

आयकर अपीलीय अधिकरण, हैदराबाद पीठ में  
IN THE INCOME TAX APPELLATE TRIBUNAL  
HYDERABAD BENCHES "A", HYDERABAD

BEFORE  
SHRI RAMA KANTA PANDA, VICE PRESIDENT  
&  
SHRI K.NARASIMHA CHARY, JUDICIAL MEMBER

आ.अपी.सं / ITA-TP No. 488/Hyd/2022  
(निर्धारण वर्ष / Assessment Year: 2018-19)

Parexel International (India) Private Limited,  
Hyderabad  
[PAN No. AAECP2199N] Vs. Asst. Commissioner of  
Income Tax,  
Circle-5(1),  
Hyderabad

अपीलार्थी / Appellant

प्रत्यर्थी / Respondent

निर्धारिती द्वारा/Assessee by: Shri Aliasgar Rampurwala &  
Shri Yogesh Malpani, ARs  
राजस्व द्वारा/Revenue by: Ms. TH Vijaya Lakshmi, CIT-DR

सुनवाई की तारीख/Date of hearing: 09/11/2023  
घोषणा की तारीख/Pronouncement on: 21/11/2023

आदेश / ORDER

**PER K. NARASIMHA CHARY, J.M:**

Aggrieved by the order dated 29/07/2022, passed by the Learned Assessing Officer ("Ld. AO") in the case of M/s. Parexel International (India) Private Limited, ("the assessee") for the assessment year 2018-19, under section 143(3) r.w.s. 144C(13) of the Income Tax Act, 1961 (for short "the

Act”), consequent to the directions of Hon'ble Dispute Resolution Panel, Bengaluru (“DRP”), assessee filed this appeal.

2. Brief facts of the case as per record are that the assessee is a subsidiary of Parexel International Holdings B.V., Netherlands which in turn is a subsidiary of Parexel USA. Assessee is a private limited company, and its unit is located in Special Economic Zone which is engaged in providing IT and IT enabled services (ITeS) to Parexel Group companies which aid the clinical trial business. During the previous year relevant to the assessment year 2018-19, the learned Transfer Pricing Officer (learned TPO) proposed a total Transfer Pricing (TP) adjustment of Rs. 30,85,31,663/- comprising of three adjustments, viz., TP adjustment of Rs. 2,62,93,347/- in the IT/software development (SWD) segment, TP adjustment of Rs. 26,80,09,843/- in the ITeS segment and TP adjustment of Rs. 1,42,28,473 towards interest on overdue receivables vide learned TPO's order dated 31/07/2021. Incorporating the aforesaid TP adjustment, the learned Assessing Officer passed the draft assessment order dated 14/09/2021.

3. Aggrieved, assessee filed objections before the learned DRP. Learned DRP vide its directions dated 08/06/2022, partly allowed the objections raised by the assessee by deleting the entire TP adjustment of Rs. 2,62,93,347/- in the IT/SWD services segment. Further, in the ITeS segment, the learned DRP granted partial relief to the assessee by directing inclusion/exclusion of certain comparables and further upheld the adjustment on interest on overdue receivables. Learned DRP upheld the adjustment qua notional interest.

4. Pursuant to the directions of the learned DRP, the learned TPO passed the order dated 14/07/2022, giving effect to the learned DRP's directions, wherein the learned TPO, inter alia, deleted the entire TP adjustment in the IT/SWD segment and reduced the TP adjustment in the ITeS segment from Rs. 26,80,09,843/- to Rs. 20,46,47,956/-. Subsequently, the learned Assessing Officer passed the impugned final assessment order dated 29/07/2022, incorporating the TP adjustment as per the learned TPO's order giving effect to the learned DRP's directions.

5. Aggrieved by the final assessment order, the assessee preferred this appeal on as many as 14 grounds. Learned AR, however, at the time of arguments not pressed all the grounds except ground No. 7 to the extent of Infosys BPM Services Pvt. Ltd., and eClerx Services Ltd., and ground No. 11 to the extent of not granting working capital adjustment.

