

THE INCOME TAX APPELLATE TRIBUNAL
"K" Bench, Mumbai
Shri B.R. Baskaran (AM) & Shri Rahul Chaudhary (JM)

I.T.A. No. 732/Mum/2022 (A.Y. 2017-18)

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| Capita India Private Ltd. Plant No. 6, Gate No. 2 Godrej and Boyce Complex LBS Marg, Pirojshah Nagar Vikroli West, Mumbai 400 079. PAN : AABCE7046A (Appellant) | Vs. | National Faceless Assessment Centre, Delhi (Respondent) |
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|-----------------------|--------------------|
| Assessee by | Shri Nikhil Tiwari |
| Department by | Dr. Yogesh Kamat |
| Date of Hearing | 29.06.2022 |
| Date of Pronouncement | 18.08.2022 |

O R D E R

Per B.R.Baskaran (AM) :-

The assessee has filed this appeal challenging the final assessment order dated 25-02-2022 passed by the assessing officer, National faceless assessment centre, Delhi for assessment year 2017-18 u/s 143(3) r.w.s 144C(13) r.w.s 144B of the Act in pursuance of directions given by Ld Dispute Resolution Panel (DRP).

2. Ground nos.1, 21 and 22 are general in nature. Ground nos. 2 to 13 relate to the addition on account of transfer pricing adjustment. Ground nos. 14 to 21 relate to the addition made u/s 14A of the Act.

3. The facts relating to the case are stated in brief. M/s Capita plc is a company based in United Kingdom and it is a leading provider of business process outsourcing and professional services. The assessee herein is a group company of Capita Plc, UK and it is engaged in providing Information Technology Enabled Services (ITES) to its Associated Enterprises (AE). The

assessee herein has got three business centers located in Mumbai, Pune and Bangalore.

4. The first issue relates to the addition made by the AO on account of transfer pricing adjustment. The assessee had entered into international transactions with its AE in the form of provision of ITES. It had received revenue of Rs.345.73 crores during the year under consideration. In its transfer pricing study, the assessee followed TNM method as most appropriate method and Operating Profit to Operating Cost (OP/OC) as Profit level indicator. The PLI of the assessee was 14.75%. The Ld A.R submitted that the assessee is being compensated by its AEs under Cost plus 15% mark-up method. In its transfer pricing study, the assessee selected 14 comparable companies. The 35th Percentile of the margin declared by the above said companies was 6.07% and 65th Percentile was 17.87%. The median was 8.03%. Since the PLI was 14.75%, the assessee claimed that its international transactions have been entered at arm's length.

5. The TPO rejected the transfer pricing study of the assessee. He selected following comparable companies:-

| Sl. No. | Name of Company | Weighted average of OP/OC (%) |
|---------|---------------------------------------|-------------------------------|
| 1. | Jindal Intellicom Limited (Seg) | 8.86% |
| 2. | Infosys BPO | 24.72% |
| 3. | CES Limited | 36.06% |
| 4. | Datamatics Financial Services Limited | 36.22% |
| 5. | MPS Ltd | 60.08% |
| | Arithmetic Mean | 33.19% |

Accordingly, the TPO took the arms length margin at 33.19% and made transfer pricing adjustment of Rs.55,55,86,006/-. The assessee did not get relief before Ld DRP and hence the AO passed the final assessment order making addition of above said amount as transfer pricing adjustment.

6. The assessee has raised many grounds with regard to many comparable companies. However, at the time of hearing, the Ld A.R restricted his arguments on the following pleas only:-

- (a) Inclusion of R Systems International Limited
- (b) Exclusion of Infosys BPO and MPS Ltd.

Accordingly, we proceed to dispose of the grounds relating to the above said three comparable companies only. Accordingly, the grounds related to all other companies are dismissed as not pressed.

