

IN THE INCOME TAX APPELLATE TRIBUNAL “C” BENCH : KOLKATA

[Before Hon’ble Shri S.S. Godara, JM & Shri M.Balaganesh, AM]

I.T.A No. 1457/Kol/2017

Assessment Year : 2008-09

ACIT, Circle-14(1), Kolkata

(Appellant)

-vs- M/s Acclaris Business Solutions (P) Ltd.

[PAN: AAECA 2366 E]

(Respondent)

For the Appellant : Shri Sanjoy Paul, Addl. CIT Sr. DR

For the Respondent : Shri J.P. Khaitan, AR

Date of Hearing : 06.09.2018

Date of Pronouncement : 14.09.2018

ORDER

Per M.Balaganesh, AM

1. This appeal by the Revenue arises out of the order of the Learned Commissioner of Income Tax(Appeals)-22, Kolkata [in short the ld CIT(A)] in Appeal No. 171/CIT(A)-22/2008-09/14-15/Kol dated 03.03.2017 against the order passed by the DCIT, Circle-4, Kolkata [in short the ld AO] under section 143(3) of the Income Tax Act, 1961 (in short “the Act”) dated 09.02.2012 for the Assessment Year 2008-09.

2. The only issue to be decided in this appeal is as to whether the ld CITA was justified in deleting the addition of Rs 1,36,61,522/- made towards adjustment to Arm’s Length Price (in short ALP) in the facts and circumstances of the case

3. The brief facts of this issue are that the assessee is a domestic company incorporated on 6.6.2003 and is a 98% subsidiary of Acclaris Inc. The residual 2% was held by two resident Indians. The assessee provides Business Process Outsourcing (in short BPO) Services including adjudication of financial service authority claims, medical claims and travel and expense claims, e-recruitment services, financial accounting services (i.e accounts payable administration, reconciliation of collections of credit card and otherwise etc) , tax processing services, mortgaging services and routine back office services which could be like indexing and enrollment for client. The assessee company bills Acclaris Inc. (Associated Enterprise – AE of the assessee) on a man month rate for the number of employees employed as on the last day of the month. On the other hand, the AE undertakes the entire marketing and business development activity to generate business, negotiates and enters into contracts with customers, bears the costs of the entire project transition phase, renders the requisite training to its employees or employees of assessee in relation to the project and performs the function of seeing the complete project through. The assessee for the Asst Year 2008-09 filed its return of income declaring total income of Rs 56,828/- after claiming deduction u/s 10A and 10B of the Act in respect of its various units. During the year under consideration, the assessee provided BPO services to its parent , Acclaris Inc. which resulted in international transactions of around Rs 14,36,38,836/- with its AE. Apart from this, the assessee also had other international transactions with its AE in respect of receipt of interest free loan of Rs 6,77,897/- and recovery of expenses of Rs 60,460/-. The last two items of international transactions are not in dispute in the present appeal and hence no discussion is made regarding the same. The assessee adopted the book value of the international transaction in respect of services rendered to its AE as the ALP in its Transfer Pricing (in short TP) study Report. The key financials of the assessee company for the year under consideration are as under:-

Turnover – Rs 14,49,80,362/-

Profit before tax – Rs 2,06,61,729/-

Net Fixed Assets – Rs 3,05,54,563/-

3.1. The Functional , Assets and Risk Profile of the assessee and AE are as under:-

The functions performed by the entities are summarized below:

Functions	Brief of the Function	Acclaris Inc.	Appellant
Deposits and disbursements	Reconciliation of the claim to confirm that all payments required to be made to client's employees have been processed by Acclaris Inc.-executed through 'Acclaim Software' owned by Acclaris Inc.	√	√
Delivery Supervision	Supervising all services to client, prioritizing deliveries to the client	√	X
Query Resolution (Non-Voice)	Basic query Handling through raising of help desk tickets	√	√
Query Resolution (Voice)	Resolving complex customer queries through voice based support	√	X
Software requirement and design	Interaction with clients to seek requirements , designing of solutions, testing and deployment	√	X
Basic coding and testing	Basic software coding and testing under supervision by Acclaris Inc.	X	√

(b) Assets

The appellant does not own any significant intangible and does not undertaken any significant Research and Development on its account that leads to the development of non-routine intangibles. It leverages on the process, know-how, technical data software, operating/quality standards etc. developed/owned by Acclaris Inc. for undertaking the above functions.

