IN THE INCOME TAX APPELLATE TRIBUNAL

"K" BENCH, MUMBAI

BEFORE SHRI PRAMOD KUMAR, VICE PRESIDENT AND

SHRI SANDEEP SINGH KARHAIL, JUDICIAL MEMBER

IT(TP)A No.1941/Del./2015

(Assessment Year : 2010–11)

Hapag–Lloyd Global Services Pvt. Ltd.
[Successor of CSAV Group (India) Pvt. Ltd.]
402–403, Dosti Pinnacle, Plot no.E–7
Road no.22, Wagle Estate, Thane (West)
Thane 400 604 PAN – AACCC1314L ……. Appellant

v/s

Dy. Commissioner of Income Tax
Circle–1(1)(1), Gurgaon .....Respondent

Assessee by : Shri Rajan R. Vora
Shri Pranay Gandhi
Revenue by : Ms. Samruddhi D. Hande

Date of Hearing – 13/07/2022	Date of Order – 10/10/2022

O R D E R

PER SANDEEP SINGH KARHAIL, J.M.

The present appeal has been filed by the assessee challenging the impugned final assessment order dated 30/01/2015, passed under section 143(3) r/w section 144C of the Income Tax Act, 1961 ('*the Act*'), for the assessment year 2010–11.

2. Pursuant to the approval of scheme of amalgamation of CSAV Group (India) Pvt. Ltd. with Hapag-Llyod Global Services Private Ltd by the Hon'ble jurisdictional High Court and Hon'ble High Court of Punjab and Haryana,

assessee filed revised Form No. 36 and grounds of appeal, vide letter dated 10/12/2020, which were taken on record.

3. The grounds of appeal raised by the assessee are as under:–

"1. On facts and in law, the Ld. Deputy Commissioner of Income-Tax, Circle 1(1), Gurgaon (Ld. AO)erred in passing the impugned assessment order dated 30 January 2015 without considering directions of the Hon'ble Dispute Resolution Panel-III, New Delhi ("Hon'ble DRP) and computing an adjustment of Rs. 2,76,42,429 to the total income of the Assessee on account of difference in the arm's length price of international transactions pertaining to Back Office Support Services segment.

2. On facts and in law, the Ld. AO/Ld. Additional Commissioner of Income-tax, Transfer Pricing Officer-I (3), New Delhi (Ld. TPO)and the Hon'ble DRP erred in violating the provisions of Rule 10B(2) by selecting comparable companies as below, without considering the differences in the functions performed, assets employed and risks assumed by such companies vis-à-vis the Assessee, thereby resorting to cherry picking of comparables:

- *Accentia Tech. Ltd.;*
- *E4e Healthcare Services Pvt. Ltd.;*
- *Fortune Infotech Limited;*
- *Infosys BPO Limited;*
- *Igate Global Solutions Limited;*
- *TCS E-Serve International Ltd.; and*
- *TCS E-Serve Ltd.*

3. On facts and in law, the Ld. AO/Ld. TPO and Hon'ble DRP violated the provisions of Rule 10B(2) by rejecting the following comparables selected by the Assessee in the TP study:

- *Cameo Corporate Services Limited;*
- *A O K In-House BPO Services Ltd.;*
- *In House Productions Limited;*
- *Aditya Birla Minacs Worldwide Ltd;*
- *Optimus Global Services Limited;*
- *Omega Healthcare Management Services Pvt Ltd.;*
- *Delta Services (1) Pvt Ltd.;*
- *Informed Technologies India Ltd.,*
- *Sparsh BPO Services Ltd.: and*

- *Timex Group India Ltd.*

4. On the facts and in law, thel.d. AO/Ld. TPO and Hon'ble DRPerred in not allowing risk adjustment to the Assessee, thereby contravening the provisions of Rule 10B(1)(e)(iii) and 10B(3) of the Rules.

5. On the facts and in law, the Ld. AO/Ld. TPO and Hon'ble DRPerred in disregarding the Assessee's use of multiple year/ prior years' data in contravention of the provision of section 92C of the Income-Tax Act, 1961 (the Act) read with Rule 10B and Rule 10D of the Income Tax Rules, 1962 ("the Rules").

6. On the facts and in law, the Ld. AO/Ld. TPO and Hon'ble DRPerred in disregarding the doctrine of impossibility of performance in contravening Section 92D of the Act read with Rule 10D(4) of the Rules, which mandate the use of contemporaneous data for the determination of arm's length price ("ALP") of international transactions.

7. On the facts and in law, the Ld. AO erred on facts and in law in proposing an adjustment of Rs. 5,523,685 to the total income of the Assessee on account of overdue receivables from its Associated Enterprises (AEs) without considering directions of the Hon'ble DRP.

7.1 Without prejudice, the Ld. AO/Ld. TPO and Hon'ble DRP erred on facts and in law in applying an ad-hoc interest rate of 13.38% for computing the interest on overdue receivables from its A.Es.

8 On the facts and in the circumstances of the case, the Ld. AO erred in initiating penalty proceedings u/s 271(1)(c) of the Act.

9 On the facts and in the circumstances of the case, the Hon'ble DRP/ Ld. AO/ Ld. TPO erred in levying interest under section 234B and 234C of the Act.

The grounds of appeal herein above are independent and without prejudice to each other. The objections embodied in the above grounds are mutually exclusive."

