental)	17.51%

13	Quintegra Solutions Limited	21.48%
14	R S Software (India) Limited	6.71%
15	S I P Technologies and Exports Limited	-33.20%
16	Satyam Computers Services Limited	NC
17	T V S Infotech Limited	NC
18	V J I L Consulting Limited	-6.06%
19	V M F Softech Limited	2.51%
20	Visualsoft Technologies Limited (Segmental)	NA
21	Zylog Systems Limited	17.00%
	Arithmetic mean	**10.39%**
	Less : Marketing Adjustment	0.90%
	Less: Risk Adjustment	5.50%
	Adjustment Arithmetic Mean	**2.99%**

However, the TPO rejected the assessee's transfer pricing documentation and the whole exercise of ALP determination by the assessee and carried out a fresh search of the comparables to determine the arm's length price (ALP) of the provision of software programming services to AE after detailed discussion. In the search process carried out by the TPO, he identified set off 23 comparables companies, the arithmetic mean margin of which were arrived at 24.99%. These comparables were confronted to the assessee to submit its objection. Finally after considering the assessee's objection/submission, the TPO finally selected set of 17 comparables which included 4 comparables chosen by the assessee company, the arithmetic mean of profit margin of these comparables were arrived at 24.97%. Thereafter, the TPO further allowed the benefit of working capital adjustment to the assessee and accordingly, the adjusted margins of the comparable companies were determined at **23.79%.** The final lists of TPO's comparables with the adjusted margins are as under:-

Sr. No.	**Name of Companies**	**OP/TC**
1	Acropetal Technologies Ltd (IT Segment)	27.09%
2	Ancient Technology (Holdings) Ltd (Earlier know as Flextronics Software Systems Ltd)	7.03%
3	Avani Cimcon Technologies Ltd.	25.31%
4	Bodhtree Consulting Ltd.	20.73%
5	E-Infochips Ltd.	29.50%
6	E-Zest Solutions Ltd.	29.59%

7	Infosys Technologies Ltd.	41.20%
8	KALS Information Systems Ltd (Application Software Segment)	40.39%
9	LGS Global Ltd. (Formerly Lanco Global Systems Ltd)	26.53%
10	Mindtree Ltd (Earlier Mindtree Consulting Ltd)	15.89%
11	Persistent Systems Ltd.	28.87%
12	Quintegra Solutions Ltd.	8.41%
13	Sasken Communication Technologies Ltd. (Software Services Segment)	13.15%
14	Thirdware Solutions Ltd. (Software Development Services Segment	21.61%
15	V G L Softech Ltd.	15.65%
16	Wipro Ltd (Wipro Technologies Segment)	30.56%
17	Goldstone Technologies Limited	22.96%
	Arithmetic mean	**23.97%**

Accordingly, he applied the PLI difference of 11% to arrive at a transfer pricing adjustment of Rs. 151,99,19,022/-.

4. From the stage of the DRP, one comparable namely, Acropetal Technologies Ltd. was excluded from the list of the final comparable on the ground that it fails the employee cost filter of 25% applied by the TPO himself. Now pursuant to the DRP's direction, the Arm's Length margin of the comparables was determined at 23.59% and accordingly, the transfer pricing adjustment on account of provision of software programming services was recomputed at Rs. 149,22,84,130/-.

5. Before us, the Ld. Counsel, Mr. M. P. Lohia submitted that, in the case of the assessee the Tribunal in the assessment year 2007-08 and 2009-10 had upheld the assessee's contention that the companies having turnover of less than Rs. 100 crores should be removed and if such an exercise is done, then the set of 16 comparables as confirmed by the DRP would get reduced to 7 comparable companies, out of which 2 companies are common, that is, they were selected by the assessee, hence there is no dispute. These 7 companies with the operating margin are as under:-

Sr. No.	**Name of the Company**	**Operating margins on costs**
1	Infosys Technologies Ltd	41.20%
2	Wipro Ltd (Wipro Technologies Segment)	30.56%
3	Ancient Technology (Holdings) Ltd (Earlier known as Flextronics Software Systems Ltd.)	7.03%
4	Mindtree Ltd. (Earlier Mindtree Consulting Ltd)	15.89%
5	Persistent Systems Ltd	28.87%
6	Sasken Communication Technologies Ltd (Software Services Segment)	13.15%
7	LGS Global Ltd (Formerly Lanco Global Systems Ltd)	26.53%
	Arithmetic Mean	**23.32%**

6. Mr. Lohia, submitted that if the lower turnover filter of Rs. 100 crores is accepted in view of Tribunal order, then, the assessee is only challenging the inclusion 2 comparables companies by the TPO, i.e., to exclude Infosys Technologies Ltd and Wipro Ltd. from comparable list and inclusion of one company in the list, i.e., Aztecsoft Ltd.

7. So far as the inclusion of Aztecsoft Limited by the assessee, he submitted that, the TPO has rejected the said company on the ground that the company fails export earning filter applied by him at 25%. However, the TPO failed to appreciate that the export turnover of this company was much higher than the threshold of 25% applied by him. On perusal of the annual report of the company, he pointed out that export earnings are 89%, thus, this company cannot be rejected at all even going by the filter applied by the TPO. Therefore, this company should be included in the final comparable list.

