

आयकर अपीलीय अधिकरण "बी" न्यायपीठ पुणे में ।  
IN THE INCOME TAX APPELLATE TRIBUNAL "B" BENCH, PUNE

श्री डी. करुणाकरा राव, लेखा सदस्य, एवं श्री विकास अवस्थी, न्यायिक सदस्य के समक्ष ।  
BEFORE SHRI D. KARUNAKARA RAO, AM AND SHRI VIKAS AWASTHY, JM

आयकर अपील सं. / ITA No.316/PUN/2015

निर्धारण वर्ष / Assessment Year : 2010-11

Visteon Engineering Center (India) Private Limited,  
Office No. 502, 5<sup>th</sup> Floor, ICC-Devi Gaurav Tech Park,  
S. No. 191 (Part) and 192 (Part),  
Sub Plot No. B, Mumbai-Pune Road,  
Pimpri Waghere, Pune-411018

PAN : AACCT2585N

.....अपीलार्थी / Appellant

**बनाम / V/s.**

The Assistant Commissioner of Income Tax,  
Circle – 13, Pune

.....प्रत्यर्थी / Respondent

आयकर अपील सं. / ITA No.540/PUN/2015

निर्धारण वर्ष / Assessment Year : 2010-11

The Assistant Commissioner of Income Tax,  
Circle – 13, Pune

.....अपीलार्थी / Appellant

**बनाम / V/s.**

Visteon Engineering Center (India) Private Limited,  
A-205/206, "A" Wing, 2<sup>nd</sup> Floor,  
ICC Trade Tower, 403 A,  
Senapati Bapat Road,  
Pune – 411016

PAN : AACCT2585N

.....प्रत्यर्थी / Respondent

Assessee by : Shri Ketan Ved & Ms. Nupoor Shah  
Revenue by : Smt. Nirupama Kotru

सुनवाई की तारीख / Date of Hearing : 01-03-2018

घोषणा की तारीख / Date of Pronouncement : 28-05-2018

**आदेश / ORDER****PER VIKAS AWASTHY, JM :**

This cross appeals by the assessee and the Revenue are directed against the assessment order dated 25-02-2015 passed u/s. 143(3) r.w.s. 144C(13) of the Income Tax Act, 1961 (hereinafter referred to as “the Act”) for the assessment year 2010-11.

2. The brief facts of the case as emanating from records are: The assessee company is engaged in the business of designing and developing products in CAD/CAM of auto parts. The assessee is a registered under the STPI and is also registered as 100% export oriented unit. The assessee is also providing customer support services and techno marketing services to the group companies. The assessee is providing IT based engineering design services to its Associated Enterprises (AEs) alone. Thus, the assessee can be characterized as captive service provider. The international transactions undertaken by the assessee during the Financial Year 2009-10 are as under :

Sr. No.	Name of the AE	Description	Amount in Rs.	Method used
1	Visteon Asia Pacific Inc. Visteon Corporation. Visteon Autopal S.R.O. Visteon Japan Ltd. Visteon Asia Pacific Inc. Visteon Engg. Services Ltd. Visteon Deutschland GmbH. Visteon Sistemas Interiors Espana S.L. Dngfeng Visteon Automotive Trim Systems Co. Ltd.	Provision of IT based Engineering Services	16,83,88,421	TNMM
2	Visteon Autopal Visteon Corporation	Receipt of IT Support services	1,35,44,677	TNMM
3	Visteon Corporation	Reimbursement of expenses (Received)	23,15,466	
4	Visteon Asia Pacific Inc. Visteon Corporation	Reimbursement of expenses (Paid)	29,95,007	
		Total	18,72,43,571	

2.1 The assessee selected Transactional Net Margin Method (TNMM) as the most appropriate method to benchmark its international transactions. The assessee selected 7 companies as comparables with average PLI (Operating Profit/Operating Cost) of 8.70% based on data of 3 years as against PLI of assessee at 11.23%. The Transfer Pricing Officer (TPO) accepted TNMM as the most appropriate method but rejected use of multiple year data for arriving at PLI. Further, the TPO rejected some of the companies selected by the assessee as comparables and introduced some new companies in the list of comparables. The TPO applied export filter of 75% while selecting the comparables. As a result some of the companies selected by the assessee were rejected by the TPO. The assessee provided for adjustment on account of unutilized capacity while calculating operating margin, the TPO rejected the same. The assessee further claimed the benefit of risk adjustment. The TPO rejected assessee's claim of risk adjustment as well. The TPO finally made adjustment of Rs.6,61,77,304/- to the international transactions of design engineering services. Based on the adjustment proposed by the TPO the Assessing Officer made draft assessment order.

Aggrieved against the proposed adjustment in the international transactions, the assessee filed objections before the Dispute Resolution Panel (DRP). The DRP vide directions dated 26-12-2014 upheld the order of TPO. However, the DRP directed the TPO to re-compute working capital adjustment in line with OECD guidelines. Thereafter, vide assessment order dated 25-02-2015, the Assessing Officer pursuant to the directions of DRP computed transfer pricing adjustment as Rs.4,84,21,100/-. Against the assessment order both, the assessee and the Revenue are in appeal.