(c) Risks

The risks assumed by the appellant and AE in course of performing the above functions are summarized below. Since, the appellant is operating under the captive arrangement and entirely under the support and guidance of the AE, it is absolved of most of the business and operational risks arising out of the operations.

Particulars	Acclaris Inc.	Acclaris India
Market Risk / Price Risk	√√	XX
Service Liability / Quality Risk	√√	XX
Credit Risk	√√	XX
Manpower Risk	√	√√
Entrepreneurial Risk	√√	XX
Foreign Exchange Risk	√√	XX

As it can be seen from above that the appellant does not assume any significant risk from its business operation.

(d) Characterization

In light of the above, the appellant being a captive service provider remunerated on a cost plus model does not bear risks like R&D risk, credit risk, price risk, capacity utilization risk and forex risk whereas Acclaris Inc, being an entrepreneur is exposed to all risks associated with its business operations. Considering the same, the appellant was characterized as a routine IT enabled service provider providing back-office services exclusively to Acclaris Inc, which assumes less than normal risks associated with carrying out such business.”

4. The assessee for the services rendered to its AE adopted Transactional Net Margin Method (TNMM in short) as the Most Appropriate Method (MAM in short). The Profit Level Indicator (PLI in short) adopted by the assessee was Operating Profit / Total Cost [OP / TC] and accordingly the PLI of the assessee was arrived at 16.38%. The PLI of the comparable companies chosen by the assessee was 12.68% and accordingly the assessee considered the pricing done by it as the ALP and did not make adjustment in its TP study and in the return of income.

5. The case was referred to Learned Transfer Pricing Officer (in short ld TPO) u/s 92CA of the Act. The ld TPO observed that the assessee had used the Prowess database developed by Centre for Monitoring Indian Economy Private Limited (CMIE) and Capitaline Plus based on which, the assessee company arrived at 10 comparable companies. The ld TPO observed that the assessee had used multiple year data for three financial years. In view of this, the assessee was asked to show cause as to why adoption of multiple year data should not be rejected as the statute prescribes adoption of contemporaneous data relevant to the year under consideration. The ld TPO observed that the assessee in its response did not provide any additional information or evidence regarding its justification for the use of multi year data other than that of its general write up on the use of multi year data provided in its TP report. The ld TPO further observed that the assessee in its TP analysis had considered loss making

companies, companies having turnover as high as Rs 100 crores and above to as low as Rs 1.50 crores etc.

6. The Id TPO performed his search taking into consideration the following filters:-

- a) All companies having accounts of the year 2007-08
- b) Companies engaged in IT enabled services
- c) Sales between 10 crores to 20 crores
- d) Operating Profit > 0
- e) Related Party Transactions as % of Sales > 10%

7. The assessee by applying the aforesaid filters also performed a detailed review of functional and product profile of 10 comparable companies as under:-

Sl No.	Name of Comparable	Database	PLI (OP/TC)
1.	A O K In-House B P O Services Ltd	Prowess	12.25%
2.	C-Edge Technologies Ltd	Prowess	5.07%
3.	Cameo Corporate Services Ltd	Prowess	4.53%
4.	Datamatics Financial Services Ltd	Prowess	37.83%
5.	Galaxy Commercial Ltd	Prowess	4.82%
6.	H O V Ar Mgmt. Services Pvt Ltd. (formerly know as Bay Area Credit Service (India) Private Ltd.)	Prowess	45.27%
7.	Hyundai Motor India Engg Pvt Ltd	Prowess	7.63%
8.	Indusind Information Technology Ltd	Prowess	79.82%
9.	Coware India	Prowess	12.50%
10.	iSmart Intl	Prowess	2.91%
Mean			21.26%

8. From the above list of comparable companies, the assessee on its own, carried out the FAR analysis of the comparables wherein the assessee accepted the following comparables :-