8. Regarding Infosys Technologies Ltd., Mr. Lohia submitted that the said company cannot be included as a comparable company for various reasons, some of which he pointed out that :-

Firstly, the functional profile of Infosys Technologies Ltd. suggests that, it is engaged into diversified activities and provides solutions to the entire software life cycle encompassing technical consulting, design, development, reengineering, maintenance, systems

integration, package evolution and implementation, distinguishing and infrastructure management services;

Secondly, no segmental results with regard to the software results and provision of software programming services are available in public domain, therefore, in absence of the same, the operating margin of the said company cannot be benched mark with the assessee. He also referred to various decisions of the Tribunal, wherein in absence of segmental information, such companies were not considered as comparable.

Thirdly, the company has significant R&D activity which has led to creation of significant intellectual property and has huge intangibles. These factors alone are sufficient to reject the company from comparability analysis, because all these factors are not there in the assessee company which is largely a captive service provider. This company has huge brand value, which has been valued at Rs. 31,863 crores. This factor has a significant impact on its pricing mechanism of its services and products and also on profit margins.

Lastly, Hon'ble Delhi High Court in the case of Agnity India Technologies Private Limited in ITA No. 1204 of 2011 held that Infosys Technologies Ltd. should be excluded as a comparable from the captive service providing company, because Infosys is full risk bearing entrepreneurial entity and cannot be compared with interest mitigated captive unit. Thus, the Infosys should be removed from being comparable company. Catena of various Tribunal decision were also filed wherein the Infosys have not been held to be comparable with the captive software service provider companies.

9. Regarding Wipro Ltd also, he submitted that the said company should not be considered as a comparable mainly on the ground that :

Firstly, the company is engaged in various services, other than software development services like BPO services, consumer products, software products etc.

Secondly, segmental information is also not available in the public domain and whatever information which was made available by the Department that does not match with the revenue details of each stream of the income as provided in the Product Description Schedule of the Annual Report of the company. Further, the annual report of the company shows that, 68% of the revenue comprises of sale of products. Thus, this company cannot be compared with the assessee company.

Lastly, this company like Infosys Technologies Ltd has significant intangibles and has more than 40 registered patents. It is operating as a full risk bearing entrepreneurial entity having huge intangibles and brand value as compared to assessee which is captive service provider.

Mr. Lohia also submitted a chart showing comparative analysis of Infosys and Wipro vis-a-vis the assessee giving the details of various parameters affecting the profit margin. These were summarized as under:-

All figures in rupees crores

Particulars	**Infosys**	**Wipro**	**CG India**
Operating Revenues	15,643	11,276	1,675
Operating Profit	4,442	2,504	190
Head count	91,187 Employees	61,815 Employees	16,400 Employees
Net block of assets	3,971	2,239	320.31
Expenditure on Research and Development	201	405	Nil
Nature of services	-Software Development services + Products -Technology Consulting	-Software Development services + Products* -Business Process	Software Development services

		Outsourcing -Technology Consulting *68% of the revenue of India Middle East & Asia Pacific IT Services & Products" comprises of sale of products (Page 880, 884 of the supplementary paperbook)	
Segmental Information	Separate segmental information not available in the public domain.	Separate segmental information not available in the public domain. However, the TPO obtained the same under section 133(6) of the Act	Not Applicable
Brand Value	31,863 (Page 877 of the supplementary paper book)	Not Available	Not Applicable
Profits attributable to brand	3,134 (As per handout)	Not Available	Not Applicable
Risk Profile	Operates as a full-fledged risk bearing entrepreneurial entity	Operates as a full-fledged risk bearing entrepreneurial entity	Operates as a risk mitigated captive service provider.

10. After explaining the above functional difference, Mr. Lohia submitted that in the assessment year 2007-08, the Tribunal has decided the exclusion of these two comparables against the assessee and has held that Infosys and Wipro can be compared with the assessee company for the purpose of bench marking the assessee's ALP margin. He submitted that, however, the earlier decision of the Tribunal should not be followed in this year for the various reasons which has been highlighted in the following manner :-

Sr. No.	**Tribunal's observation in AY 2007-08**		**CG India's observation on its relevance to AY 2008-09**
	Grounds on which the Tribunal has rejected the contentions of CG India	**Relevant extracts of Tribunal order**	
1	• Infosys and Wipro were selected as comparables by CG India in its own TP study • CG India has not raised any objections before the lower authorities (i.e. TPO/DRP)	"We also note that Infosys and Wipro were the comparables selected by the assessee itself on the basis of its own transfer pricing study. The assessee was fully aware of its work profile, while selecting Infosys and Wipro as comparables. The assessee raised no plea either before the TPO or DRP for excluding these comparables though it had added some more comparables" (Refer para 5.3.8)	• In this regard, it is submitted that Wipro Limited was not part of the comparables set considered by the Appellant in its transfer pricing report for AY 2008-09. • Further, while the Appellant has considered Infosys Technologies Limited as part of the comparables set in its transfer pricing report for assessment proceedings (refer para 5.3 on page 6 of the TPO order)
2	Infosys and Wipro were selected as comparables by CG India in its own TP study.	"The assessee, therefore, cannot be permitted to exclude Infosys and Wipro which were its own comparables. This issue is also supported by the decision of the Tribunal in the case of Kansai Nerolac Paint Ltd. (supra), which has been relied upon by the ld. CIT-DR in which it has been held that the assessee itself having selected the comparables, it cannot turnback and say that they are not comparables without giving any cogent and convincing reasons."	• As mentioned above, CG India had filed a submission with the ld. TPO for rejection in Infosys (which was part of the comparable set selected by CG India in the TP study) from the final set of comparables. • Moreover, it is observed that for AY 2008-09, the ld. TPO in para 5.8 of the order passed by him has rejected the transfer pricing documentation maintained by the assessee and brought out his own search for comparables in which he has taken Infosys as a comparable. Thus, it is submitted that Infosys can no longer be considered as a comparable selected by the assessee and has to be considered as the TPO's comparable. Thus, the observation of the Hon'ble