3. The grounds raised by the assessee in appeal assailing the assessment order are as under :

**1. “Transfer Pricing adjustment**

*The learned ACIT pursuant to the directions of the learned DRP erred in law and on the facts and in circumstances of the case in making an adjustment amounting to Rs.4,84,21,100 to the value of international transactions entered into by the Appellant with its Associated Enterprise in respect of provision of Engineering Design Services.*

**2. Erroneous non-granting of adjustment for unutilized capacity while calculating operating margin of the Appellant**

*The learned ACIT pursuant to the directions of the learned DRP erred in law and on the facts and in circumstances of the case in not granting adjustment for unutilized capacity while calculating operating margin of the Appellant in respect of provision of Engineering Design Services to its Associated Enterprises.*

**3. Erroneous computation of adjustment in respect of provision of engineering design services to Associated Enterprises**

*The learned ACIT pursuant to the directions of the learned DRP erred in law and on the facts and in circumstances of the case in not computing the transfer pricing adjustment on international transactions pertaining to provision of engineering design services to its Associated Enterprises only.*

**4. Search Matrix and FAR Analysis for fresh search carried out by learned TPO not shared**

*The learned ACIT pursuant to the directions of the learned DRP erred in law and on the facts and in circumstances of the case in not sharing the search matrix and FAR analysis for fresh search carried out by learned Transfer Pricing Officer ("TPO").*

**5. Erroneous selection of comparable company**

*The learned ACIT pursuant to the directions of learned DRP has erred in law and on the facts and in circumstances of the case in selecting the following company as a comparable company:*

- Coral Hub Limited

**6. Erroneous application of export filter in selection of comparable companies**

*The learned ACIT pursuant to the directions of learned DRP has erred in law and on the facts and in circumstances of the case in erroneous application of export filter in selection of comparable companies.*

**7. Erroneous rejection of comparable companies**

*The learned ACIT pursuant to the directions of learned DRP has erred in law and on the facts and in circumstances of the case in rejecting the following companies as comparable companies:*

- Chakkilam Infotech Limited
- ICRA Techno Analytics Limited

- ISmart International Limited
- Valuemart Info Technologies Limited.

**8. Erroneous computation of operating margins of comparable companies**

*The learned ACIT pursuant to the directions of learned DRP has erred in considering the unadjusted operating margin of Acropetal Technologies Limited at 22.27% instead of correct unadjusted operating margin of 14.47% and correct working capital adjusted operating margin of 10.12%.*

**9. Benefit of the risk adjustment**

*The learned ACIT pursuant to the directions of learned DRP has erred in law and on the facts and in circumstances of the case in not granting the risk adjustment.*

**10. Benefit of the variation / reduction of 5 percent from the arithmetic mean**

*The learned ACIT pursuant to the directions of learned DRP has erred in law and on the facts and in circumstances of the case in not granting the benefit of +/- 5 percent as per proviso to section 92C (2) of the Act.*

**11. Initiation of penalty proceedings**

*The learned ACIT erred on the facts and in law in initiating penalty proceedings section 271 (1) (c) of the Act.*

**12. Levy of interest obligation on account of transfer pricing adjustment**

*The learned ACIT has erred on the facts and in law while levying interest under section 234B of the Act, on account of the unanticipated transfer pricing adjustments.*

13. *Each one of the above grounds of appeal is without prejudice to the other.*

14. *The Appellant reserves the right to amend, alter or add to the grounds of appeal.”*

4. Shri Ketan Ved appearing on behalf of the assessee submitted that ground Nos. 1 and 4 are general in nature. In respect of ground No. 2 the assessee has assailed non-granting of adjustment for capacity utilization while computing operating margin. The assessee had claimed adjustment for capacity utilization in the light of fact that the assessee's AEs i.e. Visteon Corporation (the parent company) and some of the subsidiaries in the US had filed bankruptcy petition which had adverse impact on revenue on the assessee company. The assessee was to recover Rs.115 lakhs from

Visteon Corporation (parent company) up to the date of declaration of bankruptcy. The assessee had fully provided for Rs.115 crores. The ld. AR pointed that after the filing of bankruptcy petition by the parent company, the revenue of assessee company had substantially decreased. There was decrease in the revenue from USA to the extent of 47% and from the Europe to the extent of 54%. Consequent to sharp fall in the business from Rs.34.84 crores in the previous year to Rs.21.04 crores the assessee suffered on account of decrease in sales as well as higher fixed cost of overheads. The assessee could not reduce the fixed overheads like depreciation, rent of property, reduction in head count i.e. salary, etc. in tandem with the reduction in business. Consequently, the profitability of the assessee company was also adversely affected. The DRP without appreciating the facts on record rejected the contentions of the assessee out rightly. The ld. AR submitted that capacity utilization adjustment can be granted in two ways. Firstly, a part of the cost which is excessive due to fact that the staff/assets employed by the assessee can be identified as an extraordinary/non-recurring cost and the same can be excluded while computing the operating cost of the assessee for the purposes of calculating its margin. In support of this methodology, the assessee placed reliance on the following decisions :

- i. Ariston Thermo India Limited Vs. DCIT in ITA No. 1455/PN/2010 (Pune-Trib.);
- ii. Egain Communication P. Limited Vs. ITO, 118 TTJ 354 (Pune-Trib.);
- iii. Amdocs Business Services Pvt. Ltd. Vs. DCIT in ITA No. 1412/PN/2011 (Pune-Trib.);
- iv. ACIT Vs. Fiat India Private Limited in ITA No. 1848/Mum/2009 (Mum.-Trib.);
- v. Transwitch India Private Limited Vs. DCIT in ITA No. 6083/Del/2010 (Del.-Trib.);
- vi. Global Vantedge (P) Ltd. Vs. DCIT, 37 SOT 1 (Delhi).

4.1 The ld. AR contended that the alternate method for providing risk adjustment is through the margins of comparable companies. To support this method, the ld. AR placed reliance on the following decisions :

- i. Tasty Bite Eatables Ltd. Vs. DCIT in ITA No. 1682/PN/2011 (Pune-Trib.);
- ii. DCIT Vs. Claas India Pvt. Ltd. in ITA No. 1783/Del/2011 (Delhi-Trib.);
- iii. Affinity Express India Pvt. Ltd. Vs. DCIT in ITA No. 106/PN/2012 (Pune-Trib.).