4. Vide application dated 23/03/2021, assessee sought admission of following additional grounds of appeal:

"Based on the facts and circumstances of the case and in law:

<u>Transfer pricing adjustment made in respect of notional interest on overdue receivables from AE</u>

7.1 erred in not appreciating the fact that the overdue receivable from AEs should be aggregated with principal transaction of provision of IT-Enabled Services and vessel planning service as it is directly and inextricably linked with it.

7.2 erred in not appreciating the fact that even after reducing the notional interest (as computed by TPO) from the operating revenue, the Appellant's margin is still higher than the average margin earned by the comparable companies and therefore no separate adjustment on account of interest on overdue receivable is warranted:

7.3 erred in not allowing working capital adjustment claimed by the Appellant vis-à-vis comparable companies, which would factor the impact of overdue receivables from AES and on consideration of the same, no separate adjustment on account of interest on outstanding receivables is warranted.

7.4 Without prejudice to above, the Appellant prays that even if the notional interest is to be impute on overdue receivables, the same should be calculated using LIBOR rates."

5. The assessee vide another application dated 15/06/2021, filed following revised / modified grounds of appeal, which, inter-alia, also include the aforesaid additional grounds of appeal:

"On the facts and circumstances of the case and in law, the Deputy Commissioner of Income-tax Circle-1(1) (AO) Additional Commissioner of Income-tax, Transfer Pricing Officer-1(3), New Delhi (TPO) and the Dispute Resolution Panel-, New Delhi (Hon'ble DRP), has on facts and in law:

Transfer Pricing adjustment in respect of IT enabled support services (ITeS') segment INR 2,76,42,429/–:

1. erred in making an adjustment of INR 2,76,42,429 on account difference in the arm's length price of international transaction pertaining to ITeS segment:

2. erred in violating the provisions of Rule 10B(2) by selecting comparable companies as below, without considering the differences in the functions performed, asset employed and risk assumed by such companies vis-à-vis the Appellant, thereby resorting to cherry picking of comparable companies:

- *Accentia Technologies Ltd,*
- *Infosys BPO Limited;*
- *TCS E-Serve International Ltd, and*
- *TCS E-Serve Ltd.*

3. erred in not making suitable working capital adjustment while computing operating margins for the Appellant vis-à-vis the comparables;

Transfer Pricing adjustment in respect of Overdue Receivables - INR 30,36,780/-:

4. erred in making adjustment of INR 30,36,780 on account of overdue receivables from its Associated enterprises ('AE');

5. erred in applying adhoc interest rate of 13.38% for computing the interest on interest on overdue receivables from its A.E.;

Additional grounds (7.1 to 7.4) filed vide letter dated 23 March 2021

6. erred in not appreciating the fact that the overdue receivable from AEs should be aggregated with principal transaction of provision of ITeS and vessel planning support service as it is directly and inextricably linked with it;

7. erred in not appreciating the fact that even after reducing the notional interest (as computed by learned TPO) from the operating revenue, the Appellant's margin is still higher than the average margin earned by the comparable companies and therefore no separate adjustment on account of interest on overdue receivable is warranted;

8. erred in not allowing working capital adjustment claimed by the Appellant vis-à-vis comparable companies, which would factor the impact of overdue receivables from AES, and on consideration of the same, no separate adjustment on account of interest on overdue receivables is warranted.

9. Without prejudice to above, the Appellant prays that even if the notional interest is to be imputed on overdue receivables, the same should be calculated using LIBOR rates.

Initiating penalty proceedings under section 271(1)(c) of the Act

10. erred in initiating penalty proceedings under section 271(1)(c) of the Act.

Levy interest under section 234B and 234C of the Act

11. erred in levying interest under section 234B and 234C of the Act."

6. Since, issues raised by way of additional grounds are legal issues, which can be decided on the basis of material available on record, we are of the view that same can be admitted for consideration and adjudication in view of the ratio laid down by the Hon'ble Supreme Court in NTPC Ltd v/s CIT: 229 ITR 383. Accordingly, the revised grounds of appeal were taken on record. During the course of hearing, submissions were made by both the sides as per the aforesaid revised grounds of appeal.

7. Ground No. 1 raised in assessee's appeal is general in nature and therefore, same need no separate adjudication.

8. The issue arising in ground no.2 is pertaining to transfer pricing adjustment qua the comparables

9. The brief facts of the case, as emanating from record, are: The assessee is primarily engaged in providing vessel planning support services and other back office support services to CSAV group's shipping companies and agencies subsidiaries. For the year under consideration, assessee e-filed its return of income on 23/09/2010 declaring income of Rs. 1,38,37,911. During the year under consideration, the assessee entered into following international transactions with its associated enterprises:

Sl. No.	*Particulars*	*Amount (in Rs.)*	*Method*
1	*Provision of vessel planning support services*	*7,34,17,574*	*TNMM*
2	*Provision of back office support services*	*19,91,10,736*	*TNMM*
3	*Reimbursement of expenses*	*17,56,304*	*TNMM*
4	*Recovery against expenses*	*1,27,211*	*CUP*

10. Assessee primarily acts as a captive vessel planning and IT enabled back office support services provider for its associated enterprises. In respect of international transaction pertaining to '*IT enabled back office support services*', assessee performed following functions:

"5.2.2 Back Office Support Services

CSAV India provides various back office support services to Its AEs. The various processes which are being handled by CSAV India, as part of back office support services are as under:

- *Purchase to Payment Control (PTP) • Cost Control and inter-modal administration*
- *UCR Processing*
- *Third Party Claims Tracking (Log)*
- *Empty Overdue*
- *COD Processing*
- *Inter-modal administration*
- *Logistics Administration*
- *Data quality*
- *Documentation Control*
- *Customer Database Administration (CDA)*
- *24 Hours US custom regulations*
- *Transport folder control*
- *US Trade Administration*
- *Inland Routing*
- *BL production*
- *Arrival Notice*
- *OTC (Freight Receivables)*
- *Demurrage*
- *EZ Tariff Maintenance*
- *Customer Relationship Management (CRM)*
- *Insurance and Claims"*

11. As per transfer pricing study report, the assessee used Transactional Net Margin Method ("*TNMM"*) as the most appropriate method with Profit Level

Indicator ("*PLI*") of Operating Profit to Total Cost ("*OP/TC*"), for benchmarking this transaction. By considering itself as the tested party, assessee identified 15 comparable companies with average PLI of 14.27%. As the assessee computed its own PLI at 14.93%, accordingly, it claimed that the international transaction of '*IT enabled back office support services*' is at arm's length price ("*ALP*").

12. The Assessing Officer ('*AO*') made reference to Transfer Pricing Officer ('*TPO*') for determination of ALP of the aforesaid international transaction. During the transfer pricing assessment proceedings, assessee furnished updated single year margins of comparables including the working capital adjusted arithmetic mean. The TPO vide order dated 21/01/2014 passed under section 92CA(3) of the Act selected following 9 companies as comparables for benchmarking the international transaction pertaining to 'IT enabled back office support services', after modifying the filters selected by the assessee and proposing some new filters:

Sr. no.	Comparable	OP/OC (Without Forex)
1.	Accential Tech. Ltd.	43.07%
2.	Cosmic Global Ltd.	18.28%
3.	E4e Healthcare Services P. Ltd.	31.03%
4.	Fortune Infotech Limited	22.80%
5.	Igate Global Solutions Limited	24.54%
6.	Infosys BPO Limited	31.46%
7.	Satyam BPO Limited	–10.60%
8.	TCSE – Serve International Ltd.	54.03%
9.	TCSE – Serve Ltd.	63.42%
	Average	30.89%

13. The average operating profit to total cost of aforesaid comparables selected by the TPO was computed at 30.89%. By applying the arm's length margin, the TPO proposed an upward adjustment of Rs. 2,76,42,429, in respect of international transaction of '*IT enabled back office support services'*. The AO passed the draft assessment order under section 143(3)/144C of the Act, inter-alia, after incorporating the adjustment proposed by the TPO.

14. The assessee filed detailed objections before the learned Dispute Resolution Panel ('*learned DRP*') against the findings of TPO on selection of comparables for benchmarking the international transaction pertaining to '*IT enabled back office support services*'. The learned DRP vide its directions dated 16/12/2014, issued under section 144C (5) of the Act, inter-alia, rejected the objections filed by the assessee. The learned DRP rectified the operating margin of 2 comparables resulting in reduction of arm's length margin to 29.42% and transfer pricing adjustment to Rs 2,50,95,808. However, the AO passed the impugned final assessment order dated 30/01/2015 under section 143 (3)/144C of the Act without correctly incorporating the transfer pricing adjustment pursuant to learned DRP's directions. Being aggrieved, the assessee is in appeal before us.

15. During the course of hearing, learned Authorised Representative ('*learned AR*') prayed for exclusion of Accentia Technologies Ltd, Infosys BPO Ltd, TCS E-Serve International Ltd and TCS E-Serve Ltd for benchmarking the international transaction pertaining to '*IT enabled back office support services*' and submitted that if aforesaid companies are excluded from the list of comparables then ITeS segment of assessee will be at arm's length.

(i) Accentia Technologies Ltd

16. The first comparable under dispute is Accentia Technologies Ltd for benchmarking the international transaction pertaining to '*IT back office support services*'. Accentia Technologies Ltd was selected as a comparable by the TPO vide order passed under section 92CA(3) of the Act on the basis that the company is into healthcare and receivables cycle management which predominantly are ITeS services and passes all the filters. The TPO further held that there is no abnormal fluctuation in the profit earning capacity of this company for the year under consideration and the alleged acquisition has not affected the profitability of this company. The DRP vide its directions rejected the objections filed by the assessee against inclusion of Accentia Technologies Ltd as a comparable and held that FAR profile of the company is essentially similar to that of assessee. Being aggrieved, the assessee is in appeal before us.

17. During the course of hearing, learned AR by referring to the annual report of this company, forming part of the paper book, submitted that it is engaged in KPO services and is thus functionally not comparable to the assessee. The learned AR also submitted that there was extraordinary event of amalgamation, during the year, which renders this company as non-comparable to the ITeS segment of assessee. The learned AR placed reliance upon various judicial precedents in support of its submissions for exclusion of this company as a comparable. On the other hand, learned Departmental

Representative ('learned DR') vehemently relied upon the orders passed by the lower authorities.