			members in AY 2007-08 that the Assessee has rejected its own comparables, shall not apply in the year under consideration. • Accordingly, we humbly request your Honour's to consider our plea against inclusion the said comparables.
3	The turnover of the company should not have an impact on its profitability	"The turnover and margin of Infosys and Wipro are higher than that of the assessee whereas the turnover of the other two comparables are lower. As we have observed earlier, the assessee is a part of a multinational group, well established in this field and has been rated as one of the top 50 companies in the world as per NASSCOM database. Therefore, there is no reason that its margin should be lower than any Indian company, how big it may be." (Refer Para 5.3.10)	• The Assessee whishes to state that Infosys and Wipro other than being giant companies have huge brand value and own significant intangibles as against the Appellant who is a routine software service provider owning no intangibles. • The same has been fortified by the Delhi High court in the case of Agnity India Technologies Private Limited (refer page 909 to 911) • Further, the Assessee also wishes to submit that Infosys and Wipro being risk bearing entities cannot be considered comparable to the Assessee which has the role of a captive delivery centre and hence does not bear any risks.

He, further submitted that, now there are umpteen number of decisions wherein it has been held that, Infosys and Wipro cannot be accepted as comparable companies with those of captive service provider company and finally, there is a decision of Delhi High Court in the case of Agnity India Technologies Private Limited (*supra*), wherein Delhi High Court has rejected the inclusion of Infosys with that of service provider unit. Thus, the Tribunal decision for AY 2007-08 should not be followed as far as inclusion of these two companies is concerned.

11. On the other hand, Ld. CIT DR, Mr. Chand, after explaining the entire facts submitted that, so far as inclusion of Aztecsoft Limited, there is no finding given by the DRP on assessee's objection and also there is no analysis of annual accounts by the authorities below, therefore, this matter should be restored back to the file/stage of DRP to analyse the contention of the assessee and in case it is found that its export turnover is more than 25%, then same can be included in the comparability list.

12. As regards the inclusion of Infosys Technologies Ltd. and Wipro Ltd., he submitted that, the assessee had included both these comparables in its TP Study report for benchmarking the margin in the earlier years and Infosys was included in this year also. Not only that the Tribunal in the immediately preceding assessment year i.e. AY 2007-08 has dealt this issue of exclusion of these two companies in detailed manner which is evident from the discussion appearing from Para 5.3.2 to para 5.3.8 of the order. There is no change either on the business function or any of the facts with these comparables vis-a-vis the assessee company in this year. Therefore, no different view should be taken in the impugned assessment order. As regards the decision of Delhi High Court in the case of Agnity (*supra*) he submitted that the said decision cannot be applied in the present case for rejecting the Infosys or Wipro, because the turnover of the Agnity company was Rs.16.09 crores which cannot be compared with the established player like Infosys. On the other hand, the assessee is huge Multinational corporation having turnover of more than Rs.1,600 crores and it is also leveraging and helping its AEs to build a huge brand. Thus, the assessee itself has a huge turnover and, therefore, it has rightly been included in the comparability list of TPO. He drew our attention to the various business descriptions of the comparables and that of the assessee. In AY 2009-10, these two companies were again included by the TPO, however, the same was not contested by the assessee, because even after taking their

margins, the assessee's margin fell within the range of ± 5%, hence, the said issue was considered as academic. Thus, he submitted that, in view of the precedence of the earlier years, these two comparable companies have rightly been included in comparable analysis and consistency should be followed.

13. We have carefully considered the rival contentions put forth by the parties, perused the relevant finding given in the impugned orders and material referred to before us. The dispute regarding transfer pricing adjustments is mainly on account of software programming services. The functions carried out by the assessee *qua* the said transactions are mainly software technology services; IT outsourcing services and customize software development services. All these services are provided to Associate Enterprises i.e. Capgemini Group companies and very minor portion of sales is also made to third parties. The assessee's PLI has been worked out by using operating profit/ operating cost which has been worked out at 12.79%. The TPO had rejected the entire transfer pricing documentation and comparability analysis carried on by the assessee and also the most of the comparables selected by the assessee. He had finally chosen 17 comparables which also happens to include 4 comparables selected by the assessee. The average arithmetic means of these comparables were worked out to 23.79% and accordingly, an adjustment on account of PLI difference of 11% was made which had led to transfer pricing adjustment of Rs. 152 crores. From the stage of the DRP, one comparable was removed and accordingly, the average arithmetic mean of 16 comparables was arrived at 23.59% and consequently adjustment has been reduced to approximately Rs. 149.25 crores.