6. Learned AR submitted that the contention of the assessee before the learned TPO was that because of the functional differentials, possession of brand value, being a market leader and its global presence and incurring consultancy expenses in the nature of sub-contracting charges, Infosys BPM Services Pvt. Ltd., is not a comparable company. He further submitted that in respect of eClerx Services Ltd., also assessee canvassed before the learned TPO that this entity too functionally not comparable, because segmental details are not available. Assessee further submitted in respect of eClerx Services Ltd., that this company possessed global intangibles, incurs advertising and sales promotion expenses apart from sub-contracting expenses. Learned AR submitted that in spite of this, the learned TPO did not consider that the huge turnover and brand value

of these companies, but brushing this aside, the learned TPO held that these two companies are good comparables.

7. In respect of Infosys BPM Services Pvt. Ltd , he submitted that the company is functionally different and is engaged into diversified activities. Infosys BPM Services Pvt. Ltd was formerly known as Infosys BPO Ltd. The company provides new age services such as Business of Digital, Robotic Process Automation ('RBA'), Mortgage Origination Services, Business Transformation Services, Analytics, McCamish Insurance Utilities etc., that it is engaged in providing high-end integrated services through managing their business processes, in addition to providing increased value and further, the company is engaged in diversified activities; that the company also renders onsite services at client sites or global development centers located in the same country where the client is based out of and the onsite revenue of the company is 77.3% of the total revenues; that majority-owned and controlled subsidiary of 'Infosys Limited'. Leverage on Brand value of "Infosys" - strong brand name across the globe including Europe, Latin America, Africa and USA; that the substantial amount of selling & marketing expenses (Rs. 166 crores) & brand building expenses (Rs. 3 crores); that the revenue from operations - Rs. 3061 crores; that the higher profit margin derived by Infosys BPM is predominantly due to brand building exercise undertaken; this by itself allows Infosys BPM to have a premium price for its products and services; that in comparison, the assessee is a captive service provider, rendering services to its overseas affiliate without having such benefit of brand image.

8. Regarding outsourcing costs, he submitted that cost of technical sub-contractors and professional charges; that the outsourcing cost incurred by Infosys BPM reflects that a different operating model is being followed vis-a-vis the assessee and hence, cannot be compared with the assessee. In this connection, he relied upon assessee's own case - Parexel International (India) Private Limited ITA. No 423/Hyd/2016 (Hyd. Trib.) for the assessment year 2011-12, wherein Infosys BPO (now Infosys BPM) was excluded owing to different business model, brand value, sub-contracting, diversified activity and other functional dissimilarities. He further submitted that in the case of Cadence Design Systems (I.) (P.) Ltd. [(2018) 93 taxmann.com 227 (Delhi ITAT) also Infosys BPO Ltd. (now Infosys BPM) excluded because, unlike the assessee, it is providing high end and integrated services for business platforms, customer services, outsourcing, finance and accounting, human resource outsourcing, legal process outsourcing, sales and fulfillment etc., thus, it is not comparable to the assessee's ITeS segment. The exclusion of the above two companies from the list of comparables in the ITes segment in the case of Cadence Design Systems (I.) (P.) Ltd. (supra) has been upheld by the Hon'ble Delhi High Court in the case of PCIT vs. Cadence (2020) 119 taxmann.com 415 and the SLP against the order of the Hon'ble Delhi High Court was dismissed by the Hon'ble Supreme Court reported in (2020) 119 taxmann.com 416 SC.

9. Learned AR also relied in the case of Equant Solutions India (P.) Ltd. [(2020) 113 taxmann.com 517 - P&H HC], wherein it was decided that the brand of Infosys BPO (Infosys BPM) definitely results in higher profits and hence, the same could not be compared to the assessee being an ITeS provider. In the case of Symphony Marketing Solutions India P. Ltd. [(2020)

113 taxmann.com 77 — Delhi HC) also Infosys BPO (now Infosys BPM) excluded since it was engaged in business process management services whereas the assessee was a routine captive service provider. Further, Infosys had high goodwill, significant marketing expenses etc. Relies on another Delhi High Court decision [ITA 420 of 2019] which held that Infosys BPO, being a Infosys group company was a 'giant corporation' and therefore, could not be taken as a comparable.