18. We have considered the rival submissions and perused the material available on record. In the present case, functional profile of the assessee in respect of IT enabled back office support services is not in dispute. From the perusal of annual report of Accentia Technologies Ltd, forming part of the paper book at page 508 – 534 and financials at page 183 – 202, we find that Accentia Technologies Ltd in Healthcare Receivables Cycle Management provides diversified services including medical transcription, medical coding, billing and receivables management using Software as a Service (SaaS) model. Under medical coding, the company claims that its margin is on higher side when compared to medical transcription and company has claimed to have developed a sizeable number of certified coders who could straightaway be deployed in outsourced medical coding work. Further, as per segmental information the company is operating in only one segment despite being engaged in diversified activities. Thus, in view of the above, we are of the considered opinion that the functions rendered by Accentia Technologies Ltd under Healthcare Receivables Cycle Management are not comparable to assessee's IT enabled back office support services. Further from the notes to accounts (B)(1), we find that though Asscent Infoserve Pvt Ltd (subsidiary of the company) was amalgamated with Accentia Technologies Ltd w.e.f. 01/04/2008 vide amalgamation scheme sanctioned by the Hon'ble High Courts in the year under consideration, however, the scheme has been given effect to in the accounts of this year. We further find that assets, liabilities and

accumulated reserves of the erstwhile company have been incorporated in the books of accounts of Accentia Technologies Ltd. Further, goodwill as specified in the scheme of amalgamation has also been incorporated in the books of accounts of Accentia Technologies Ltd. At page 197 of the paper book, the company claims as follows "*In view of the above amalgamation being effective the figures for the year ended 31/03/2010 are inclusive of the figures relating to the amalgamating company and thus are not comparable with those of the previous year*". From the above, it is thus evident that extraordinary event relating to amalgamation has impacted the financials of this company.

19. We find that the coordinate bench of the Tribunal in Agilyst Consulting Pvt Ltd vs DCIT, in IT(TP)A No. 3999/Mum./2017, for assessment year 2010–11, vide order dated 14/10/2019, while directing exclusion of Accentia Technologies Ltd, observed as under:

> *"8. We have considered rival submissions and perused material on record. The annual report of this comparable placed in the paper book indicates that the service provided by the company, such as, medical transcription is in the nature of KPO services. Though, it is into diversified activities, however, segmental information is not available in the annual report of the company. Further, extra ordinary events relating to acquisition and amalgamation in the company might have impacted the profitability. Thus, from the aforesaid analysis of facts it becomes clear that the company is not only functionally dissimilar to the assessee, but various other factors also make this company non–comparable to the assessee. It is relevant to observe, considering the above narrated facts different Benches of the Tribunal have held that this company is not a comparable to ITES service provider. Pertinently, the decision of the Tribunal in case of Ameriprise India Pvt. Ltd. (supra), B.C. Management Services Pvt. Ltd., BNY Mellon International Operations (supra) and Aptara Technologies Pvt. Ltd. (supra) have been approved by the Hon'ble High Courts. Since, many of these decisions pertained to the very same assessment year, consistent with the view taken in these decisions, we hold that this company cannot be a comparable to the assessee."*

20. In view of the above, we are of the considered opinion that Accentia Technologies Ltd is not comparable to the assessee for benchmarking the

international transaction pertaining to '*IT enabled back office support services*' and accordingly, we direct the TPO/AO to exclude this company.

(ii) Infosys BPO Ltd.

21. The next comparable under dispute is Infosys BPO Ltd. for benchmarking the international transaction pertaining to '*IT enabled back office support services*'. Infosys BPO Ltd was selected as a comparable by the assessee in its transfer pricing study report. During the transfer pricing assessment proceedings, assessee sought exclusion of this company, inter-alia, on the basis that selling and marketing expenses of the company account for 6.96% of its total revenue and company has goodwill which constitutes 9.1% of its total fixed assets. Further, Infosys BPO Ltd has acquired the membership interest of McCamish Systems LLC. However, the TPO vide order passed under section 92CA(3) of the Act did not accept the submissions of the assessee and considered Infosys BPO Ltd as a comparable. The DRP vide its directions rejected the objections filed by the assessee against inclusion of Infosys BPO Ltd as a comparable and held that FAR profile of the company is essentially similar to that of assessee. The DRP also noted that the assessee had itself taken this company as comparable. Being aggrieved, the assessee is in appeal before us.

22. During the course of hearing, learned AR submitted that Infosys BPO Ltd is engaged in high end software services and owns IPs. The learned AR further submitted that Infosys BPO Ltd has a high brand value and operates on a huge economic upscale and able to command and generate better profits. Learned

AR also submitted that even if assessee has taken Infosys BPO Ltd as a comparable in its transfer pricing study report, considering the vast differences with the tested party, Infosys BPO Ltd should be excluded. On the other hand, learned DR vehemently relied upon the orders passed by the lower authorities.

23. We have considered the rival submissions and perused the material available on record. We find that Hon'ble Delhi High Court in PCIT vs EVALUESERVE SEZ (Gurgaon) Pvt Ltd., in ITA No. 241 of 2018, vide judgment dated 26/02/2018, dismissed the appeal filed by the Revenue and upheld the conclusion reached by the coordinate bench of the Tribunal in, inter-alia, excluding Infosys BPO Ltd on the basis of its high brand value and consequent higher profitability. The relevant observations of Hon'ble Delhi High Court in aforesaid judgment are as under:

> *"5. This Court notices that as far as the exclusion of three comparables – M/s. TCS E-Serve Limited; M/s. TCS E-Serve International Limited and M/s. Infosys BPO Ltd. is concerned, the ITAT was cognizant of and took note of the circumstances that these entities had a high brand value and, therefore, were able to command greater profits; besides, they operated on economic upscale. This approach cannot be faulted having regard to the decision of this Court in Pr. Commissioner of Income Tax v. B.C. Management Services Pvt. Ltd. 2018 (89) Taxman.com 68 (Del), which reads as follows:*
>
> > *"13. The exclusion of second comparable ICRA Techno Analytics Ltd. was on the basis that it had engaged itself in processing and providing software development and consultancy and engineering services/web development services. The reasons for execution were functional dissimilarities and that segmental data were unavailable. Again the findings of the ITAT are reasonable and based on record. The third comparable that the AO/TPO excluded is TCS E-serve. The ITAT observed that though there is a close functional similarity between that entity and the assessee, however, there is a close connection between TCS E-serve and TATA Consultancy Service Ltd. which was high brand value; that distinguished it and marked it out for exclusion. The ITAT recorded that the brand value associated with TCS Consultancy reflected impacted TCS E-serve profitability in a very positive manner. This inference too in the opinion of Court, cannot be termed as unreasonable. The rationale for exclusion is therefore upheld. The assessee was aggrieved by the inclusion of Accentia a Software Development Company. The Revenue is aggrieved by the exclusion of Accentia from the TP analysis. The DRP had directed its deletion. We observe that the ITAT has noticed the unavailability of the segmental data so far as*