7. With regard to the plea of inclusion of M/s R systems International limited, the Ld A.R submitted that the TPO has rejected this company for two reasons, viz.,

- (a) this company has got different accounting year and
- (b) this company was rejected by the TPO in AY 2015-16.

The Ld DRP upheld the view of the TPO on the ground that this company fails in the filter, viz, "Use of different accounting year filter for comparable analysis".

7.1 The Ld A.R submitted that this company has published quarterly results and hence the financial data relating to the accounting year 1.4.2016 to 31.3.2017 can be collated. He submitted that this company is functionally comparable with the assessee herein. In support of this contention, the Ld A.R placed his reliance on the decision rendered by Hon'ble Delhi High Court in the case of CIT-II vs. McKinsey Knowledge Centre India P ltd (ITA No.217/2014 dated 27th March 2015).

7.2 The Ld D.R submitted that this company has been rejected by TPO on the reasoning that it is having different accounting year. If the results could be collated for the year matching with that of the assessee, then it is required to be examined as to whether this company qualifies itself in respect of other filters applied by TPO. Further, the Ld A.R also took support of Rule 10C(2)(c) of Income tax Rules, which states that the most appropriate method

has to be selected on the basis of the availability, coverage and reliability of data necessary for application of method.

7.3 We heard the parties and perused the record. With regard to the application of filter of different accounting year, the Hon'ble Delhi High Court in the above said case has expressed the following view:-

“14. The Revenue is in appeal before this Court questioning the admissibility of the above mentioned comparables while computing Arm's Length Price regarding the IT Support services after the TPO and AO rejected the above mentioned companies but was later allowed by the CIT (A) and ITAT. While the AO had confirmed the findings of the TPO, the Ld. CIT(A) after considering the Assessee's submissions accepted all the four companies rejected by the TPO. The revenue submits that Fortune Infotech Ltd. was correctly rejected by TPO because the company had different financial year ending on December, 2006, whereas Assessee's financial year ended on March, 2006. There is nothing shown to the court that supports the revenue's argument that the ITAT fell into error in holding that if a comparable is following different financial year then the same cannot be included in the list of comparables selected for benchmarking the international transaction. Therefore, the ITAT has held that if the comparable is functionally same as that of tested party then same cannot be rejected merely on the ground that data for entire financial year is not available. **If from the available data on record, the results for financial year can reasonably be extrapolated then the comparable cannot be excluded solely on the ground that the comparables have different financial year endings.**”

In view of the above said decision rendered by Hon'ble Delhi High Court, we accept the contentions of Ld A.R that this company could not have been rejected by the TPO merely for the reason that it follows different accounting year, when the financial year results for the period matching with that of the assessee could be collated. However, as submitted by Ld D.R, it is required to be examined as to whether this company gets itself qualified in other filters applied by the TPO also. Accordingly, we are of the view that this comparable company needs to be examined afresh at the end of AO/TPO. Accordingly, we restore this comparable company to the file of AO/TPO for examining it afresh.

8. The assessee seeks exclusion of M/s Infosys BPO and M/s MPS Ltd.

8.1 With regard to M/s Infosys BPO Ltd, the Ld A.R submitted that this company is engaged in providing high-end integrated services by assisting its clients in improving their competitive positioning by managing their business processes in addition to providing increased value. The Ld A.R submitted that the assessee herein is merely providing low-end services to its AEs bearing minimal risks. The services provided by the assessee are routine back office support services to its AEs. On the contrary, M/s Infosys BPO Ltd is providing high end services in order to optimize business process of its clients. The nature of services provided by this company include:-

- (a) Sourcing and procurement outsourcing services
- (b) Analytics and customer services
- (c) Finance and accounting
- (d) Legal process outsourcing
- (e) Human resources outsourcing services
- (f) Sales and fulfillment related services
- (g) Digital business services
- (h) Banking financial services and insurance
- (i) Health care
- (g) Energy and Utilities.