Sl No.	Name of Comparable	Database	PLI (OP/TC)
1.	A O K In-House B P O Services Ltd	Prowess	12.25%
3.	Cameo Corporate Services Ltd	Prowess	4.53%
4.	Datamatics Financial Services Ltd	Prowess	37.83%
5.	Galaxy Commercial Ltd	Prowess	4.82%
6.	H O V Ar Mgmt. Services Pvt Ltd. (formerly know as Bay Area Credit Service (India) Private Ltd.)	Prowess	45.27%
7.	Hyundai Motor India Engg Pvt Ltd	Prowess	7.63%
Mean			18.72%

9. The assessee filed a written submission dated 14.10.2011 explaining the reasons for accepting and rejecting the comparables chosen. On examination of the assessee's reasons for rejection of the comparables in Annexure 9 to the said letter dated 14.10.2011, it was found that one comparable company namely , Indusind Information Technology Ltd has been rejected by the assessee as comparable on the basis that the annual report and the website of the company could not be found. Subsequently the assessee vide order sheet noting dated 21.10.2011 was requested to provide an explanation on how non-availability of the annual report or the website of Indusind Information Technology Ltd can be regarded as a ground for rejection. The assessee in its reply dated 27.10.2011 submitted as under:-

"..... For determining comparability of comparable companies with the assessee, the 'Annual Report' and 'Website Review' of respective comparables was analyzed. However, the Annual report and Website Review of comparable company, Indusind Information Technology Ltd. could not be obtained. Hence, due to unavailability of information on the functional profile of the company, it was not possible for the assessee to conclude that the said comparable is into providing ITes/BPO services and that the same can be included in the comparable set for the assessee....."

10. The Id TPO in his order rejected the adoption of multi year data done by the assessee and further observed that the comparable Indusind Information Technology Ltd company details are available on the database and hence non-availability of annual report and website cannot be a ground for rejection of the said comparable.

Accordingly, the Id TPO by applying the data for the relevant financial year i.e FY 2007-08 and by including the comparable Indusind Information Technology Ltd arrived at the PLI of comparables as under:-

Sl No.	Name of Comparable	Database	PLI (OP/TC)
1.	A O K In-House B P O Services Ltd	Prowess	12.25%
2.	Cameo Corporate Services Ltd	Prowess	4.53%
3.	Datamatics Financial Services Ltd	Prowess	37.83%
4.	Galaxy Commercial Ltd	Prowess	4.82%
5.	H O V Ar Mgmt. Services Pvt Ltd. (formerly know as Bay Area Credit Service (India) Private Ltd.)	Prowess	45.27%
6.	Hyundai Motor India Engg Pvt Ltd	Prowess	7.63%
7.	Indusind Information Technology Ltd	Prowess	79.82%
Mean			27.45%

11. The Id TPO determined the ALP of services rendered by the assessee to its AE as under:-

Operating Expenses of the tested party being the assessee – Rs 12,34,21,430/-

“The Arm’s Length Price would be 123,421,430/- x [1+0.2745] = Rs. 157,300,358/-.

Applying the Variation of +-5%, the allowable range of ALP, which can be chosen by assessee, would be from Rs. 149,435,340 to Rs. 165,165,376/-.

Hence, the adjustment required to be made to the transaction is as below:

Sl. No.	Nature of transaction	Amount Received by assessee (Rs.)
1	Services Rendered	143,638,836/-
Total		143,638,836/-
Arm's Length Price		157,300,358/-
Upward Adjustment Required		Rs. 13,661,522/-

12. This sum of Rs 1,36,61,522/- towards upward adjustment to ALP in respect of services rendered by the assessee to its AE was added by the ld AO in the order passed u/s 143(3) of the Act dated 9.2.2012. This adjustment was deleted by the ld CITA by placing reliance on the decision of this tribunal in assessee's own case for the Asst Year 2007-08. Aggrieved, the revenue is in appeal before us.