> *these comparables are concerned. Furthermore, the functionality of this entity was concerned, it is different from that of the assessee; Accentia was engaged in KPO services in the healthcare sector.*
>
> *14. In view of the above findings, this Court is of the opinion that no substantial question of law arises. The appeals are dismissed."*

24. Insofar as the observation of TPO as well as learned DRP that assessee is seeking exclusion of its own comparable, it is pertinent to note that Special Bench of the Tribunal in DCIT vs Quark Systems Private Limited, [2010] 38 SOT 307 (Chd.) (SB) held that there is no estoppel on the taxpayer from pointing out that a particular company has been wrongly taken as a comparable. We further find that the aforesaid decision rendered by Special Bench of the Tribunal has been affirmed by Hon'ble Punjab and Haryana High Court in CIT vs Quark Systems Private Limited, [2011] 244 CTR 542 (P&H). Similarly was held by Hon'ble jurisdictional High Court in CIT vs Tata Power Solar Systems Ltd, [2017] 245 Taxman 93 (Bombay). Thus, respectfully following the aforesaid decision of Hon'ble Delhi High Court in EVALUESERVE SEZ (Gurgaon) Pvt Ltd. (supra), we direct the TPO/AO to exclude Infosys BPO Ltd for benchmarking the international transaction pertaining to '*IT enabled back office support services*'.

(iii) <u>TCS E-Serve International Ltd.</u>
(iv) <u>TCS E-Serve Ltd.</u>

25. The last two comparables under challenge are TCS E-Serve International Ltd and TCS E-Serve Ltd. for benchmarking the international transaction pertaining to '*IT enabled back office support services*'. Both these companies were selected as comparable by the TPO vide order passed under section 92CA(3) of the Act, inter-alia, on the basis that services offered by these

companies are in the nature of IT enabled services only. The DRP vide its directions rejected the objections filed by the assessee against inclusion of TCS E-Serve International Ltd and TCS E-Serve Ltd as comparable and held that FAR profile of these companies is essentially similar to that of the assessee. Being aggrieved, the assessee is in appeal before us.

26. During the course of hearing, learned AR submitted that both these companies are engaged in high end software services and own IPs. It was further submitted that both these companies have high brand value and operates on huge economic upscale and able to command and generate better profits. The learned AR also submitted that both these companies have also made payment for Tata Brand Equity contribution to parent entity. On the other hand, learned DR reverently relied upon the orders passed by the lower authorities.

27. We have considered the rival submissions and perused the material available on record. We find that Hon'ble Delhi High Court in PCIT vs EVALUESERVE SEZ (Gurgaon) Pvt Ltd., vide judgment dated 26/02/2018, as noted above, dismissed the appeal filed by the Revenue and upheld the conclusion reached by the coordinate bench of the Tribunal in, inter-alia, excluding TCS E-Serve International Ltd and TCS E-Serve Ltd on the basis of its high brand value and consequent higher profitability. Thus, respectfully following the aforesaid decision of Hon'ble Delhi High Court in EVALUESERVE SEZ (Gurgaon) Pvt Ltd. (supra), we direct the TPO/AO to exclude TCS E-Serve International Ltd and TCS E-Serve Ltd for benchmarking the international transaction pertaining to '*IT enabled back office support services*'.

28. As a result, ground No. 2 raised in assessee's appeal is allowed.

29. The issue arising in ground No. 3 is pertaining to denial of working capital adjustment claimed by the assessee vis-à-vis comparable companies.

30. The brief facts of the case, pertaining to this issue, are: As noted above, during the course of transfer pricing assessment proceedings, assessee provided the updated single year margin of comparables in respect of back office support services segment. In the computation of updated margin of comparables, which forms part of the paper book at page 114, assessee also provided working capital adjusted net cost plus margin of the comparable companies and arrive at the arithmetic mean of 11.72%. The TPO vide order passed under section 92CA(3) of the Act denied the claim of grant of working capital adjustment as sought by the assessee. Before the learned DRP, the assessee raised no objection in this regard.

31. During the course of hearing, learned AR submitted that as per Rule 10 B of Income Tax Rules, a transaction can be considered as comparable, if reasonably accurate adjustment can be made to eliminate differences that are likely to materially affect the price or the cost or profit between a controlled and uncontrolled transaction. Thus, it was submitted that in case there are significant differences in the working capital between the tested party and the comparable companies, appropriate adjustment may be required for such difference in determining the arm's length price. On the other hand, learned DR, vehemently relied upon the orders passed by the TPO.