10. As far as eClerx Services Ltd., is concerned, learned DRP held that a BPO trying to upgrade itself as KPO is likely to render both the services and therefore cannot be strictly considered as KPO; further, high-end and low-end activity cannot be distinguished since only broad comparability is to be seen under TNMM. Learned DRP also held that there is nothing in the annual report to suggest that brand has contributed to the growth or profitability and marketing expenses equating to 18.51% of total sales are not much significant; that the company is involved in the business of providing KPO services and therefore, is functionally different from the assessee. The company is engaged in diversified activities such as quality monitoring insights, advanced analytics, technical operations, digital care services, financial services, digital marketing, digital branding and cable, telecom and analytics and advanced automation as also derivative trade support, high advertising marketing and promotion expenses. It had incurred significant sales and marketing costs (Rs. 21: crores), which corresponds to around 18.5% of the total revenue of Rs. 1142 crores; that such marketing and advertising activities carried out by the entrepreneurial companies result in creation of marketing intangibles and thereby demand a return on such investment made in creation of such

intangibles. Therefore, the return of such companies would include an embedded return towards marketing activities/efforts and related investment and risks.

11. As far as outsourcing costs, it was submitted that the cost of technical sub-contractors - outsourcing costs Rs. 8.09 crores. As the company gets its work done through outsourcing the business model of the company is different from a routine service provider and lack of segmental data. Although the company has diversified segments, it only reports its operations under one segment for reporting purposes by clubbing data management, analytics solutions and process outsourcing services and does not maintain segmental data. He relied upon the decision of the Co-ordinate Bench in assessee's own case in ITA No 144/Hyd/2014 (AY, 2009- 10), wherein eClerx Services Ltd., was excluded from the list of comparables on the basis that it is functionally different and not comparable to the assessee's ITeS business by relying upon another decision to hold that eClerx Services Ltd., is involved in diverse nature of services, no segmental data is available and it is a KPO, hence, not comparable to the assessee;

12. In respect of this entity also, learned AR submitted that in all the decisions cited with reference to the Infosys BPM Services Pvt. Ltd., are equally applicable in respect of eClerx Services Ltd., also and he invited our attention to the relevant portions of such judgment.

13. Per contra, learned DR vehemently disputed the objection of the assessee, basing on the turnover and brand. By taking the turnover, operating profit and costs of Infosys Technology Ltd., as an example,

learned DR submitted that over a period of twenty years, the turnover of this company has increased from Rs. 139 crores to Rs. 61.941 crores, but the OP/OR remained around 25.90% only with small fluctuations here and there. She placed reliance on the decision of the Hon'ble Delhi High Court in the case of Chryscapital Investment Advisors (India) (P.) Ltd. vs. DCIT [2015] 56 taxmann.com 417 (Delhi), for the principle that huge profit or a huge turnover, ipso facto does not lead to its exclusion.

14. We have considered these contentions in the light of the decided case law. Insofar as the turnover filter is concerned, Hon'ble Delhi High Court in the case of Chryscapital Investment Advisors (India) (P.) Ltd. (supra), held that huge profit or a huge turnover, ipso facto does not lead to its exclusion; whereas in the case of CIT vs. M/s. Pentair Water India Pvt. Ltd. (2016) 69 taxmann.com 180, the Hon'ble Bombay High Court held that turnover is a relevant criteria for choosing companies as comparables in determining the ALP in Transfer Pricing cases. Hon'ble Karnataka High Court, however, in the case of PCIT vs. M/s. Obopay Mobile Technology India Private Ltd., in ITA No. 586/2016, dated 23/07/2018, having noticed the view taken by the Hon'ble Delhi High Court in the case Chryscapital Investment Advisors (India) (P.) Ltd. (supra), and also the decision of the Hon'ble Bombay High Court in the case of CIT vs. M/s. Pentair Water India Pvt. Ltd. (supra), upheld the Tribunal's order excluding certain entities from the list of comparables on the ground of huge turnover, while following the principle that where two views are possible on an issue, the view favourable to the assessee has to be adopted.