15. Before us, one of the main contentions raised by the Ld. Counsel is that, in the earlier year (AY 2007-08) as well as in the subsequent year (AY 2009-10), the Tribunal has held that lower turnover filter for selecting the comparables companies should be taken pegged at Rs. 100 crores for the purpose of benchmarking

the international transaction of software programming services. If such a filter is applied then finally, there would be 7 comparables companies out of which only 2 have been contested for exclusion and one company, which was selected by the assessee and rejected by the TPO, has been contended for inclusion in the comparable list. If such an exercise would be carried out then average arithmetic mean would worked out to 16.19% and adjustment accordingly, would get reduced.

16. So far as capping of lower turnover filter of Rs. 100 crores, it is an admitted fact that in assessee's own case for the assessment years 2007-08 and 2009-10 the minimum turnover filter of Rs. 100 crores has been held by the Tribunal to be adopted for selecting the comparables. Such a cap of minimum turnover has been put for limited purpose to ensure that the selected comparables should be of certain critical mass for carrying out proper comparability analysis and there margins can be compared qualitatively. We agree with the proposition of the Tribunal laying down the minimum turnover filter of Rs. 100 crores in the case of the assessee, because the selection of the comparables has to be seen both on quantitative and qualitative criteria. A turnover of a company most likely has a bearing on its comparability as the size of a transaction in absolute value or in proportion to the activities of the companies might affect the relative competitive positions of the buyer and the seller. The size of the two companies and relative economies of scale under which they operate have a huge bearing while carrying out the comparability analysis of price or profit margin. It also affects the FAR analysis (ie., functions performed; assets employed; and risks assumed) to a great extent Thus, for initial screening of potential comparables quantitative filter of turnover should be applied so as to evaluate in qualitative terms the selected few in a given range. Thus, we hold that, in this year also there could not be any deviation for rejecting the comparables having turnover of less than Rs.100 crores. Accordingly, we direct

the TPO/AO to remove the comparables having turnover of Rs. 100 crores.

17. In this manner, we are only left with the exclusion of two comparables as contended by the assessee's counsel, i.e. Infosys Technologies Ltd. and Wipro Ltd. (segment). However, we shall deal first with the one comparable company which has been contended for inclusion by the assessee, namely Aztecsoft Limited which was a comparable selected by the assessee and rejected by the TPO. The TPO has rejected the said comparable on the ground that it fails on the export earning filter of 25%. The assessee's objection before the DRP has been that, it has export earnings at 89% and, therefore, it could not have been rejected on the basis of export earning filter of 25% applied by the TPO. However, the DRP has not given its finding on this objection/submission of the assessee. As pointed out by the Ld. Counsel, the annual report of the company which has been placed in the paper book at page 422, categorically mentions that during the financial year 2007-08, the company's revenue derived from the exports were at 89%. Otherwise there is no other point of dispute between the assessee and the revenue on this comparable. In view of this fact, the reason for rejecting the comparable by the TPO gets vitiated and has no legs to stand. Accordingly, we hold that such a comparable cannot be rejected on the export earning filter of 25% as admittedly this company has an export turnover of 89% and hence, this company should be included in the final list of comparables for benchmarking the assessee's profit margin.

18. As regards the inclusion of Infosys Technologies Ltd. and Wipro Ltd, it is an admitted fact that in assessment year 2007-08, the Tribunal has held that these two companies cannot be excluded as pleaded by the assessee. However, before us the Ld. Counsel has made his detailed submissions for distinguishing the relevant finding given by the Tribunal in the order and also the reasons as to why such a finding cannot having a binding

precedent in this year. The Ld. Counsel's submission in this regard has already been incorporated above. Apart from that, the Ld. Counsel has also relied upon catena of decisions wherein these two comparable companies have been held to be excluded from companies providing software programming services, especially in the cases of captive service provider. Some 20 decisions of Tribunal including that of the Delhi High Court in the case of Agnity India Technologies Private Limited (*supra*) have been filed and relied upon. The department's case on the inclusion of these two comparables are that, *firstly*, it is squarely covered by the decision of the Tribunal in the assessee's own case and there being no change in material facts and circumstances, no different view should be taken and *secondly*, the decision of Delhi High Court in Aginity's case would not be applicable on the facts of the present case. From the perusal of the Tribunal order for the assessment year 2007-08, we find major reason for rejecting the assessee's contention for exclusion of these two comparables was that, they were selected by the assessee itself in its own transfer pricing study report and hence, the assessee was fully aware of their work profile and its own profile while selecting these companies. Further, the assessee has raised no plea either before the TPO/DRP for excluding these comparables. As compared, in this year the assessee has not included Wipro as part of its TP study and comparables and *secondly*, in the case of Infosys Technologies Ltd., which though was chosen, but had immediately raised objection before the TPO for rejecting the said comparable based on detailed analysis of differences. In this year, the TPO has rejected the entire transfer pricing documentation maintained by the assessee and, therefore, now it cannot be held that assessee is precluded from raising the objection when TPO has selected these comparables for comparability analysis. Another main reason given by the Tribunal was that assessee had strongly contended that these companies have a very high turnover as compared to the

assessee, to which Tribunal held that high turnover cannot be the criteria for rejecting the said comparables.