4.2 The ld. AR submitted that as far as grant of capacity utilization adjustment is concerned the Tribunal has allowed the same in various cases. To buttress his submissions, the ld. AR placed reliance on the following decisions :

- i. Amdocs Business Services Pvt. Ltd. Vs. DCIT in ITA No. 1412/PN/2011 (Pune-Trib.);
- ii. Affinity Express India Pvt. Ltd. Vs. DCIT in ITA No. 106/PN/2012 (Pune-Trib.).
- iii. Genisys Integrating Systems (India) Pvt. Ltd. Vs. DCIT in ITA No. 1231/Bang/2010 (Bang.-Trib.);

4.3 In respect of ground No. 3 relating to erroneous computation of adjustment in respect of Provision of Engineering Design Services to AEs the ld. AR submitted that similar issue had come up before the Tribunal in assessee's own case in ITA No. 358/PN/2013 for assessment year 2008-09. The Tribunal held that the adjustment arising as a result of TP analysis is to be confined to the international transactions undertaken with AEs alone and not in relation to none AE transactions.

4.4 In ground No. 5 the assessee has assailed erroneous selection of comparable company – Coral Hub Limited the ld. AR submitted that the

said company is not functionally comparable with the assessee. The assessee is providing IT based engineering services whereas Coral Hub Limited is engaged in electronic publishing and converting the books/articles into digitized format to be sold online. The ld. AR submitted that the Coral Hub Limited cannot be selected as comparable on account of different financial year, different business model and abnormal profitability trend. The ld. AR pointed that Coral Hub Limited is outsourcing its work whereas the assessee is rendering services through in-house employees. The financial results of Coral Hub Limited comprises of 15 months i.e. starting from 1<sup>st</sup> April, 2009 to 30<sup>th</sup> June, 2010 as against financial results of the assessee for 12 months starting from 1<sup>st</sup> April, 2009 to 31<sup>st</sup> March, 2010. The ld. AR submitted that the Tribunal in various cases has held that Coral Hub Limited is not a good comparable with a company engaged in ITES. To support his submissions, the ld. AR placed reliance on the following decisions :

- i. Rampgreen Solutions Pvt. Ltd. Vs. CIT, 377 ITR 533 (Delhi);
- ii. John Deere India (P.) Ltd. Vs. DCIT, 77 taxmann.com 7 (Pune-Trib.);
- iii. PTC Software (India) Pvt. Ltd. Vs. DCIT 67 SOT 138 (Pune-Trib.).

4.5 In ground No. 6 of the appeal the assessee has assailed application of export turnover filter in selection of comparable companies. The ld. AR fairly admitted that in the earlier assessment years the assessee has not agitated this ground.

4.6 In ground No. 7 of the appeal the assessee has assailed the findings of DRP/Assessing Officer in rejecting following companies as comparables.

- i. Chakkilam Infotech Limited.
- ii. ICRA Techno Analytics Limited.
- iii. ISmart International limited.
- iv. Valuemart Info Technologies Limited.

The ld. AR filed written submissions giving reasons for selecting companies as comparables. However, the ld. AR fairly admitted that the aforesaid companies may not qualify the filters applied by the TPO for selecting the comparable companies.

4.7 In ground No. 8 of the appeal the assessee has assailed erroneous computation of operating margin of comparable entity Acropetal Technologies Ltd. The ld. AR submitted that the TPO/Assessing Officer/DRP erred in considering the adjusted PLI of Acropetal Technologies Ltd. at 18.16% instead of correct margin of 10.12%. The ld. AR referred to working of operating margin of Acropetal Technologies Ltd. at page 247 of the appeal set. The ld. AR to substantiate his contentions placed reliance on the decision of Hyderabad Bench of the Tribunal in the case of ACIT Vs. Hyundai Motors India Engineering P. Ltd. reported as 64 taxmann.com 442 where the correct PLI of Acropetal Technologies Ltd. has been taken as 10.12%. The ld. AR submitted that the issue may be remitted back to the file of Assessing Officer/TPO for re-computation of operating margin.

4.8 In ground No. 9 of the appeal the assessee has prayed for allowing the benefit of risk adjustment in accordance with the directions of Tribunal. The ld. AR submitted that in assessment years 2008-09 and 2009-10 the benefit of risk adjustment was granted to the assessee by the Tribunal. The ld. AR furnished the copy of ITA No. 358/PN/2013 for assessment year 2008-09 and ITA No. 331/PN/2014 for assessment year 2009-10 in assessee's own case.

5. On the other hand Smt. Nirupama Kotru representing the Department vehemently defended the assessment order/directions of DRP.

The ld. DR vehemently prayed for dismissing the appeal of assessee and upholding the impugned order on the issues impugned by the assessee in the grounds of appeal.

5.1 The ld. DR submitted that the Department in appeal has assailed the findings of DRP in accepting segmental profitability to complete TP adjustment. The ld. DR submitted that the issue raised by the Revenue in appeal is squarely covered in favour of the assessee by the order of Tribunal in assessee's own case in ITA No. 358/PN/2013 for assessment year 2008-09 and ITA No. 331/PN/2014 for assessment year 2009-10. The Tribunal has held that the segmental level results should be considered for the TP analysis, and not for the entity level results.

6. We have heard the submissions made by representatives of rival sides and have perused the orders of authorities below. We have also considered the decisions and documents on which the ld. AR of the assessee has placed reliance in support of his contentions.