15. Apart from this, in assessee's own case, for the assessment years 2009-10, eClerx Services Ltd., and for the assessment year 2011-12 Infosys BPM Services Pvt. Ltd., was considered and excluded due to the different model, brand value, sub-contracting, diversified activities, non-availability of segmental data etc., apart from holding that eClerx Services Ltd., is rendering KPO services. Further, in the case of Cadence Design Systems (I.) (P.) Ltd. (supra), these two entities were considered. Infosys BPM Services Pvt. Ltd., was held to have been providing high end integrated services for business platforms, customer services, outsourcing, finance and accounting, human resource outsourcing, legal process outsourcing, sales and fulfilment etc., and thus is not comparable to the assessee's ITeS segment. eClerx Services Ltd., was held to be a KPO company, outsourcing substantial work to third parties during that year whereas the assessee, an ITeS provider, was rendering back office support services with their own human resource, and, therefore, not a good comparable with the companies like assessee. The view taken by the Tribunal in the case of Cadence Design Systems (I.) (P.) Ltd. [(2018) 93 taxmann.com 227 (Delhi ITAT)], was upheld by the Hon'ble Delhi High Court in the light of its decision in the case of Avaya India (P.) Ltd., vs. ACIT [2019] 108 taxmann.com 222. An SLP filed by the Revenue against the same was dismissed by the Hon'ble Apex Court in the decision reported in [2020] 119 taxmann.com 416 (SC).

16. In these circumstances, following the foot prints of the Hon'ble Karnataka High Court in the case of Obopay Mobile Technology India Private Ltd., (supra), Hon'ble Delhi High Court in the case Avaya India (P.) Ltd., vs. ACIT (supra) and in the case of Cadence Design Systems (I.) (P.) Ltd. (supra), we hold that the turnover and brand name are relevant criteria for

choosing companies as comparables in determining the ALP in Transfer Pricing cases. We, therefore, direct the learned Assessing Officer/learned TPO to exclude these two entities from the list of comparables.

17. Coming to the other issue relating to the denial of working capital adjustment, it is submitted that the assessee had carried out working capital adjustment in the transfer pricing study report and further, the assessee was asked for working capital adjustment before the learned TPO, demonstrated the need for grant of working capital adjustment and had furnished the relevant workings. However, the learned TPO did not allow working capital adjustment. Further, the assessee claimed for grant of working capital adjustment before the learned DRP as well. Learned AR submitted that detailed submissions from Pg. No. 202 to 208 of Form 35A clearly show wherein the assessee typically reasoned that 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. However, the learned DRP denied working capital adjustment stating that though the assessee argued that there exist differences in the payable and receivable positions between assessee and comparables, it was not demonstrated with any data or information as to the impact of such difference on the price, cost or profit and as to whether such difference materially effect the price and cost or profits. According to the learned DRP, the accounts payables and receivables shown in the balance sheet only reflects the position as at the end of the financial year, and as such it would not enable to measure the impact of working capital on the costs, price or profits; that the working capital requirements and impact depends on various factors such as business cycle, the nature of business

activity with its correlation on the general economic trends, the fund and capital position of the company, its marketing strategies and its market share etc., all of which cannot be captured in the year end receivable or payable position. Learned DRP felt that the payable and receivable position stated in the balance sheet may not exactly reflect as to whether it arises from transaction relating to Revenue Account or Capital Account as there is no uniformity in the accounting or reporting requirements, and an intermixing is generally possible. Learned DRP further opined that the cost ascribable to the working capital would be different to different enterprises depending on the cost of fund to the enterprise, the cost of money in the economy it operates etc. In view of these, learned DRP held that a reasonable accurate adjustment is not possible as the difference in working capital requirements itself is based on various assumptions, and also that the assessee had failed to demonstrate such material differences so as to warrant an adjustment. Learned DRP accordingly upheld the learned TPO's reasons and reject the assessee's claim for working capital adjustment.

18. Learned AR submits that transfer pricing analysis is an estimation and not an exact science. There is always an element of estimation and working capital adjustment must be based on opening and closing working capital deployed and daily working capital requirements data cannot be insisted upon. One has to see that reasonable adjustment be made wherever it is needed so as to bring both comparables and tested party on the same footing. Moreover, assessee cannot be asked to provide for segmental details and details of trade and non-trade debtors of comparable companies as these details are beyond power of assessee to