13. We have heard the rival submissions. It is not in dispute that the TNMM is the MAM adopted by both the assessee as well as the revenue. There is no dispute in adoption of OP / TC as the PLI in the facts of the instant case. The issue is only with regard to exclusion of a comparable. The short point that arises for our consideration in the instant appeal is as to whether the exclusion of one comparable company i.e Indusind Information Technology Ltd by the ld CITA is in order. It is the case of the ld AR that if this one comparable alone is rejected , then the price charged by the assessee to its AE on the services rendered would be at Arm's Length as the said price falls within the tolerance range of (+) / (-) 5%. In this regard, we would like to make it clear that the ld AR did not seek for standard deduction of 5% tolerance limit to justify the pricing done by the assessee company in the instant case. It was submitted that after exclusion of Indusind Information Technology Ltd , the arithmetic mean of the comparables would be 18.72% and accordingly the price charged by the assessee to its AE on the services rendered would be at Arm's Length. We find that the ld CITA had only granted relief to the assessee by placing reliance on the order of this tribunal in assessee's own case for the Asst Year 2007-08 in ITA No. 695/Kol/2011 dated 11.6.2015.

“6.3. As regards Indusind Information Technological Limited, it is the case of the assessee that the business model of the comparable chosen by the TPO is that of software development unlike that of the assessee company which is engaged in the business of BPO service.

6.4. After considering the submissions made by the parties and the judgments relied upon, we are in agreement with the averments made by the ld. Sr. Counsel for the assessee that the aforesaid comparable may be excluded for the purpose of

benchmarking the arm's length price of the international transactions entered into by the assessee. The software development company has a completely different functional profile as compared to a company engaged in BPO Services. The risk undertaken and the assets employed by a software development company cannot be compared to a BPO company.

6.5. A similar issue arose for consideration before the ITAT Chennai Bench in the case of *S.R.A.Systems Ltd. vs ACIT (2014) 147 ITD 353* wherein the Tribunal has held as under :-

“7. We considered this issue in detail. It is the case of the assessee before the lower authorities that the turnover of the assessee for the past five years averaged to Rs.25 crores and therefore its turnover base for the purpose of arriving at comparables should be taken in the range of Rs.15 to 25 crores after eliminating related party transactions. On the above basis, the assessee stated that the PLI came to 2.53% as against the PLI reported by the assessee at 3.33%. Even when the turnover criterion is adopted at Rs.50 crores, the PLI came to 3.18%, which is much higher than the PLI criterion of 2.53%. It was the contention of the assessee that the business model of the assessee is based more on turnkey projects, where cost overruns were borne by the assessee that actual bench costs were much more than that estimated by the assessee, that the assessee had to incur considerable expenditure on research and development and that the assessee's financials should be compared to software development companies and not with companies in the area of BPO, KPO etc. 8. It is seen that it is against the above objections raised by the assessee that the TPO has worked out the PLI at 25.44% as against the PLI at 3.5%, resulting an upward adjustment of Rs.4,33,80,146/-. There is no justification on the part of the TPO to compare the financials of the assessee- company to those of BPO and KPO companies. The financials of the assessee should be compared only with software development companies. When a general comparison is made, huge expenditure incurred on research and development should be considered. It is also to be seen that the business model of the assessee was based more on turnkey projects, in which case cost overruns would have to be borne by the assessee-company. In the facts and circumstances of the case, we are not in a position to accept the PLI at 25.44% determined by the TPO on the ratio of operating profit to operating cost. This against the PLI returned by the assessee company at 3.5%. Therefore, we do not approve the upward adjustment of Rs.4,33,80,146/- made by the Assessing Officer to its full extent. On same set of facts, the issue of ALP determination was considered by Dispute Resolution Panel at Chennai in assessee's own case for the assessment year 2008-09. In their direction dated 4-6- 2012 issued under section 144C(5), the Panel has directed the Assessing Officer to adopt the PLI at 13.35% as against the PLI of 21.86% adopted in the assessment. This shows that the upward adjustment made in the impugned assessment is quite arbitrary.”

6.6. In the case of ACIT vs M/s.Maersk Global Service Centers (India) Pvt. Ltd. in ITA No.3774/Mum/2011 vide order dated 09.11.2011 the ITAT Mumbai Bench has held as under :-