19. As regards the first reason that assessee itself has included these comparables in the TP study report and, therefore, assessee is precluded from objecting the same, we have already observed above that these facts are not applicable in this year because, in case of Wipro, the assessee has not included this comparable in its TP Study report and in case of Infosys, assessee at very first instance has raised the objection for excluding the said comparable, more so, when assessee's entire TP documentation have been rejected by the TPO, which assessee had not raised the objection till the stage of Tribunal in the earlier year. In the case of TATA Solar Power Systems Pvt. Ltd., reported in (2014) 62 SOT 63(Mum), this Tribunal had laid down that under the transfer pricing mechanism, a comparability analysis has to be undertaken for comparing the controlled transactions with an uncontrolled transaction. This is achieved by identifying potential comparables having similar functions that can stand the test of FAR analysis. However, if the same has not been done properly then it has to stand the scrutiny of the taxing authorities. If, on a deep examination, it is found that the comparables chosen by the assessee do not stand the test of FAR analysis, requirement of the statutory provisions and correct selection of most appropriate methods, the same can be rejected. At the same time, if during the course of transfer pricing proceedings, if the assessee points out the cogent reasons and gives proper analysis as to why the comparables chosen by it were not correct, it cannot be said that the assessee is out rightly precluded from raising such objections. The ultimate aim of the transfer pricing provisions is to determine the appropriate ALP, which can be done only by bench marking with the proper comparables based on FAR analysis and under the prescribed methods. If in the course of the proceedings, it is found that certain comparables do not stand the test of functional

analysis or for some other reasons, then the same should be excluded and we do not find any reason in the contention raised by the ld. DR that they should be included simply because the assessee had included the same. The initial onus of duty is cast upon the assessee to carry out the selection of proper comparables based on FAR analysis and by adopting suitable transfer pricing method and then analyse its transaction to show the correct arm's length result. Thereafter, it is axiomatic that the taxing authorities / TPO, should scrutinize the assessee's report on arm's length result and the entire process of arriving at the ALP, whether they are based on transfer pricing principles and statutory provisions or not. If he himself founds some irregularity or mistake in any of the process or the steps undertaken, then he is bound to correct in accordance with the settled principles and law. If the assessee points out some mistake or any irregularity in the arm's length result, then it is incumbent upon the TPO to examine and consider the same and it the assessee's contentions are found to be correct or tenable, then he has to accept the same. There cannot be estoppel against correct procedure of law and principles solely on account of acquiescence or mistake of the assessee. The TPO is required under law to analyze every comparables and then only determine the correct ALP based on proper comparability analysis. Hence, we hold that assessee is not precluded from raising objections for exclusion of these two comparables on the ground that they were in the earlier year or in this year have been chosen by the assessee in TP study, more so in the circumstances when the assessee's TP study documentation has been rejected and assessee has duly objected at the initial stage.

20. Now, coming to the second reason of the Tribunal that the higher turnover will not make a difference and cannot be the criteria for rejecting the comparable on a higher turnover basis. So far as in principle this reason is concerned we do not wish to take a contrary stand and we agree with the observation of the Tribunal,

however, the high turnover filter alone is not the guiding factor in most of the cases, the qualitative criteria approach for analyzing the comparables has to be seen. Such a qualitative approach has to be examined on FAR analysis. A high turnover company may be functional comparable but at times they differ significantly on assets employed like capital, human resources, marketing intangibles, intellectual property rights, brand names, R&D activities etc. and risks undertaken or assumed because the reward is intimately linked with risk undertaken, all of which have a significant impact on the pricing of the product and services, market penetrations and consequently on the profit margins. While evaluating the qualitative criteria, various factors like intellectual properties associated with the transaction like valuation of brand name, trademark etc. has to be factored and taken into consideration while carrying out the comparability analysis. Even if two companies are chosen based on similar functions having huge variation in turnover, a qualitative analysis has to be carried out for comparability analysis and see the material factors for choosing it as a comparable for benchmarking the controlled transactions. Thus, we are of the opinion that qualitative analysis assumes great significance for selecting or rejecting the comparables. While dealing with the arguments of the ld. Counsel in the foregoing paragraphs, we have already incorporated the analysis of Infosys Technologies Ltd. and Wipro vis-a-vis the assessee giving quantitative and qualitative parameters of difference. The main distinguishing features which can be gauged are *firstly*, the presence of huge intangibles and brand value in the case of Wipro and Infosys whereas in the case of the assessee which is a captive service provider, there are no such intangibles; s*econdly*, both the comparables are full-fledged risk bearing entrepreneurial entity whereas, the assessee operates as a risk mitigated service provider; *thirdly*, both these companies also have significant R&D activities which has led to creation of significant intellectual property and branded products. These factors go to affect significantly the

pricing mechanism and the profit margins. Such a huge risk bearing entrepreneurial entity cannot be compared with a risk mitigated captive service provider. Further, the other qualitative differences have already been discussed and highlighted while dealing with the contentions raised by the assessee. On such a qualitative level, these two companies cannot be held to be good comparable for benchmarking the assessee's profit margin. Though we are not applying any upper turnover filter but on qualitative level, we are of the opinion that these companies having huge presence of brand value and intangible R&D activities etc which cannot be chosen for comparability analysis with a captive service provider company like the assessee. Thus, on these reasons, we are deviating from the conclusion reached by the Tribunal, because the material facts as highlighted by the Tribunal is absent in the present year. In view of our above discussion, we hold that, these two companies are to be removed from the final list of comparables. Thus, in all, there would be 6 comparable companies in the final stage of comparables which are as under:-