obtain, unless they are available in public domain. Thus, where complete working capital adjustment working had been given by assessee and no specific defect had been pointed out in these workings, then working capital adjustment as worked out by the assessee must be allowed. Further, even OECD guidelines (at paragraphs 13 to 16), emphasizes need for working capital adjustment in terms of receivables and payables. Regarding comparable companies learned AR submitted that one has to fall back upon only on information available in public domain. If that information is insufficient, it is beyond the power of the assessee to produce correct information about comparable companies. He further argued that Revenue, on the other hand has sufficient powers under section 133(6) of the Act to compel production of required details from comparable companies. If this power is not exercised to find to get information required, then it is no defense to say that assessee has not furnished required details to deny any adjustment on account of working capital differences. Thus, learned AR insisted that the assessee wishes to re-iterate that working capital adjustment, which should be allowed on actuals. This means that working capital of the assessee and the comparables should be adjusted to ensure a fair comparison. He further submitted that the assessee submitted all the relevant details for the computation of the working capital adjustment to the lower authorities, but were outrightly rejected by them. In this regard, he placed reliance in the cases of Huawei Technologies India Pvt Ltd vs. JCIT, IT(TP)A No. 1939/Bang/2017, Parexel International Clinical Research Private Limited vs. ACIT: IT(TP)A No. 894/Bang/2022, Denso India Limited vs. ACIT, ITA No.

4788/Del/2010, DCIT vs. Apotex Pharmachem India (P.) Ltd, IT(TP)A No. 156/Bang/2014.

19. Learned AR further submitted that for the assessment years 2009-10 and 2011-12, authorities themselves granted working capital adjustment. In view of the above, learned AR most humbly prayed that working capital adjustment be granted to the assessee in the interest of justice and equity.

20. Learned DR on the other hand, vehemently relied on the orders of the authorities below and submitted that in the facts and circumstances of the case, it is not possible to determine the reasonably accurate adjustment as the differences in working capital requirements itself is based on various assumptions.

21. We have gone through the record in the light of the submissions made on either side. On a careful perusal of the view taken by the Bangalore Bench of the Tribunal in the case of Parexel International Clinical Research Private Limited vs. ACIT (supra), the facts are identical in both these cases and the relevant findings of the Tribunal are extracted hereunder for the sake of completeness:

*“8.1 The Id. DRP observed that Rule 10B provides for making reasonably accurate adjustment to the uncontrolled comparable transaction to eliminate the material effects of differences on the price, cost or profits. The assessee has argued for working capital adjustment contending that there exist differences in the payable and receivable position between the assessee and the comparables. However, it was not demonstrated with any data or information as to the impact of such difference on the price, cost or profits, and as to whether such difference materially affect the price, cost or profits. The 'Accounts payables' and 'Receivables' shown in the balance sheet only reflects the position as at the end of the financial year,*

*and as such it would not enable to measure the impact of working capital on the costs, price or profits. The working capital requirements and impact depends on various factors such as business cycle, the nature of business activity with its correlation on the general economic trends, the fund and capital position of the company, its marketing strategies, its market share etc. all of which cannot be captured in the year end Receivable or Payable position. Besides, the 'Payable' and 'Receivable' position stated in the Balance Sheet may not exactly reflect as to whether it arises from transaction relating to Revenue Account or Capital Account as there is no uniformity in the accounting or reporting requirements, and an intermixing is generally possible. The cost ascribable to the working capital would be different to different enterprises depending on the cost of fund to the enterprise, the cost of money in the economy it operates etc. In view of these, a reasonable accurate adjustment is not possible, as the differences in working capital requirements itself is based on various assumptions. Besides, the assessee had failed to demonstrate such material differences so as to warrant an adjustment. In these circumstances, the Id. DRP inclined to uphold the TPO's reasoning and rejected the assessee's claim for working capital adjustment. Against this assessee is in appeal before us.*

*9. After hearing both the parties, we are of the opinion that similar issue came for consideration before this Tribunal in IT(TP)A No.3270/Bang/2018 in assessee's own case vide order dated 18.4.22 wherein held as under:*

*"22. With regard to the question whether working capital adjustment should be given or not, we find that the reasons given by the DRP for not allowing working capital adjustment are the same reasons as was given in the case of Huawei Technologies India Pvt. Ltd. v. JCIT [2019] 101 taxmann.com 313 (Bang. Trib.). In the aforesaid decision on an identical issue, the Tribunal held that working capital adjustment has to be given. The following are the relevant observations of the Tribunal :-*