7. The ground Nos. 1 and 4 of the appeal are general in nature, hence, require no adjudication.

8. In ground No. 2 of the appeal the assessee has assailed non-grant of capacity utilization adjustment while calculating operating margin. It is an undisputed fact that the assessee is a captive service provider. The contention of the assessee is that during the period relevant to the assessment year under appeal the parent company of the assessee filed bankruptcy petition, consequently, there was substantial reduction in the volume of business. The ld. AR of assessee has pointed that the revenue from the US market sharply decreased by 47% and the revenue from

European market constituting of France, Germany and UK has fallen by 54%. It is the contention of the assessee that the assessee could not reduce fixed costs viz. depreciation, rent, employees etc. commensurating to reduction in the business.

In so far as allowability of capacity utilization adjustment is concerned, it has been approved by the Tribunal in various decisions. The Pune Bench of the Tribunal in the case of Amdocs Business Services Pvt. Ltd. Vs. DCIT (supra) by following the decision rendered in the case of Global Vantedge Pvt. Ltd. Vs. DCIT (supra) and various other decisions has observed :

*“The plea set-up by the assessee for economic adjustments on account of under capacity utilization and being in start up phase, is not something which is unreasonable and neither it is otiose to the mechanism of transfer pricing assessments.”*

Thus, the concept of capacity utilization is well accepted. Now, whether the facts in the present case warrant grant of capacity utilization adjustment has to be considered. The TPO outrightly rejected capacity utilization adjustment made by the assessee on the ground that the adjustment is not supported by documentary evidence. The DRP rejected assessee's plea of grant of capacity utilization on two counts : (i) Global slowdown in the auto industry has not only affected the assessee but the other entities as well; and (ii) The capacity utilization sought on the ground of parent company filing bankruptcy petition has not materially affected the business of the assessee. The observations made by the authorities below to disallow capacity utilization are not sustainable. The global meltdown may have affected entire auto industry worldwide but bankruptcy of the present company is an event that is peculiar to the assessee. The assessee before the Tribunal has furnished a table giving the details of 'approved billable hours' in Financial Year 2008-09 and

Financial Year 2009-10 to contend that the business of the assessee has substantially reduced. However, all these details are subject matter of verification. The ld. AR has submitted that during proceedings before the TPO complete working of unutilized capacity was furnished with documentary evidence, however, once again the assessee would reinforce his claim with the support of necessary documents. We are of considered view that this issue needs revisit to TPO for de-novo consideration. The TPO after considering the evidences filed by assessee in support of its claim shall decide this issue, in accordance with law. Accordingly, ground No. 2 raised in the appeal by the assessee is allowed for statistical purpose.

9. In ground No. 3 of the appeal the assessee has assailed computation of adjustment in respect of Provision of Engineering Design Services to AEs. The ld. AR pointed that the TPO while computing transfer pricing adjustment has not restricted the adjustment to the value of international transactions alone. We find that the Co-ordinate Bench of the Tribunal in assessee's own case in ITA No. 358/PN/2013 for assessment year 2008-09 after placing reliance on the decisions rendered in the case of Demag Cranes & Components India Pvt. Ltd. Vs. DCIT reported as 49 SOT 610 has held that TP analysis is to be confined to the international transactions undertaken with AEs alone and not in relation to none AE transactions. We deem it appropriate to remit this issue back to the file of TPO to re-compute adjustment in the light of order of Tribunal in assessee's own case for assessment year 2008-09 (supra). Accordingly, the ground No. 3 raised in the appeal is allowed for statistical purpose.

10. In ground No. 5 of the appeal the assessee has assailed selection of Coral Hub Limited in the final list of comparables on the ground that the said company is functionally different, has abnormal profitability trend,

different financial year and different business model. The ld. AR has pointed that the said company is engaged in E-publishing and converting books/articles into digitized format to be sold online. Whereas, the assessee is providing IT based engineering services. The ld. AR has pointed that the Co-ordinate Bench of the Tribunal in the case of John Deere India (P.) Ltd. Vs. DCIT (supra) has held that Coral Hub Limited is not a good comparable with a company engaged in ITES. The relevant extract of the order of the Tribunal in the case of John Deere India (P.) Ltd. Vs. DCIT (supra) reads as under :

*“51. So far as Coral Hubs Ltd. (earlier known as Vishal Information Technologies Ltd.) is concerned we find the TPO has selected this company as comparable mainly on the ground that it was also considered as comparable for A.Y. 2008-09. We find on the basis of the submission of the assessee that this company is engaged in e-publishing and therefore the business model of the said company is not comparable with that of the assessee company, the Tribunal in assessee’s own case for A.Y. 2008-09 has rejected this company as comparable. The relevant observation of the Tribunal at para 24.1 of the order reads as under :*

*“24.1 Coral Hubs Ltd. (earlier known as Vishal Information Technologies Limited) : The objection of the assessee is that the said company is engaged in E-publishing which is quite different in function from the activities carried out by the assessee. The another objection raised by the assessee is that the operating margin of the said comparables is abnormally high i.e. 51.79%. The Ld. Counsel pointed that in the case of Symphony Marketing Solutions India Pvt. Ltd. Vs. ITO in IT(TP) A.No.1316/Bang/2012, A.Y. 2008-09 decided on 14-08-2013 it has been held that Coral Hubs is not a good comparable on account of functional disparity as well as on account of abnormally high profits. The relevant extract of the order of Tribunal in the case of Symphony Marketing Solutions Pvt. Ltd. (Supra) is as under:*