He further submitted that the turnover of this company is Rs.2,940 crores, which is very much higher than the turnover of Rs.347 crores achieved by the assessee. He submitted that this company is a group company of M/s Infosys group, which is an industrial giant and it derives benefits significantly from the brand value, viz., brand name of "Infosys". The presence of brand commands premium price and the customers would be willing to pay any price for the services offered by such companies. Further, this company possesses significant intangible assets in the form of goodwill. It has also incurred huge selling and marketing expenses to the tune of Rs.156 crores, where as the assessee herein is a captive service provider. This company is also heavily investing in implementing "Robotics Process Automation. Accordingly, he submitted that this company cannot be considered as a comparable company with the assessee. The Ld A.R also took support of various decisions, wherein

it has been held that M/s Infosys BPO cannot be taken as a comparable company for a captive low end service provider.

8.2 The Id D.R submitted that the TPO has found this company as functionally comparable one. He submitted that the TPO has not applied “Brand value” filter while selecting comparable companies. He further submitted that this company’s margin is only 24.72%, which proves that this company has not gained on account of existence of brand value.

8.3 We heard rival contentions on this issue and perused the record. The following observations made by the Special bench of Tribunal in the case of Maersk Global Centres (India) Private Limited (ITA No.7466/Mum/2012) are relevant here:-

“.....In our opinion, the answer to this question will depend on the facts and circumstances of each case inasmuch as if the assessee company, on the basis of its own functional profile, is found to have provided to its AE the low-end back office support services like voice or data processing services as a whole or substantially the whole, the companies providing mainly high-end services by using their specialized knowledge and domain expertise cannot be considered as comparables.”

The Ld A.R placed his reliance on the above said observations made by the Special bench and submitted that the assessee is providing low end back officer support services like voice or data processing services and hence it cannot be compared with the company providing high-end services by using specialized knowledge and domain expertise. In the case of M/s Acuity Knowledge Centre (India) P Ltd vs. DCIT (ITA No.2869/Bang/2017 dated 28th February, 2022), the Bangalore bench of Tribunal has held this company as not comparable for a low end back office support service provider. The relevant observations made by the Tribunal are extracted below:-

“8. As far as comparability of Infosys BPO Ltd is concerned, we find factual position is that this company provides a gamut of services that includes sourcing and procurement, customer services, financial and accounting, legal process outsourcing, sales & fulfillment, analytics, business platform, business transformation services, human resources outsourcing etc. Services such as analytics, human source outsourcing, which are not comparable with the assessee. This company is a market leader. The company should be rejected

as it is an established player and also a market leader and operates as a full-fledged risk bearing entrepreneur. The company has a huge turnover of Rs.1861 crores and hence not comparable to the assessee. It has significant selling, marketing and brand building expenses, brand value. Infosys BPO is an industry giant and commands a very high brand value in the market and also bears all related risk and cannot be compared to the assessee which is a captive service provider. Further, since it commands a very high brand value it enjoys premium pricing. The aforesaid company is therefore directed to be excluded from the list of comparable companies.”

8.4 Though the above said decision has been rendered by Bangalore bench of Tribunal for AY 2013-14, yet the facts relating to the above said company remain the same. We have noticed that the turnover of M/s Infosys BPO was Rs.2940 crores during the year under consideration, while the turnover of the assessee was Rs.347 crores only. The Ld A.R has pointed out the nature of services rendered by M/s Infosys BPO, which has been referred to by us in the preceding paragraph. The Ld A.R submitted that the services rendered by M/s Infosys BPO are specialized services, which cannot be compared with the low end back officer support services provided by the assessee as captive service provider. The existence of brand value for M/s Infosys BPO would definitely get premium price for the services provided by it. Accordingly, we are also of the view that M/s Infosys BPO Ltd cannot be compared with the assessee herein. Accordingly, we direct the AO/TPO to exclude the same.