*"10. The next grievance projected by the Assessee in its appeal is with regard to the action of the CIT (A) in not allowing any adjustment towards working capital differences. On this issue we have heard the rival submissions. The relevant provisions of the Act in so far as comparability of international transaction with a transaction of similar nature entered into between unrelated parties, provides as follows:*

*Determination of arm's length price under section 92C.*

10B. (1) For the purposes of sub-section (2) of section 92C, the arm's length price in relation to an international transaction [or a specified domestic transaction] shall be determined by any of the following methods, being the most appropriate method, in the following manner, namely;— (a) to (b)\*\* \*\* \*

€ transactional net margin method, by which,—

- (i) the net profit margin 15ransact by the enterprise from an international transaction [or a specified domestic transaction] entered into with an associated enterprise is computed in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise or having regard to any other relevant base;
- (ii) the net profit margin 15ransact by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction or a number of such transactions is computed having regard to the same base;
- (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;
- (iv) the net profit margin 15ransact by the enterprise and referred to in subclause (i) is established to be the same as the net profit margin referred to in sub-clause (iii);
- (v) the net profit margin thus established is then taken into account to arrive at an arm's length price in relation to the international transaction [or the specified domestic transaction];
- (f) \*\* \*\* \*

(2) For the purposes of sub-rule (1), the comparability of an international transaction [or a specified domestic transaction] with an uncontrolled transaction shall be judged with reference to the following, namely:--

*(a) the specific characteristics of the property transferred or services provided in either transaction;*

*(b) the functions performed, taking into account assets employed or to be employed and the risks assumed, by the respective parties to the transactions;*

*€ the contractual terms (whether or not such terms are formal or in writing) of the transactions which lay down explicitly or implicitly how the responsibilities, risks and benefits are to be divided between the respective parties to the transactions;*

*(d) conditions prevailing in the markets in which the respective parties to the transactions operate, including the geographical location and size of the markets, the laws and Government orders in force, costs of labour and capital in the markets, overall economic development and level of competition and whether the markets are wholesale or retail.*

*(3) An uncontrolled transaction shall be comparable to an international transaction [or a specified domestic transaction]if—*

*(i) none of the differences, if any, between the transactions being compared, or between the enterprises entering into such transactions are likely to materially affect the price or cost charged or paid in, or the profit arising from, such transactions in the open market; or*

*(ii) reasonably accurate adjustments can be made to eliminate the material effects of such differences.*

*11. A reading of Rule 10B(l)€(iii) of the Rules read with Sec.92CA of the Act, would clearly shows that the net profit margin arising in comparable uncontrolled transactions has to be adjusted to take into account the differences, if any, between the international transaction and the comparable uncontrolled transactions, which could materially affect the amount of net profit margin in the open market.*

*12. Chapters I and III of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (hereafter the “TPG”) contain extensive guidance on comparability analyses for transfer pricing purposes. Guidance on comparability adjustments is found in paragraphs 3.47-3.54 and in the Annex to Chapter III of the TPG. A revised version of this guidance was approved by the*

*Council of the OECD on 22 July 2010. In paragraph 2 of these guidelines it has been explained as to what is comparability adjustment. The guideline explains that when applying the arm's length principle, the conditions of a controlled transaction (i.e. a transaction between a taxpayer and an associated enterprise) are generally compared to the conditions of comparable uncontrolled transactions. In this context, to be comparable means that:*

- ◆ None of the differences (if any) between the situations being compared could materially affect the condition being examined in the methodology (e.g. price or margin), or*
- ◆ Reasonably accurate adjustments can be made to eliminate the effect of any such differences. These are called "comparability adjustments."*

*13. In Paragraphs 13 to 16 of the aforesaid OECD guidelines, need for working capital adjustment has been explained as follows:*

*"13. In a competitive environment, money has a time value. If a company provided, say, 60 days trade terms for payment of accounts, the price of the goods should equate to the price for immediate payment plus 60 days of interest on the immediate payment price. By carrying high accounts receivable a company is allowing its customers a relatively long period to pay their accounts. It would need to borrow money to fund the credit terms and/or suffer a reduction in the amount of cash surplus which it would otherwise have available to invest. In a competitive environment, the price should therefore include an element to reflect these payment terms and compensate for the timing effect.*