*“14. This company is listed at Sl.No.6 of the list of comparable companies chosen by the TPO. As far as this company is concerned, it is seen that this company was earlier known as Vishal Information Technologies Ltd. The comparability of this company in the case of an ITES company by name 24 x 7 Customer.com Pvt. Ltd. was considered by the Tribunal in ITA No.227/Bang/2010 and by order dated 09.11.2012 the Tribunal held that this company is not functionally comparable with ITES for the following reason:-*

*“17.3 Vishal Information Technologies Ltd. (VIT) - In the case of this comparable, we find that the Mumbai Tribunal in the case of Mearsk Global Services (I) Pvt Ltd in ITA No.3774/Mum/2011 by order dt.9.11.2011 has held that since Vishal Information Technologies Ltd*

is outsourcing most of its work it has to be excluded from the list whereas the assessee in the cited case was carrying out the work by itself. In the instant case of the assessee also the assessee was carrying out its work by itself whereas in the case of VITL, it is outsourcing most of its work. We are therefore of the considered opinion that the decision of the ITAT, Mumbai in the cited case on the issue of excluding VITL as a comparable squarely applies. This decision was followed by the decision of the co-ordinate bench of this Tribunal in the case of Netlinx India(P) Ltd in ITA No.454/Bang/2011 dt.19.10.2012 wherein it was held that Vishal Information Technologies Ltd cannot be considered as a comparable. We, therefore, respectfully following the decision of the Mumbai Tribunal in the case of Mearsk Global Services (I) Pvt Ltd, direct the Assessing Officer / TPO to exclude Vishal Information Technologies Ltd. from the list of comparables.”

15. Following the decision of the Tribunal referred to above, we hold that Coral Hubs Ltd. cannot be considered as a comparable. It may also be relevant to point out that the TPO in his order has observed that this company is retained as a comparable on the basis of detailed discussion in the TP order for the A.Y. 2007-08. In fact in A.Y. 2007-08, there was no determination of ALP and therefore there was no occasion for any order being passed by the TPO. It is also seen that this company entered into an area of business known as New Vertical Digital Library & Print on Demand in F.Y. 2007-08. In the case of Capital IQ Information Systems India Pvt. Ltd. (supra), the ITAT Hyderabad Bench in the case of ITES company considered the comparable of this company as an ITES company and held as follows:-

“IV. Coral Hub Limited (Earlier known as Vishal Information Technologies Ltd.):

16. The assessee has objected for this company being taken as comparable mainly on the ground that the activities of the company is not only functionally different, but the business model of the company is also different as it sub-contracts majority of its ITES works to third party vendors and has also made significant payments to those vendors. The payments made to vendors towards the data entry charges also supports the fact that the company outsources its works. In the circumstances, it cannot be taken as a comparable to the ITES functions performed by the assessee. Since this company is acting as agent only by outsourcing its works to the third party vendors. In this context, the assessee relied upon the order of the DRP in assessee's own case for the assessment year 2008-09, wherein the DRP, after taking into consideration, the aforesaid aspect, has accepted the claim of the assessee. The assessee further submitted that the Incometax Appellate Tribunal Mumbai Bench in the case of Asstt. CIT v. Maersk Global Service Centre (India) (P.) Ltd. [2011] 133 ITD 543/16 taxmann.com 47 (Mum.), a copy of which is submitted before us, has also directed for the exclusion of the aforesaid company since it has outsourced a considerable portion of its business.

17. After considering the submissions of the learned Authorised Representative for the assessee, we find that the DRP, in the proceedings for the assessment year 2008-09 in assessee's own case, after taking note of the composition of the vendor payments of Coral Hub for the last three years, and the fact that it has also commenced a new line of business of Printing on Demand(POD), wherein it prints upon clients request, concluded as follows-

"18.4. In view of this major difference in functionality and the business model, this Panel is of the view that 'Coral Hub' is not a suitable comparable to the taxpayer and hence needs to be dropped from the final list of comparables.

"In case of Maersk Global service Centre India (P.) Ltd. (supra), the ITAT Mumbai Bench has also directed for exclusion of the aforesaid company, by observing in the following manner-

"Insofar as the cases of Tulsyan Technologies Limited and Vishal Information Technologies Limited are concerned, it is noticed from their annual accounts that these companies outsourced a considerable portion of their business. As the assessee carried out entire operations by itself, in our considered opinion, these two cases were rightly excluded."

In view of the observations made by the DRP as well as the decision of the ITAT Mumbai in the case of Maersk Global Service Centre, (supra), we accept that this company cannot be taken as a comparable."

16. It is also further noticed that the employee cost/operating sales of this company is a mere 3%, whereas the threshold limit for acceptance as a comparable on the basis of employee cost to sales should be at least 25%. This Tribunal in the case of First Advantage Offshore Services Ltd. v. CIT, IT(TP)A No.1086/Bang/2011, order dated 30.4.2013, has taken the following view:-

"36. Having heard both the parties and having considered their rival contentions and the material on record, we find that this issue had arisen in the assessee's own case for the assessment year 2006-07. This Tribunal has held that employee cost filter is to be the same even for ITES segment also. The learned DR's argument that the employee cost filter is applicable only to software development segment and not to ITES segment is not acceptable. Though it is without any dispute that the software development would require skilled employees and, therefore, the employee cost would definitely be more than 25% of the total expenses, it cannot be said that the said filter is not applicable to ITES segment, where 38 comparably less skilled employees are employed. In the ITES segment, the entire work is to be done by the employees and, therefore, even though they may be less skilled compared to software development segment, the number of employees would definitely be more and thus the employee cost would be high and thus application of employee cost filter to the ITES sector is also justified. In view of the same, we direct the TPO to apply the employee