“30. The assessee in its transfer pricing study considered transactional net margin method (hereinafter called “TNMM”) as the most appropriate method with NCP margin as the profit level indicator to benchmark its international transactions with AEs. The assessee conducted analysis for determining the ALP of international transactions pertaining to the provisions of back office support services. Based on data available, the weighted average Arithmetical Mean of NCP margins earned by the comparable independent companies performing similar functions, was determined at 7.62%. As the assessee earned NCP of 7.90% from its international transactions, it was concluded that such transactions with AEs were at ALP. The Assessing Officer made reference to TPO for computation of ALP in respect of international transactions. The TPO, vide his order dated 31.10.2008, computed the adjustments to the ALP amounting to Rs.10,49,07,225. In such computation the TPO noted in para 4 of his order that “No companies were identified as comparables”. He selected twelve companies as comparable with the assessee’s international transactions, depicting the NCPs as under:-

Sr.No.	Comparable companies	OP/T%
1.	Allsec Technologies Limited	30.49
2.	Tulsyan Technologies Ltd. (Cosmic Global)	19.08
3.	Saffron Global	24.89
4.	WIPRO BPO Solutions Ltd.	27.60
5.	Vishal Information Technologies Ltd.	45.65
6.	Ace Software Exports Ltd.	15.46
7.	Nucleus Netsoft & GIS India Ltd.	40.60
8.	Asian Cerc Information Technology Ltd.	37.40
9.	Airline Financial Support Services (I) Ltd. (Seg)	26.54
10.	Goldstone Teleservices Ltd. (Seg)	15.95
11.	Transworks Information Services Ltd.	2.87
12.	Cepha Imaging Pvt. Ltd.	47.70
	Mean	27.80”

“48. 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. Coming to the cases of Cepha Imaging Private Limited and Asian Cerc Information Technology Ltd. (Seg.), we find that these companies are engaged in providing software development services as is evident from their annual reports available on pages 52 onwards and 64 onwards of the paper book. Thus these companies become functionally different. Insofar as WIPRO BPO Solutions Limited is concerned, we find that their turnover is eleven times greater than that of the assessee. This

company having such a high brand value along with much higher turnover, in our considered opinion, has been rightly excluded by the ld. CIT(A). The last case being that of Airline Financial Support Services (I) Ltd. has 31.76% of the total service fees received from the controlled transactions with the related parties. This fact is evident from pages 62 of the paper book, which makes it incomparable with the assessee.”

6.7. In ACIT vs M/s. Hapag Lloyd Global Services Private Limited in ITA No.8499/Mum/2010 vide order dated 28.02.2013 similar issue arose wherein ITAT, Mumbai Bench has held as under :-

“4.1. The TPO observed that this company was in ITES both as per Board’s Notification and also D&B Websites. As the assessee had not considered this case, the TPO held it as comparable and included it in the list of comparables. The assessee contended before the learned CIT(A) that the said company was functionally incomparable as it was mainly engaged in software and application development. The learned CIT(A) considered the Annual report of this company and observed that it referred mainly to the income from export sales of software as against the assessee’s business of ITES. Accordingly this case was excluded from the list of comparables.

4.2. The ld. AR mainly relied on the decision of the Mumbai Bench of the tribunal in the case of ACIT v.Mearsk Global Service Centres (India) Private Limited [(2011) 133 ITD 543 (Mum)] to bring home the point that the case of Cepha Imaging Private Limited should be excluded as the same has been held by the tribunal in that case as incomparable.”

“4.4. Adverting to the facts of the instant case we find that the assessee in Mearsk Global Service Centres (India)Private Limited (supra) was a service provider rendering back office support service to its Associated Enterprises (AEs). In para 29 of this order, it has been recorded by the tribunal that the activities undertaken by the assessee were essentially ITES, such as, data entry, transcription and data of shipping documents such as bill of leading etc. The instant assessee before us is also in the same line of business providing similar services as were rendered in the case of Mearsk Global Service Centres (India)Private Limited (supra). Further the A.Y. in both the cases is also similar, that is, 2005-2006. In that case also, the TPO introduced Cepha Imaging Private Limited as comparable. However, the Tribunal vide para 48 of its order observed that this company is “engaged in providing software development service as its evident from their annual report available on pages 52 onwards and 64 onwards of the paper book.” We find that the finding recorded by the learned CIT(A) in the impugned order that Cepha Imaging Private Limited was mainly engaged in export of software tallies with that recorded by the tribunal in the case of Maersk. As the assessee is engaged in ITES, any company engaged in exporting software, cannot be considered as comparable. We, therefore, hold that this case was rightly excluded by the learned CIT(A).