*14. The opposite applies to higher levels of accounts payable. By carrying high accounts payable, a company is benefitting from a relatively long period to pay its suppliers. It would need to borrow less money to fund its purchases and/or benefit from an increase in the amount of cash surplus available to invest. In a competitive environment, the cost of goods sold should include an element to reflect these payment terms and compensate for the timing effect.*

15. A company with high levels of inventory would similarly need to either borrow to fund the purchase, or reduce the amount of cash surplus which it is able to invest. Note that the interest rate July 2010 Page 6 might be affected by the funding structure (e.g. where the purchase of inventory is partly funded by equity) or by the risk associated with holding specific types of inventory) 16. Making a working capital adjustment is an attempt to adjust for the differences in time value of money between the tested party and potential comparables, with an assumption that the difference should be reflected in profits. The underlying reasoning is that:

◆ A company will need funding to cover the time gap between the time it invests money (i.e. pays money to supplier) and the time it collects the investment (i.e. collects money from customers)

◆ This time gap is calculated as: the period needed to sell inventories to customers + (plus) the period needed to collect money from customers – (less) the period granted to pay debts to suppliers.”

14. Examples of how to work out adjustment on account of working capital adjustment is also given in the said guidelines. The guideline also expresses the difficulty in making working capital adjustment by concluding that the following factors have to be kept in mind (i) The point in time at which the Receivables, Inventory and Payables should be compared between the tested party and the comparables, whether it should be the figures of receivables, inventory and payable at the year end or beginning of the year or average of these figures, (ii) the selection of the appropriate interest rate (or rates) to use. The rate (or rates) should generally be determined by reference to the rate(s) of interest applicable to a commercial enterprise operating in the same market as the tested party. The guidelines conclude by observing that the purpose of working capital adjustments is to improve the reliability of the comparables.

15. In the present case the TPO allowed working capital adjustment accepting the calculation given by the Assessee. The CIT (A) in exercise of his powers of enhancement held that no adjustment should be made to the profit margins on account of working capital differences between the tested party and the comparable companies for the following reasons:

- (i) The daily working capital levels of the tested party and the comparables was the only reliable basis of determining adjustment to be made on account of working capital because that would be on the basis of working capital deployed throughout the year.*
- (ii) Segmental working capital is not disclosed in the annual reports of companies engaged in different segments and therefore proper comparison cannot be made.*
- (iii) Disclose in the balance sheet does not contain break up of trade and nontrade debtors and creditors and therefore working capital adjustment done without such break up would result in computation being skewed.*
- (iv) Cost of capital would be different for different companies and therefore working capital adjustment made disregarding this different based on broad approximations, estimations and assumptions may not lead to reliable results.*

*16. The CIT (A) also placed reliance on a decision of Chennai ITAT in the case of Mobis India Ltd. v. Dy. CIT [2013] 38 taxmann.com 231/[2014] 61 SOT 40. That decision was based on the factual aspect that the Assessee was not able to demonstrate how working capital adjustment was arrived at by the Assessee. Therefore nothing turns on the decision relied upon by the CIT (A) in the impugned order. In the matter of determination of Arm's Length Price, it cannot be said that the burden is on the Assessee or the Department to show what is the Arm's Length Price. The data available with the Assessee and the Department would be the starting point and depending on the facts and circumstances of a case further details can be called for. As far as the Assessee is concerned, the facts and figures with regard to his business has to be furnished. Regarding comparable companies, one has to fall back upon only on the information available in the public domain. If that information is insufficient, it is beyond the power of the Assessee to produce the correct information about the comparable companies. The Revenue has on the other hand powers to compel production of the required details from the comparable companies. If that power is not exercised to find out the truth then it is no defence to say that the Assessee has not furnished the required details and on that score deny adjustment on account of working capital differences. Regarding applying the daily balances of inventory, receivables and payables for computing working capital adjustment, the Delhi Bench of ITAT in*