Sr. No.	**Name of the company**	**Operating margins on costs**
1	Aztecsoft Limited	5.66%
2	Aricent Technology (Holdings) Ltd. (Earlier know as Flextronics Software Systems Ltd)	7.03%
3	Mindtree Ltd. (Earlier Mindtree Consulting Ltd.)	15.89%
4	Persistent Systems Ltd	28.87%
5	Sasken Communication Technologies Ltd (Software Services Segment)	13.15%
6	LGS Global Ltd. (Formerly Lanco Global Systems Ltd)	26.53%
	Arithmetic Mean	**16.19%**

The adjustment will be thus made from the margins of the aforesaid comparables. Accordingly, we direct the TPO / AO to make the transfer pricing adjustments based on average arithmetical mean of profit margin of aforesaid 6 comparables. Thus, the grounds raised by the assessee on transfer pricing adjustments are treated as partly allowed.

21. Now we will take-up other domestic corporate tax grounds. In Ground no. 10, assessee has raised the following ground :-

> *" DRP has erred in reducing the losses of Chennai unit at Rs. 11,35,20,100/- and Kolkata unit at Rs. 84,80,844/-, aggregating to Rs. 12,20,00,944/- from the deduction allowable to the Appellant under Section 10A of the Act.*

22. Facts in brief on the impugned issue as submitted by the assessee are that, during the year under consideration, Capgemini India Private Limited owned and operated nine software units, namely, Mumbai I (non 10A unit), Mumbai II (section 10A unit-5th year of claim), Mumbai III (section 10A unit-4th year of claim), Bangalore unit (section 10A-4th year of claim), Kolkata unit (section 10A unit-3rd year of claim), Pune I (Non 10A unit), Pune 2 (section 10A unit-7th year of claim), Hyderabad (section 10A unit-5th year of claim), Chennai (section 10A unit-8th year of claim). The Assessee claimed Section 10A deduction in respect of Mumbai II, Mumbai III, Bangalore unit, Pune 2 and Hyderabad. No deduction under section 10A has been claimed in respect of Mumbai I and Pune I unit as they are not eligible for deduction u/s.10A and in respect of Kolkata unit and Chennai Unit as these units have incurred losses during the year under consideration. The Assessee has set off the loss of Kolkata unit of Rs. 84,80,844/- and Chennai Unit of Rs. 113,520,100 against its business income for the year under consideration i.e. against the taxable profits of units which are not eligible for deduction under section 10A. Section 10A provides for deduction of profits derived by the eligible undertaking and no longer provides for exemption.

23. It has been contended before us that, as per the provisions of section 10A deduction is allowed in respect of profits and gains derived by an undertaking from the export of articles or things or computer software for a period of 10 consecutive assessment years beginning with the year in which the undertaking begins to manufacture or produce such article or things or computer

software while computing the total income. Further, it was clarified by the amended provisions of section 10A w.e.f. 1.4.2001 that the section 10A provides for a "deduction" of profits derived by the eligible undertaking and no longer provide for an "exemption". It was also clarified by the CBDT circular no.794 dated 9.8.2000 that the deduction under section 10A is in respect of a particular undertaking and not from the total income. There is no provision in section 10A for setting off the loss of other eligible undertakings before arriving at the deduction under section 10A. Prior to Assessment Year 2001-2002, when section 10A was an exemption provision, section 10A(6) provided restriction on set-off and carry forward of business loss and unabsorbed depreciation. However, subsequently, section 10A(6) was amended by Finance Act, 2003, with effect from Assessment Year 2001-2002 and such restriction was withdrawn, which amendment was consistent with the new scheme of section 10A which is a deduction provision and not an exemption provision for Assessment Year 2001-2002. In view of the above amendment, losses of section 10A units have to be adjusted against taxable profits of other units after deduction under section 10A has been allowed in respect of each of the profitable unit under section 10A.