32. We have considered the rival submissions and perused the material available on record. We find that Rule 10 B(1)(e)(iii) of the Income Tax Rules, provides as under:

> *"(iii) the net profit margin referred to in sub-clause (ii) arising in comparable uncontrolled transactions is adjusted to take into account the differences, if any, between the international transaction [or the specified domestic transaction] and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of net profit margin in the open market;"*

33. We find that coordinate bench of the Tribunal in Mercer consulting (India) Pvt. Ltd vs DCIT, in ITA No. 966/Del/2014, vide order dated 06/06/2014, observed as under:

> *"16.2. Having heard the rival submissions and perused the relevant material on record, we find that the viewpoint canvassed by the authorities below is sans merit. Working capital adjustment is ordinarily confined to inventory, trade receivables and trade payables. If a company carries on high trade receivables, it would mean that it is allowing its customers a relatively longer period to pay their amount which will result into higher interest cost and the resultant less profit. Similarly, by carrying high trade payables, a company benefits from a relatively longer period available to it to pay back its suppliers which lowers the interest cost and accelerates profits. To have a level playing field, it is sine qua non that the working capital adjustment should be carried out to bring two otherwise comparable cases at par with each other. We are unable to comprehend any reason or rhyme to restrict the grant of working capital adjustment only in the case of manufacturers or traders. What is true for these categories of businesses, is fully true for a service provider as well. It is a different matter that in the case of service provider, no working capital adjustment would be required towards higher or lower inventory, but the same may be warranted in respect of higher or lower trade receivables/payables. Since the authorities below have rejected the assessee's contention for grant of working capital adjustment at the threshold, which in our considered opinion is not correct, we set aside the impugned order and remit the matter to the file of the TPO/AO for examining the assessee's claim for grant of working capital adjustment on merits and thereafter, allow the same, if it is available. Needless to say, the assessee will be allowed an adequate opportunity of hearing."*

34. Thus, in view of the above, we are of the considered opinion that the claim of the assessee for working capital adjustment cannot be rejected at the

outset. The impugned order on this issue is set aside and the matter is remanded to the AO/TPO for verifying the calculation so made by the assessee in support of its claim of working capital adjustment, and then allow it as per law, after affording reasonable opportunity of being heard to the assessee. As a result, ground No. 3 is allowed for statistical purpose.

35. The issue arising in grounds No. 4 to 9 is pertaining to transfer pricing adjustment on account of overdue receivables from its associated enterprises.

36. The brief facts of the case, as emanating from the record, are: During the course of transfer pricing proceedings, the assessee was asked to submit the details of realisation of various invoices raised by it, during the year under consideration. It was noticed that there was lot of delay in the realisation of various invoices. Accordingly, the TPO proceeded to benchmark the alleged transaction of extending interest free credit to the associated enterprises and proposed to determine the ALP of interest on outstanding receivables beyond the normal credit period of 30 days. The TPO vide order passed under section 92CA(3) of the Act treated the aforesaid transaction as an international transaction by placing reliance upon Explanation (1) (c) to section 92B of the Act. The TPO, further, treated the outstanding receivables as deemed loans extended by the assessee to its associated enterprise. The TPO also rejected the plea of the assessee of aggregation of international transactions and held that outstanding receivables is a separate class of transaction, which requires separate analysis. The TPO by applying the SBI PLR of 11.88%, for the financial year 2009 – 10, + 1.5% markup, computed the arm's length interest on receivables at Rs. 55,23,685. The learned DRP vide its directions, inter-alia,

rejected the objections filed by the assessee and upheld the approach of TPO of separately benchmarking the alleged transaction of outstanding receivables from associated enterprises. The learned DRP, however, directed the AO/TPO to grant the relief to the assessee in respect of notional interest to be received on advance payments received from associated enterprises. Accordingly, the TPO vide order dated 24/02/2015, while giving effect to DRP's directions reduced the transfer pricing adjustment on account of outstanding receivables to Rs. 30,36,780. However, the AO passed the impugned final assessment order without correctly incorporating the transfer pricing adjustment pursuant to learned DRP's directions. Being aggrieved, assessee is in appeal before us.

37. Having heard the rival submissions and perused the material available on record, we find that the delay is in respect of realisation of invoices raised by the assessee for provisions of services to the associated enterprises. Thus, the delay of receivables is only incidental to principal transaction, i.e. provision of services. As noted above, the assessee provided provision of vessel planning support services and back office support services to its associated enterprises. Insofar as the provision of vessel planning support services is concerned, no dispute was raised by the TPO in respect of TNMM benchmarking conducted by the assessee and the transaction was accepted to be at arm's length. However, only in respect of provision of back office support services, the TPO, inter-alia, proposed the adjustment, which after exclusion of aforesaid comparables under challenge in present appeal, will also be at arm's length on TNMM basis.

38. We find that coordinate bench of the Tribunal in Rusabh Diamonds vs ACIT, (2016) 158 ITD 564 (Mumbai) observed as under:

> *"12. In our considered view, even if we proceed on the basis that Explanation to Section 92B is Indeed retrospective in effect and it does cover delay in realization of debts, as long as sale is benchmarked on TNMM basis, as in this situation before us, there cannot be any occasion to make a separate adjustment for delay in realization of debts. The reason is that the interest income is an integral part of the PBIT inasmuch as interest income, in cases other than finance companies, is required to be included in the 'other income' and thus affects the profit before interest and taxes. While profit before interest and taxes does not take into account interest expenditure, it does take into account interest income' because the interest income is part of the 'other income, under pre amended as well as post amended schedule VI to the Companies Act, which is duly taken into account into computation of PBIT. In a way PBIT is a misnomer, as while PBIT does not take into account interest expenditure, it does take into account interest income- appearing in the other income. Once the profitability, as per PBIT, is found to be comparable, there cannot be a separate adjustment for interest income on delayed realization which is an integral part of the PBIT figure.*
>
> *13. It is in this background that we may refer to the observations made by a coordinate bench of this Tribunal, In the case of Micro Ink Ltd Vs ACIT (supra), as follows:*
>
> > *"7. We find that, as evident from audit report on form 3CEB (pages 39 to 52 of the paper-book), the arm's length price of exports to the AES, including Micro USA, has been determined on the basis of the transactional net margin method (TNMM). By way of a note at page 51, it is specifically stated that "further, the said amount of Rs 2478.26 millions has also been determined/ computed by the assessee having regard to the arm's length price on application of Transactional Net Margin Method (TNMM), on aggregation of transactions, as prescribed under section 92C of the Income Tax Act, 1961". In this backdrop, we can usefully refer to the decision of Hon'ble Delhi High Court, in the case of Sony Ericsson Mobile Corporation Pvt Ltd Vs ACIT [(2015) 374 ITR 118(Del)] wherein Their Lordships had, inter alia, observed as follows:*
> >
> > *"Where the Assessing Officer/TPO accepts the comparables adopted by the assessed, with or without making adjustments, as a bundled transaction, it would be illogical and improper to treat AMP expenses as a separate international transaction, for the simple reason that if the functions performed by the tested parties and the comparables match, with or without adjustments, AMP expenses are duly accounted for. It would be Incongruous to accept the comparables and determine or accept the transfer price and still segregate AMP expenses as an international transaction,*
> >
> > *8. By way of an example, this aspect of the matter was then explained by Hon'ble Delhi High Court as follows:*
> >
> > *"An example given below would make it clear:*

Particulars	*Case 1*	*Case 2*
Sales	*1000*	*1,000*
Purchase Price	*600*	*500*
Gross Margin	*400 (40%)*	*500*
Marketing Sale promotion	*50*	*150*
Overhead expenses	*300*	*300*
Net profit	*50 (5%)*	*50 (5%)*

The above illustrations draw a distinction between two distributors having different marketing actions. In case 2, a distributor having significant marketing functions nous substantial expenditure on AMP, three times more than in case 1, but the purchase price being lower, the Indian AE gets adequately compensated and, therefore, transfer pricing adjustment is required. In case we treat the AMP expenses in case 2 as Rs.501- Le identical as case 1 and AMP of Rs. 100 as a separate transaction, the position in case 2 would be:

Particulars	*Case 2*
Sales	*1,000*
Purchase Price	*500*
Gross Margin	*500 (50%)*
Overhead expenses	*300*
Marketing Sale promotion	*50*
Net profit	*150 (15%)*

It is obvious that this would not be the correct way and method to compute the arm's length price. The purchase price adjustments/set off would be mandated to arrive at the arm's length price, if the AMP expenses are segregated as an independent international transaction".

9. By the same logic, even making an adjustment for interest on excess credit allowed on sales to AEs will vitiate the picture, inasmuch as what has already been factored in the TNMM analysis, by taking operating profit figure which incorporate financial impact of the excess credit period allowed, will be adjusted again separately as well. Of course, in the example used by Hon'ble Delhi High Court, the AMP expenses are deductibles in computation of operating profit but that does not make any material difference because the interest levy for late realization of debtors, being inextricably connected with the sales, is also part of operating income. In the case of Nirma Industries Limited Vs DCIT [(2006) 283 ITR 402 (Guj)), Hon'ble High Court has dealing with the nature of interest on debtors, held it to be integral to business income. The same is the principle for the transfer pricing cases to that extent interest is to be taken as integral to sale proceeds, and, as such, includible in operating income. When such an interest is includible in operating Income and the operating income itself has been accepted as reasonable under the TNMM, there cannot be an occasion to make adjustment for notional interest on delayed realization of debtors. One can understand separate adjustment for excess credit period when the arm's length price for exports has been benchmarked on the CUP basis but not in a case when the arm's length price of the exports has been benchmarked on the basis of TNMM. The very conceptual foundation, for separate adjustment for delayed realization of debtors and on the facts of this case, is thus devoid of legally sustainable merits.