*the case of ITO v. E Value Serve.com [2016] 75 taxmann.com 195 (Delhi – Trib.). has held that insisting on daily balances of working capital requirements to compute working capital adjustment is not proper as it will be impossible to carry out such exercise and that working capital adjustment has to be based on the opening and closing working capital deployed. The Bench has also observed that that in Transfer Pricing Analysis there is always an element of estimation because it is not an exact science. One has to see that reasonable adjustment is being made so as to bring both comparable and test party on same footing. Therefore there is little merit in CIT (A)'s objection on working adjustment based on unavailable daily working capital requirements data. There is also no merit in the objection of the CIT (A) regarding absence of segmental details available of working capital requirements of comparable companies chosen and absence of details of trade and non-trade debtors of comparable companies as these details are beyond the power of the Assessee to obtain, unless these details are available in public domain. Regarding absence of cost of working capital funds, the OECD guidelines clearly advocates adopting rate(s) of interest applicable to a commercial enterprise operating in the same market as the tested party. Therefore this objection of the CIT (A) is also not sustainable.*

*17. In the light of the above discussion we are of the view that the CIT (A) was not justified in denying adjustment on account of working capital adjustment. Since, the CIT (A) has not found any error in the TPO's working of working capital adjustment, the working capital adjustment as worked out by the TPO has to be allowed. We may also add that the complete working capital adjustment working has been given by the Assessee and a copy of the same is at pages 173 & 192 of the Assessee's paper book. No defect whatsoever has been pointed out in these working by the CIT (A). We may also further add that in terms of Rule 10B(1)(iii) of the Rules, the net profit margin arising in comparable uncontrolled transactions should be adjusted to take into account the differences, if any, between the international transaction and the comparable uncontrolled transactions which could materially affect the amount of net profit margin in the open market. It is not the case of the CIT (A) that differences in working capital requirements of the international transaction and the uncontrolled comparable transactions is not a difference which will materially affect the amount of net profit margin in the open market. If for reasons given by CIT (A) working capital adjustment*

*cannot be allowed to the profit margins, then the comparable uncontrolled transactions chosen for the purpose of comparison will have to be treated as not comparable in terms of Rule 10B(3) of the Rules, which provides as follows:*

*“(3) An uncontrolled transaction shall be comparable to an international transaction if—*

*(i) none of the differences, if any, between the transactions being compared, or between the enterprises entering into such transactions are likely to materially affect the price or cost charged to paid in, or the profit arising from, such transactions in the open market; or*

*(ii) reasonably accurate adjustments can be made to eliminate the material effects of such differences.”*

*18. In such a scenario there would remain no comparable uncontrolled transactions for the purpose of comparison. The transfer pricing exercise would therefore fail. Therefore in keeping with the OECD guidelines, endeavor should be made to bring in comparable companies for the purpose of broad comparison. Therefore the working capital adjustment as claimed by the Assessee should be allowed. We hold and direct accordingly.”*

*9. The aforesaid decision clearly lays down the proposition that working capital adjustment is to be given effect to while determining ALP while adopting TNMM method. Respectfully following the said decision, we allow this issue in favour of the assessee.”*

*9.1 In view of the above order of the Tribunal in assessee’s own case, we decide the issue in favour of the assessee and against the department.”*

22. in view of the fact that for the assessment years 2009-10 and 2011-12, working capital adjustment is said to have been granted to the assessee apart from in sister concern’s case of Parexel International Clinical Research Private Limited (supra), we set aside this issue to the file of the learned Assessing Officer/learned TPO to decide the issue afresh in the

light of the above, after obtaining necessary information from the assessee. Grounds are accordingly treated as allowed for statistical purposes.

23. In the result, appeal of the assessee is treated as partly allowed for statistical purposes.

Order pronounced in the open court on this the 21<sup>st</sup> day of November, 2023.

Sd/-  
**(RAMA KANTA PANDA)**  
**VICE PRESIDENT**

Sd/-  
**(K. NARASIMHA CHARY)**  
**JUDICIAL MEMBER**

Hyderabad,  
Dated: 21/11/2023

TNMM

Copy forwarded to:

1. Parexel International (India) Private Limited, 11<sup>th</sup> Floor,  
Building No. 20, Raheja Mindspace, Madhapur, Hyderabad.
2. The Asst. Commissioner of Income Tax, Circle-5(1), Hyderabad.
3. The Dispute Resolution Panel (DRP), Bengaluru.
4. The Director of Income Tax (IT & TP), Hyderabad.
5. The Addl. Commissioner of Income Tax (Transfer Pricing), Hyderabad.
6. DR, ITAT, Hyderabad.
7. GUARD FILE

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ITAT, HYDERABAD