9. The next company, which the assessee seeks exclusion is M/s MPS Ltd. The Ld A.R submitted that this company is engaged in rendering end to end services to its clients in publishing sector, which included content creation and production services. He submitted that this company is also engaged in software services and product development. In the annual report of this company, it is reported that it is engaged in five lines of businesses, viz., (a) Content creation and development, (b) Content production and transformation, (c) Learning media solutions and customer support, (d) Order management and (e) Platform development and technology services. However, it has not given any segmental details. The platforms developed by this company are named as Digicore, MPSTrak, MPSInsight, Content Store, ScholarStor,

MPSScholarlyStats. The Ld A.R submitted that this company has got in-house platform development and technology division for publishers powered by 300+ experienced developers. Thus this company undertakes R & D Activities. The Ld A.R further submitted that this company also outsources some of its activities. The outsourcing cost to total cost works out to about 7.50%. Accordingly, the Ld A.R submitted that this company is performing different functions and also adopt different business model. Further, it is involved in developing contents with the help of high skilled personnel. Accordingly, he submitted that this company cannot be considered as a comparable company. The Ld A.R placed his reliance on various case laws.

9.1 The Ld D.R, however submitted the services provided by this company has been classified as ITES in AY 2015-16. Accordingly he submitted that this company has been rightly taken as comparable company.

9.2 We heard rival contentions on this issue and perused the record. We notice that the comparability of this company with ITES provider was examined by the co-ordinate bench in the case of M/s Emerson Electric Co (India) (P) Ltd (2020)(116 taxmann.com 640)(Mum) and it was held as under:-

“9.3 From the perusal of the annual report for the year ended 31/03/2014 of the said comparable, we find from page 707 of the paper book that the said comparable had incurred outsourcing cost of Rs. 1078.76 Crores which is included under the head "miscellaneous expenses" which goes to prove that it has got a different business model. From the various functions performed by MPS Ltd., we find that the said comparable is predominantly in the business of digital publishing which cannot be treated at par with ITeS which is the case of the assessee in ITeS segment. In this regard, we find that the reliance placed by the ld. AR on the Co-ordinate Bench decision of Bangalore Tribunal in the case of *Google (India) (P). Ltd., v. Dy DCIT [2013] 29 taxmann.com 412/55 SOT 489* is well founded wherein it was held as under:—

"16. As far as (4) Apex Knowledge Solutions Pvt. Ltd., is concerned, we find that the assessee had taken objections before the TPO that it is functionally different, as it provides services such as E-publishing knowledge based services etc. But TPO has rejected the objection on the ground the assessee has not considered the verticals or functional lines during the search process conducted by it and, therefore, it is not proper to make any objection on this basis now. We are not able to agree with the finding of the TPO as confirmed by the DRP on this issue. Merely because, the assessee itself has not considered the said

filter while making its TP study; it cannot be said that it cannot raise such an objection before the TPO. It is the TPO who has adopted this company as comparable. On such adoption, the assessee has every right to raise the objections as regards the functional differences between the assessee and comparable. It is the bounden duty of the TPO to consider the said objections in accordance with law. As brought out by the assessee, the assessee is in the IT enabled services, whereas the said company Apex Knowledge Salutation Pvt. Ltd., is in the business of E-publishing which cannot be said to be in the same line of business. The functional differences are likely to affect the profit marking capacity of both the companies. In view of the same, we are of the opinion that this company is also to be excluded from the list of comparables."

9.3.1 In view of the above, we hold that the comparable chosen by the Id. TPO, M/s. MPS Ltd., is functionally not comparable with that of the assessee and accordingly, we direct the Id. TPO to exclude the same from the list of comparables."

9.3 From the submissions made by Ld A.R, we notice that the functions performed by this company in the present year under consideration are identical in nature. The Ld A.R also pointed out that this company offers different types of services such as (a) Content creation and development, (b) Content production and transformation, (c) Learning media solutions and customer support, (d) Order management and (e) Platform development and technology services. Further it has developed different domain platforms involving specialized technologies. However, the assessee herein is a low end back officer support services provider. Accordingly, we are also of the view that this company cannot be taken as a comparable company for the assessee herein. Accordingly, we direct exclusion of this company.