*cost filter to exclude companies with employee cost of less than 25% from the list of comparables for the computation of ALP.”*

*17. Applying the aforesaid decisions, we are of the view that Coral Hubs Ltd. cannot be considered as a comparable.”*

*We are of the considered view that the assessee company is functionally different from Coral Hub Limited. Both the companies have different operating models, thus there cannot be any comparison between two entities having different business spheres and distinct mode of operation. Accordingly, we direct the TPO/AO to exclude the company from the list of comparable entities.”*

*52. Following the decision of the Tribunal in assessee’s own case in the immediately preceding assessment year and in absence of any contrary material brought to our notice, we direct the TPO/AO to exclude Coral Hubs Ltd. from the list of comparables on account of different operating models/different business spheres and distinct mode of operation.”*

The Hon’ble Delhi High Court in the case of Rampgreen Solutions Pvt. Ltd. Vs. CIT (supra) has excluded Coral Hub Limited (earlier known as Vishal Information Technologies Ltd.) from the list of comparables on the ground of functional dissimilarity. The Relevant extract of the order of Hon’ble High Court in the case of Rampgreen Solutions Pvt. Ltd. Vs. CIT (supra) reads as under :

*“38. In our view, even Vishal could not be considered as a comparable, as admittedly, its business model was completely different. Admittedly, Vishal’s expenditure on employment cost during the relevant period was a small fraction of the proportionate cost incurred by the Assessee, apparently, for the reason that most of its work was outsourced to other vendors/service providers. The DRP and the Tribunal erred in brushing aside this vital difference by observing that outsourcing was common in ITeS industry and the same would not have a bearing on profitability. Plainly, a business model where services are rendered by employing own employees and using one’s own infrastructure would have a different cost structure as compared to a business model where services are outsourced. There was no material for the Tribunal to conclude that the outsourcing of services by Vishal would have no bearing on the profitability of the said entity.*

*39. It is also relevant to note that in the case of **Maersk Global Centers (India) Pvt. Ltd. (supra)**, the DRP itself had accepted the objection of the Assessee and had excluded Vishal as a comparable for the reason as quoted below:-*

*“... that it had a very low employment cost and very high cost on account of venture payment, which suggested that its business model was that of an outsourcing company and in view of this functional difference, Vishal Ltd. could not be considered as a comparable.”*

40. The Assessee had also sought the exclusion of eClerx and Vishal on the ground that both the companies had returned supernormal profits. Whereas the operating margins (operating margin over total cost) in case of Vishal and eClerx were 50.68% and 65.88% respectively, the PLIs of all other comparables were in the range of 2.2% to 24%. In our view, it would not be apposite to exclude comparables only for the reason that their profits are high, as the same is not provided for in the statutory framework. The OECD Guidelines suggest that a quartile method be adopted which excludes entities that fall in the extreme quartiles for comparability. However, neither Chapter X of the Act nor the Rules made by CBDT provide for exclusion for such statistical reason.

41. Having stated the same, it may be necessary to bear in mind that supernormal profits may in certain cases indicate a functional dissimilarity or dissimilarity with respect to a feature that has a material bearing on the profitability. In such circumstances, it would be necessary to undertake further analysis to eliminate the possibility of the high profits resulting on account of any material dissimilarity between the tested party and the chosen comparable. A wide deviation in the PLI amongst selected comparables could be indicative that the comparables selected are either materially dissimilar or the data used is not reliable. The Tribunal proceeded on the basis that an adjustment could be made only in cases where supernormal profits resulted from the factors indicated in Rule 10B of the Income Tax Rules, 1962. In our view, the factors mentioned in Rule 10B are not exhaustive. The principal object of benchmarking international transactions against uncontrolled transactions is to impute an ALP to those transactions. This exercise would fail if a factor, which has a material bearing on the value or the profitability, as the case may be, depending on the method used, is ignored.

42. Before concluding, there is yet another aspect of the matter that needs consideration. The Tribunal proceeded on the basis that while applying TNMM method, broad functionality is sufficient and it is not necessary that further effort be taken to find a comparable entity rendering services of similar characteristics as the tested entity. The DRP held that TNMM allows flexibility and tolerance in selection of comparables, as functional dissimilarities are subsumed at net margin levels, as compared to Resale Price Method or Comparable Uncontrolled Price Method and, therefore, the functional dissimilarities pointed out by the Assessee did not warrant rejection of eClerx and Vishal as comparables.”

Thus, in view of the above decisions we hold that Coral Hub Limited is liable to be rejected from the list of comparables on account of different business model and functional differences. We hold and direct, accordingly. Hence, ground No. 5 raised in the appeal is allowed.

11. In ground No. 6 of the appeal the assessee has assailed application of export turnover filter in selection of comparables. The ld. AR fairly

admitted that in the earlier assessment years, the assessee has not challenged the application of export filter. Since, export filter has been applied for selecting comparables in the past and the same was not assailed by the assessee, we find no reason to exclude the same in the assessment year under appeal. Accordingly, ground No. 6 raised in the appeal by the assessee is dismissed.

12. In ground No. 7 of the appeal the assessee has assailed rejection of **Chakkilam Infotech Limited** - The said company has been rejected by the TPO/DRP as the company fails to qualify export turnover filter. The TPO has applied export turnover filter of 75%. The ld. AR of the assessee has failed to show that the export revenue of the said company is more than 75% of the total revenue. We do not find any merit in the submissions of the ld. AR of the assessee. Accordingly, we confirm the findings of authorities below in rejecting the said company.