24 It has been admitted by both the parties, that this issue is covered by the Tribunal in the assessee's own case for the assessment year 2006-07 which has been affirmed by the Hon'ble High Court in ITA No. 2501 of 2011 and ITAT order for AY 2009-10. Ld. DR also accepted that this issue is covered in favour of the assessee by the order of the Tribunal order. The relevant observation of the Tribunal in the assessment year 2006-07 reads as under:-

> *"We have perused the records and considered the rival contentions carefully. The dispute is regarding set off of loss of a s. 10A unit against the taxable profit of other units. The assessee had four 10A units in respect of which deduction under s. 10A was allowable and one non-s.10A unit wax exempt, loss from s. 10A unit has to*

be ignored or alternatively the loss has to be adjusted against the profit of another s. 10A unit before allowing deduction under s. 10A. We have gone through the provisions of s. 10A and find that as per the provisions in force prior to asst. yr. 2001-02, the profit and gain from the eligible undertaking was not to be included in the total income which meant that the income from the eligible unit was exempt from tax. However, provisions were amended with effect from asst. yr. 2001-02 and as per the amended provisions, the profit and gain derived by an eligible undertaking are required to be deducted from the total income. Thus asst. yr. 2001-02, s. 10A is no longer an exemption provisions and it allows only deduction from total income. The deduction is to be allowed in respect of each eligible undertaking separately which has also been clarified by the CBDT. We also note that prior to asst. yr. 2001-02 when s. 10A was an exemption provision, s. 10(6) provided restriction on set off and carried forward of business loss and unabsorbed depreciation. However, subsequently, s. 10(6) was amended by Finance Act 2003 with effect from asst. yr. 2001-02 and such restriction was withdrawn which was consistent with the new scheme of s. 10A which is a deduction provision and not exemption provision from asst. yr. 2001-02. Therefore the loss from s. 10A unit has to be adjusted against taxable profits of other units after deduction under s. 10A has been allowed in respect of each eligible unit. Same view has been taken by the Hon'ble High Court of Bombay in case of Hindustan Unilever Ltd. vs. Dy. CIT (supra) in which it has held that deduction has to be allowed in respect of three eligible units and loss of the fourth s. 10A unit has to be set off against the normal business income. The Tribunal in case of Honeywell International (India) (P) ltd. vs Dy. CIT (supra) has also followed the same view. Therefore respectfully following the above judgments, the order of the Addl. CIT cannot be sustained. We accordingly set aside the order of the Addl. CIT and allow the claim of the assessee".

25. This finding has been affirmed by the Hon'ble Bombay High Court judgment and order dated 30th April, 2014. Wherein, the High Court has held that, this issue is covered by the decision of Hon'ble Bombay High Court in the case of Hindustan Unilever Ltd. wherein it was held as under :-

" ... the first ground relates to the adjustment contemplated by section 10A of the Income Tax Acts 1961. The Tribunal has

directed that loss of one unit can he adjusted against the profit of another unit but after allowance of deduction under section 10A of such profitable units. The loss of one unit under section 10A of the Act shall be adjusted against the income liable for deduction under the same but in relation to the income from other unit. As far as that aspect is concerned the counsel agree that the same is answered in favour of the assessee and against the revenue. This controversy has been dealt with by a Division Bench of this Court in the case of Hindustan Unilever Ltd vs Deputy Commissioner of Income Tax & anr., reported in [2010] 325 ITR 102. The parties agree that the discussion of the Division Bench and particularly at paragraph 17 of the judgment covers the point".

26. Accordingly, respectfully following the decision of the Hon'ble High Court, the ground no. 10 as raised by the assessee is treated as allowed.

27. In ground no. 11, the assessee has challenged that DRP has erred in reducing the telecommunication expenditure aggregating to Rs. 12,01,53,644/- from the export turnover of the eligible units, the while computing deduction under section 10A of the Act.

28. The assessee is engaged in development and export of computer software and not in providing technical services outside India. The assessee has not separately charged its clients telecommunication expenses incurred by it. Therefore, such expenses are not included in the export turnover of the eligible units. As per the definition given in clause (iv) of Explanation 2 to section 10A, export turnover does not include freight, telecommunication charges or insurance attributable to the delivery of the articles or things or computer software outside India. Thus, it was submitted that the expenses sought to be covered above are only incidental expenses which are charged in the invoice by CG India to its clients. This is also substantiated by the fact that the definition states that the above expenses are not to be included and not that the export turnover should be reduced by such expenses. Accordingly, it is submitted that only expenses those are separately charged to the client in the invoice, should be

reduced in computing the export turnover if such expenses are already included in the turnover. In the present case, CG India's turnover does not include any such expenses. Hence, it is submitted that the same should not be reduced from the export turnover. Such a legal arguments have been upheld by the Bombay High Court in assessee's case for AY 2006-07 which for the sake of ready reference is reproduced herein below :-

> *"These expenses have been incurred for the purposes of the business of software development at the software units in India. It is that finding which the Assessing Officer was unable to controvert or unable to bring any contrary material to disprove the same. It is in that light that the Tribunal found that the Assessing Officer could not have insisted on the deduction. It is that exercise undertaken by the Assessing Officer which has not been upheld but rather disapproved by the Tribunal. This is a finding purely on the facts and pertaining to the business of the assessee. The facts pertaining to the assessee's business of software development, the charges and which are claimed to have incurred, are in relation to the business of software development within India. They could not be said to be costs deductible from export turnover for the purposes of Section 10A of the Act. In such circumstances, we are of the opinion that any wider controversy or larger question does not require any answer. We can leave that aspect open for the decision in an appropriate case. In the facts and circumstances of the present case and in relation to the business of the assessee before us, it is not necessary to go into the other contentions raised before us by the revenue ".*

This order of the High Court has been followed by the Tribunal in ITA No. 540/Mum/2014 for AY 2009-10 also. Thus, respectfully following the same, ground no. 11 is treated as allowed.