10. In ground no.11 and 12, the assessee has pleaded that the AO/TPO has not granted working capital adjustment and risk adjustment. We restore this issue to the file of AO/TPO to take decision on these two issues in accordance with law.

11. In view of the above, we restore the issue of determining ALP of international transaction of provision of ITES services to the file of AO/TPO for examining the same in the light of discussions made supra.

12. The next issue urged by the assessee relates to the disallowance made u/s 14A of the Act. During the year under consideration, the assessee has earned exempt dividend income of Rs.1,53,67,756/- and it disallowed a sum of Rs.4,29,529/- u/s 14A of the Act. The AO took the view that the assessee is required to compute disallowance as per Rule 8D of I T Rules. Accordingly, he sought explanations from the assessee in this regard. The AO was not satisfied with the workings given by the assessee and accordingly computed disallowance under rule 8D at Rs.1,15,77,966/-. After giving set off of the amount of Rs.4,29,529/- made by the assessee, the AO disallowed the difference amount of Rs.1,11,48,437/-. The Ld DRP also confirmed the same.

12.1 We heard the parties on this issue and perused the record. We notice that the assessee has made investments in a group company named M/s Ventura (India) P Ltd and also in three schemes of mutual funds. The break up details of investments as on 31.3.2017 is given below:-

| | | |
|--|---|----------------|
| Ventura (India) Private Limited | - | 1,48,05,12,852 |
| HDFC Liquid fund daily dividend | - | 6,15,10,546 |
| IDFC Cash fund daily dividend | - | 6,12,88,263 |
| IDFC Money Manager fund daily dividend | - | 60,483 |
| | | ----- |
| | | 1,60,33,72,144 |
| | | ===== |

The assessee has received dividend income of Rs.92,96,786/- from Ventura (India) P Ltd and dividend income of Rs.60,70,970/- from mutual fund investments. Hence the assessee has computed disallowance to be made u/s 14A of the Act at Rs.4,29,529/- considering salary and related cost of employees of the assessee who are involved in investment decisions, other administrative and overhead costs. It is submitted that the above said computation is based on detailed workings undertaken by the assessee and the said computation has been certified by a Chartered Accountant also.

12.2 We notice that the major investment has been made by the assessee in its group company from which about 60% of dividend income has been received. The remaining dividend income has been received from the three

schemes of mutual funds. The investment made in the group company does not involve significant efforts. The investment made in mutual fund schemes also would not require much deliberations as required in the normal course of making investments in shares. Further the assessee has invested in three schemes only. Hence we are of the view that the disallowance, in the facts and circumstances of the case, is not required to be made in accordance with Rule 8D of IT Rules.

12.3 In the written submissions, the assessee has made alternative computation for disallowance u/s 14A at Rs.5,52,490/- by apportioning the common expenses between business income and exempt income in proportionate ratio. In the facts and circumstances of the case, we are of the view that this alternative computation may be accepted. Hence we hold that the AO was not justified in applying rule 8D without properly appreciating the facts surrounding this issue. Accordingly, we direct the AO to restrict the disallowance to Rs.5,52,490/- and we order accordingly.

13. In the result, the appeal filed by the assessee is partly allowed.

Order pronounced in the open court on 18.08.2022.

Sd/-
(RAHUL CHAUDHARY)
JUDICIAL MEMBER

Sd/-
(B.R. BASKARAN)
ACCOUNTANT MEMBER

Mumbai; Dated : 18/08/2022

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent
3. The CIT(A)
4. CIT
5. DR, ITAT, Mumbai
6. Guard File.

//True Copy//

BY ORDER,

(Assistant Registrar)
ITAT, Mumbai

PS