**ICRA Techno Analytics Limited** - The company has been rejected by the DRP on the ground that the assessee has failed to furnish annual report for comparability analysis. Moreover, information extracted from the website of the company does not give segmental account of engineering design service. In the absence of segmental accounts the said company has been excluded from the list of comparables. The ld. AR has failed to controvert the findings of authorities below. No material has been placed on record to show the segmental accounts of engineering design service of the said company. We do not find any error in the findings of authorities below in rejecting the said company as comparable.

**ISmart International limited** - The said company has been rejected from the list of comparables as the financial data of the company is not available. The ld. AR of assessee has fairly admitted that the assessee has

failed to furnish annual report of the said company. The financial results of the company are not available in public domain. In the absence of financial results an entity cannot be selected as comparable. Hence, the authorities below have rightly rejected the company for TP analysis.

**Valuemart Info Technologies Limited** – The said company has been excluded from the list of comparables on account of functional disparity. The authorities below have observed that the company is engaged in Consultancy and Software Development. The company provides specialized and customized solutions to address the specific needs of its clients. The activities of the company fall within the domain of KPO. Whereas, the assessee is engaged in business of designing and developing products in CAD/CAM of auto parts. The functions performed by both the companies are entirely different, therefore, the aforesaid company cannot be selected as comparable. The ld. AR of assessee has failed to controvert the findings of the DRP. No material is brought to our notice indicating that the activities of the company is similar to that of the assessee. We find no reason to interfere with the findings of authorities below to exclude the company from the list of comparables. Hence, the submissions made by ld. AR for inclusion of Valuemart Info Technologies Ltd. are rejected.

In the result, the ground No. 7 raised in the appeal by assessee is dismissed being devoid of any merit.

13. In ground No. 8 of the appeal the assessee has assailed computation of operating margin of comparable companies. The assessee has prayed for re-computation of operating margin of Acropetal Technologies Ltd. It has been pointed that the correct operating margin of the company is 10.12% as against 18.16% computed by TPO. To support his submissions the ld. AR draws strength from the decision rendered in the case of ACIT

Vs. Hyundai Motors India Engineering P. Ltd. (supra). The assessee has furnished working of operating margin of Acropetal Technologies Ltd. at page 247 of the appeal set. The computation of operating margin requires verification. Accordingly, we deem it appropriate to remit this issue back to the file of TPO for re-computation of operating margin of Acropetal Technologies Ltd. and apply the correct margin for comparable analysis. Accordingly, ground No. 8 raised in the appeal by the assessee is allowed for statistical purpose.

14. In ground No. 9 of the appeal the assessee has assailed non-granting of risk adjustment. The ld. AR of the assessee has pointed that risk adjustment has been allowed to the assessee by the Tribunal in earlier assessment years i.e. assessment years 2008-09 and 2009-10. It is not controverted that there has been no change in the facts and circumstances in the assessment year under appeal. We find that the Co-ordinate Bench of the Tribunal in assessee's own case in ITA No. 358/PN/2013 for assessment year 2008-09 has allowed risk adjustment to the assessee subject to fulfillment of certain conditions. We deem it appropriate to remit this issue back to the file of TPO to allow risk adjustment in line with the directions of the Tribunal in ITA No. 358/PN/2013 (supra). Accordingly, ground No. 9 raised in the appeal by assessee is allowed for statistical purpose.

15. In ground No. 10 of the appeal, the assessee has prayed for allowing benefit of variation of  $\pm 5\%$ . The TPO is directed to grant the benefit of  $\pm 5\%$  to the assessee, in accordance with law.

16. In ground No. 11 of the appeal the assessee has challenged initiation of penalty u/s. 271(1)(c) of the Act. The challenge to penalty proceedings

at this stage is pre-mature. Accordingly, ground No. 11 raised in the appeal by assessee is dismissed.

17. In ground No. 12 of the appeal, the assessee has assailed charging of interest u/s. 234B of the Act. The charging of interest u/s. 234B is mandatory and consequential. Accordingly, ground No. 12 of the appeal is dismissed.

18. The ground Nos. 13 and 14 are general in nature. Hence, require no adjudication.

19. In the result, the appeal of assessee is partly allowed for statistical purpose in the terms aforesaid.

**ITA No. 540/PUN/2015 (A.Y. 2010-11)**

20. The Revenue has assailed the assessment order on following grounds:

*“01. On the facts of the case and in law, the DRP erred in directing the AO to compute the TP adjustment by accepting segmental profitability computed by assessee when assessee did not maintain separate books for AE and Non AE transactions.*

*02. On the facts of the case and in law, the DRP erred in directing the AO to compute the TP adjustment by accepting segmental profitability computed by assessee, whereas the assessee has applied TNMM and therefore adjustment would have to be computed at entity level. The law does not provide for a pro-rate adjustment when TNMM is applied at entity level.*

*03. On the facts and in law DRP erred in directing the AO to allocate unallocable expenses to each segment in proportion to segmental turnover, to total turnover as such allocation is unscientific and not based on actual figures.*

*04. The appellant craves leaves to add, amend alter any or all of the above grounds of appeal.”*

21. Both the sides are unanimous in accepting that the grounds raised in the appeal by Revenue against accepting segmental profitability for computing TP adjustment has been decided by the Tribunal in assessee's own case in ITA No. 358/PN/2013 (supra). The relevant extract of the findings of the Tribunal are as under :