10. The other aspect of the matter is that a separate adjustment for delayed realization of debtors can, even in a fit case, can only be made only to the extent the credit period allowed to the associated enterprises is more than the credit period allowed to independent enterprise in respect of the same or materially similar transactions. In the present case, it is an undisputed position that semi finished goods, as sold to Micro USA, is not sold to any other independent enterprises. The assessee did have trading transactions in respect of the finished goods with trading subsidiaries in China and Hong Kong but it is not even the case of the TPO that excessive credit period was allowed to these AEs vis-à-vis the credit period allowed to independent enterprises, nor any ALP adjustment has been recommended in connection with the same. This fact, if anything, shows that the credit period allowed to the AEs is comparable with credit period of non AES in respect of similar goods. To compare credit period in respect of finished goods with the credit period in respect of semi-finished goods, is, therefore, somewhat fallacious in approach and untenable in law. In our considered view, merely because there is a delay in realization of debts cannot be reason enough to make an addition as long as such a delay is peculiar to the transactions with AES. The adjustment before us is an adjustment to arrive at an arm's length price and unless there is something, more than sweeping generalizations as implicit in the arguments before us, to at least indicate that such a delay in realization of debts in similar transactions is absent in arm's length transactions, these adjustments cannot be made even when sales are benchmarked on CUP basis. The delay in realization of debts, resulting in a continuing debit balance, is not a standalone international transaction per se, but is a result of the international transaction as it only to be made as soon as goods or services are delivered. A call is to be taken by the vendor, in consultation with its client and based on the business exigencies, as to what should be the terms on which payments for the supplies is to be made. It is a harsh commercial reality that immediate payments are more of exceptions rather than rule, and more so in a complex case in which the assessee is sole vendor and the very existence of the buyer is to process the semi- finished goods and sell it to the end buyers Many factors, such normal business practices and the commercial exigencies, influence the fact of payment in respect of a commercial transaction. Whether a payment is made immediately by the AE or is made after six months cannot, therefore, be seen in isolation with what is the position is with respect to similar payments due from non AEs. The whole exercise of ALP adjustments is to neutralize the impact of inter se relationships between the AEs and it is, therefore, not the delay simplictor in payment but delay in payment vis-à-vis similar situations with non AES (i.e. independent enterprises) which is of crucial consideration. Such a comparison cannot be based on the hypothesis as to what would have, in the wisdom of the TPO, happened if assessee was to have similar transactions with non- AES. The comparison has to be based on real transactions of similar nature, if at all such transactions have taken place. When no such transactions have taken place, as is the case before us, there is obviously no occasion of any comparison. The stand taken by the learned Departmental Representative, therefore, is not only quite detached from commercial reality but also wholly untenable in law. In any case, what can be examined on the touchstone of arm's length principles is the commercial transaction itself, as a result of which the debit balance has come into existence, and the terms and conditions, including terms of payment, on which the said commercial transaction has been entered into. In this view of the matter, learned Departmental Representative's reliance on Aztec decision (supra) is of no assistance to the case of the revenue. The international transaction is exports of goods which been benchmarked on TNMM basis and which is duly accepted by the TPO. In view of these discussions, and respectfully following the decision of the coordinate bench in assessee's own case for the

earlier years, we uphold the grievance of the assessee and direct the Assessing Officer to delete the impugned ALP adjustment of Rs 2,10,95,346.

14. As regards learned Departmental Representative's contention that Sony Ericsson Mobile Corporation decision (supra) will not apply in the case before us in the context of interest an delayed realization of debts for the simple reason that while AMP expenses, as in that case, are taken into account in the computation of the PLI, interest on delayed realization of debts is not taken into account in computation of the PLI, we can only say that it proceeds on the fallacious assumption that interest income is not taken into account in computation of profit before interest and taxes. The profit before tax and interest (PBIT) so computed takes into account interest income because, on the given facts, it is in the nature of 'other income' which is duly included in the PBIT figure. It is only interest expenditure which is not taken into account in the PBIT computation. There is no warrant for the proposition that interest expenditure taken into account is net of interest income en account of delay in realization of debts. We, therefore, reject this contention of the Departmental Representative.

15. As for learned Departmental Representative's suggestion that it is to be verified whether the comparables include interest income, if any, all we can say is that the statutory provisions requires the interest income, unless it is an interest income of the finance and banking companies, to be included in the other income which is taken into account for computing PBIT (e. profit before interest and taxes) The presumption therefore is that the accounts are drawn up as per the statutory requirements, and the exclusions from other income are specifically discussed on the facts of each case, and as such constitute integral part of the transfer pricing documentation. There is nothing on record to show these exclusions.

16. As regards the contention that normally all Interest incomes are excluded in the computation of PBIT as such incomes rarely constitute operational income, we see no need to be guided by such hypothesis and generalities. There is nothing on the records, as we have noted earlier, such exclusions on the facts of this case. In any event, setting off of interest expenditure with interest on account of delay in realization of debts, even if so, is not too common an occurrence and more of an exceptions than the rule. The apprehensions of the learned DR are purely hypothetical and, therefore, devoid of legally sustainable merits.

17. In view of these discussions, as also bearing in mind entirety of the case, we are of the considered view that no ALP adjustments can be made, on the facts of this case, in respect of delay in realization of sale proceeds. Such being our conclusions, we also see no need to address ourselves to the specific factual arguments advanced by the learned counsel. In effect thus, we uphold the grievance of the assessee, and direct the Assessing Officer to delete the impugned arm's length price adjustment."

39. Since, both the transactions entered into by the assessee with associated enterprises are benchmarked on TNMM basis and both the transactions are

also at arm's length, therefore, respectfully following the aforesaid decision of coordinate bench of the Tribunal, we direct the AO/TPO to delete the transfer pricing adjustment on account of outstanding receivables from associated enterprises. As a result, grounds No. 4 – 9 are allowed.

40. Ground no. 10 is pertaining to initiation of penalty proceedings, which is premature in nature and therefore is dismissed.

41. Ground No. 11 pertains to levy of interest under section 234B and 234C of the Act, which is consequential in nature. Therefore, the said ground is allowed for statistical purpose.

42. In the result, appeal by the assessee is partly allowed for statistical purpose.

Order pronounced in the open Court on 10/10/2022

Sd/-	**Sd/-**
PRAMOD KUMAR	**SANDEEP SINGH KARHAIL**
VICE PRESIDENT	**JUDICIAL MEMBER**

MUMBAI, DATED: 10/10/2022

Copy of the order forwarded to:

(1) The Assessee;
(2) The Revenue;
(3) The CIT(A);
(4) The CIT, Mumbai City concerned;
(5) The DR, ITAT, Mumbai;
(6) Guard file.

True Copy
By Order

Pradeep J. Chowdhury
Sr. Private Secretary

Assistant Registrar
ITAT, Mumbai