29. Ground no.12 is general in nature and no adjudication is called for accordingly dismissed as it becomes infructuous.

30. In ground no. 13, the assessee has challenged that, the DRP has erred in reducing the expenditure incurred in foreign currency aggregating to Rs. 94,54,13,470/- from the export turnover of the units eligible, while computing deduction under Section 10A of the Act. The facts in impugned issue are that, assessee is engaged in development and export of computer software and not in providing technical services outside India. Assessee submitted copies of Audit Report under section 56F in respect of each of the eligible

unit, wherein the Chartered Accountants had certified that CG India's eligible unit was engaged in the development and export of computer software. Before the AO the assessee submitted that wordings "attributable to the delivery of computer software outside India" are not present in the second limb of the definition regarding the expenses incurred in foreign exchange. Therefore, CG India submitted that the second exclusion in respect of expenses incurred in foreign exchange would not be applicable in respect of export turnover from delivery of computer software outside India. Since, the assessee is engaged in development and export of computer software and not in provision of technical services outside India, the second exclusion would not be applicable in CG India's facts at all.

31. Ld. Counsel submitted that this issue is covered by the decision of Tribunal in assessee's own case for the assessment year 2009-10 wherein it is held it is similar to issue of telecommunication expenses and accordingly, decision of Bombay High Court will be followed. Thus, respectfully following the order of the Hon'ble Bombay High Court and the ITAT decision for AY 2009-10 we set aside the orders of the revenue authorities and direct the AO to delete the disallowance and compute the exemption as per law.

32. In ground no. 14, assessee has challenged the disallowance of interest amounting to Rs. 1,86,089/- and expenses amounting to Rs. 8,62,370/- u/s 14A of the Act, as expenditure incurred for earning dividend income.

33. The relevant facts are that, the assessee has earned dividend income of Rs. 2,83,000/- from units of mutual fund, which were claimed as exempt. The assessee's case had been that, it had made investment out of its surplus funds which was at Rs. 244 crores in the beginning of the year against which it has invested only Rs. 17 crores, therefore, no interest expenses can be attributed to the

earning of exempt income. For the purpose of indirect expenses, the assessee submitted that has calculated the time taken by one of its employee who was an Accountant Manager and attributed the same for managing the investments, accordingly, the assessee offered sum of Rs. 50,000/- as disallowance u/s 14A.

34. Before us, the Ld. Counsel submitted that *Firstly,* disallowance u/s 14A will not be applicable on shares held for strategic investments or investment made in subsidiaries, as the assessee has made the investment in shares of subsidiaries; *Secondly*, only investment from which exempt income has been earned should be considered in computing the disallowance; and *Lastly*, the Ld. Counsel submitted that the disallowances of expenses should not exceed the exempt income and, therefore, the same should be restricted to the extent of dividend income only.

35. On the other hand, Ld. DR submitted that, even if the investment has been made in subsidiary companies then also it cannot be held that no disallowance u/s 14A can be made because, ultimately such investments would yield exempt income and further the disallowance cannot be restricted to exempt income only, because there can be expenditure directly attributable to investments which may not yield exempt income immediately but in future. The concept of income includes loss has to brought in such circumstances.

36. After considering the rival contentions and on perusal of the impugned order, we find that so far as disallowance of interest of Rs. 1,86,089/- is concerned, the same cannot be made as admittedly, the assessee has huge surplus funds which are interest free and, therefore, no disallowance of interest should be made. As regards the indirect expenses, the same has been disallowed under Rule 8D by the AO in a mechanical way, without satisfying himself after looking into the nature of accounts of the assessee and the nature of expenses debited in the books of accounts as per mandatory requirement of section 14A(2). If

assessee's investments are only in subsidiary companies and mutual funds, then it cannot be held that assessee might have incurred huge expenditure. The assessee had *suo moto* offered a sum of Rs. 50,000/- for disallowance, which in our opinion, is sufficient for attributing the indirect expenses for earning the exempt income of Rs. 2,83,000/-. Accordingly, the addition made by the AO and confirmed by DRP stands deleted. Accordingly, ground no. 14 raised by the assessee is allowed.

37. In ground no. 15, the assessee has challenged that AO has not granting of foreign tax credit amounting to Rs. 4,04,789/-.

38. We direct the AO to examine the same and grant credit for the said foreign tax credit paid, after verification.

39. In the result, appeal of the assessee stands partly allowed.

Order pronounced in the open court on 10th December, 2015

Sd/-	**Sd/-**
(बी. आर. बास्करन)	(अमित शुक्ला)
लेखा सदस्य	न्यायिक सदस्य
(B R BASKARAN)	**(AMIT SHUKLA)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Mumbai, Date: 10th December, 2015

प्रति/Copy to:-

1) अपीलार्थी /The Appellant.
2) प्रत्यर्थी /The Respondent.
3) The CIT/DRP -11, Mumbai.
4) The CIT/DIT– Concerned , Mumbai.
5) विभागीय प्रतिनिधि "के", आयकर अपीलीय अधिकरण, मुंबई/
   The D.R. "K" Bench, Mumbai.
6) गार्ड फाईल \
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Dy./Asstt. Registrar
I.T.A.T., Mumbai

*चव्हान व.नि.स
*Chavan, Sr.PS