*17. We have considered the rival arguments made by both the sides, perused the orders of the TPO/AO/DRP and the paper book filed on behalf of the assessee. We have also considered the various decisions cited before us. We find the TPO in the instant case made an adjustment to the assessee's international transaction of the provision of IT based Engineering Services considering the operating margin of 11.67% of the whole entity. While doing so, he rejected the contention of the assessee that adjustment should be made only on segmental profitability of "Exports to AEs" as profitability of domestic sales does not reflect profits earned from any international transactions. We find the DRP agreed in principle that PLI should be computed only on international transaction and accordingly held that it should be computing according to the segment consisting of the international transactions with the AEs. Accordingly, they directed the AO to work out PLI of the segment consisting of the international transactions only if such segmental data is available.*

*18. It is the submission of the Ld. Counsel for the assessee that he has filed such segmental profitability before DRP, copies of which are placed at pages 73 to 80 of the paper book. From pages 73 to 80 of the appeal memo we find the assessee has given segmental profitability based on scientific and consistent methodology. No mistakes have been pointed out by the DRP/TPO. The Various Benches of the Tribunal are consistently taking the view that PLI should be considered only for the segment pertaining to international transactions with AEs. We accordingly hold that the TPO should not have rejected the segmental profitability of the assessee in respect of provision of Engineering Design Services to its AEs. Since the segmental profitability as submitted by the assessee has not been examined either by the TPO or the DRP and since the DRP had also directed the AO to work out the PLI of the segment consisting of the international transactions if such segmental data is available, therefore, we, in the interest of justice, direct the AO to work out PLI of the segment consisting of the international transactions only. The ground raised by the assessee is accordingly allowed for statistical purposes."*

Similarly, in the assessment year 2009-10 in ITA No. 331/PN/2014 the Tribunal in assessee's own case decided this issue in favour of the assessee. The relevant extract of the findings of Tribunal are as under :

*"12. We find that similar adjustment of the PLI by only considering the segmental profitability of exports made by the assessee to its associate enterprises to be considered for working out the PLI of assessee company,*

arose before Pune Bench of Tribunal in assessee's own case in assessment year 2008-09 and the Tribunal vide order dated 21.10.2015 held as under:-

“17. We have considered the rival arguments made by both the sides, perused the orders of the TPO/AO/DRP and the paper book filed on behalf of the assessee. We have also considered the various decisions cited before us. We find the TPO in the instant case made an adjustment to the assessee's international transaction of the provision of IT based Engineering Services considering the operating margin of 11.67% of the whole entity. While doing so, he rejected the contention of the assessee that adjustment should be made only on segmental profitability of “Exports to AEs” as profitability of domestic sales does not reflect profits earned from any international transactions. We find the DRP agreed in principle that PLI should be computed only on international transaction and accordingly held that it should be computing according to the segment consisting of the international transactions with the AEs. Accordingly, they directed the AO to work out PLI of the segment consisting of the international transactions only if such segmental data is available.

18. It is the submission of the Ld. Counsel for the assessee that he has filed such segmental profitability before DRP, copies of which are placed at pages 73 to 80 of the paper book. From pages 73 to 80 of the appeal memo we find the assessee has given segmental profitability based on scientific and consistent methodology. No mistakes have been pointed out by the DRP/TPO. The Various Benches of the Tribunal are consistently taking the view that PLI should be considered only for the segment pertaining to international transactions with AEs. We accordingly hold that the TPO should not have rejected the segmental profitability of the assessee in respect of provision of Engineering Design Services to its AEs. Since the segmental profitability as submitted by the assessee has not been examined either by the TPO or the DRP and since the DRP had also directed the AO to work out the PLI of the segment consisting of the international transactions if such segmental data is available, therefore, we, in the interest of justice, direct the AO to work out PLI of the segment consisting of the international transactions only. The ground raised by the assessee is accordingly allowed for statistical purposes.”

13. Similar issue has been decided by Chennai Bench of Tribunal in *3i Infotech Ltd. Vs. ITO* (2013) 35 taxmann.com 582 and *Honeywell Electrical Devices & Systems India Ltd. Vs. ACIT* (2014) 64 SOT 118. Following the same parity of reasoning, we hold that segmental profitability in respect of provision of engineering design services by the assessee to its associate enterprises, should be considered to work out the PLI of international transactions undertaken by the assessee. The Assessing Officer / TPO is thus, directed to re-work the PLI of segment consisting of international transactions and we direct the Assessing Officer to work out the same after affording reasonable opportunity of hearing to the assessee. The ground of appeal No.2 raised by the assessee is allowed for statistical purposes.”

22. Thus, in view of the decision of Co-ordinate Bench in assessee's own case, the grounds raised by the Revenue are dismissed. Accordingly, the appeal of Revenue is dismissed.

23. To sum up, the appeal of assessee is partly allowed for statistical purpose and the appeal by the Revenue is dismissed.

Order pronounced on Monday, the 28<sup>th</sup> day of May, 2018.

Sd/-	Sd/-
(डी. करुणाकरा राव/D. Karunakara Rao)	(विकास अवस्थी / Vikas Awasthy)
लेखा सदस्य / ACCOUNTANT MEMBER	न्यायिक सदस्य / JUDICIAL MEMBER

पुणे / Pune; दिनांक / Dated : 28<sup>th</sup> May, 2018

RK

**आदेश की प्रतिलिपि अग्रेषित / Copy of the Order forwarded to :**

1. अपीलार्थी / The Appellant.
2. प्रत्यर्थी / The Respondent.
3. The Dispute Resolution Panel, Pune
4. The DIT(TP/IT), Pune
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, "बी" बेंच,  
पुणे / DR, ITAT, "B" Bench, Pune.
6. गार्ड फ़ाइल / Guard File.

//सत्यापित प्रति // True Copy//

आदेशानुसार / BY ORDER,

निजी सचिव / Private Secretary,  
आयकर अपीलीय अधिकरण, पुणे / ITAT, Pune