

**IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCH 'A', BANGALORE**

**BEFORE SMT ASHA VIJAYARAGHAVAN, JUDICIAL MEMBER
AND
SHRI JASON P BOAZ, ACCOUNTANT MEMBER**

**IT(TP)A No.324(B)/2015
(Assessment year : 2010-11)**

M/s e4e Business Solutions India Pvt.Ltd.,
Unit No.1303-1304, 13th Floor,
Prestige Meridian – II, No.30, MG Road,
Bangalore

PAN No.AAACI6324A

Appellant

Vs

The Deputy Commissioner of Income-tax
Circle-3(1)(2)
Bangalore

Respondent

And

**IT(TP)A No.220(Bang.)/2015
(Assessment year : 2010-11)**

The Deputy Commissioner of Income-tax
Circle-3(1)(2)
Bangalore

Appellant

Vs

M/s e4e Business Solutions India Pvt.Ltd.,
Unit No.1303-1304, 13th Floor,
Prestige Meridian – II, No.30, MG Road,
Bangalore

PAN No.AAACI6324A

Respondent

**Assessee by : Shri Ajith Kumar Jain, CA
Revenue by : Shri G.R.Reddy, CIT, DR-I**

**Date of hearing : 28-10-2015
Date of pronouncement : 04-11-2015**

ORDER**PER SMT ASHA VIJAYARAGHAVAN, JM:**

These are cross appeals by the assessee and the revenue directed against the DRP direction dated 26-11-2014 for the assessment years 2010-11.

2. The facts of the case are that the assessee

2.1 The assessee M/s E4e Business Solutions India Pvt.Ltd.,(“e4e India or the Company”) (formerly known as iSeva Systems Pvt.Ltd) was incorporated in March, 2000 under the Companies Act, 1956. The Company is engaged in the business of customer relationship management services and related business process outsourcing services through a variety of customer contract channels such as voice, e mail, chat and web-based services. The company acquired all the business (all assets, liabilities, employees and business) from e4e Tech Support ((India) Pvt.Ltd. a group company, with effect April 1, 2007 on slump sale basis. Consequent to the same, the company has also started rendering infrastructure management services, which is in the nature of Information Technology enabled services (“ITES”) e4e India renders such IT enabled services to its AE’s and other third parties.

3. For the assessment year 2010-11, relevant to the financial year 2009-10, the assessee e-filed its return of income on October 15,2010 declaring a taxable income of Rs.23,945,375/-

3.1 The case was selected for scrutiny assessment proceedings and during the course of the proceedings for the AY: 2010-11, the international transactions entered into by the assessee were referred by the learned DCIT, Circle-11(3) to the DCIT (Transfer Pricing)-IV for determination of Arm's Length Price (ALP) under Sec.92CA of the IT Act, 1961 (The Act).

3.2 The company has adopted transactional Net margin method (TNMM) as the most appropriate method (MAM) to arrive at the ALP which is evident from the Transfer Pricing (TP) Documentation maintained for AY: 2009-10. The Profit Level Indicator (PLI) adopted by the company is operating profit to the total costs as applicable to the AE segment alone, and on this basis, the assessee had computed its PLI at 17.61 percent. The company has selected 8 comparable companies with an arithmetic mean of 14.39 percent, since the margin earned by the company is higher than the arms' length price determined the international transactions were concluded to be at ALP.

4. The case was referred to the learned TPO who rejected the TP documentation maintained by the assessee. The TPO re-determined the ALP considering companies as comparable to the business of the

assessee. These 10 companies included 8 new companies and 2 of the companies selected by the assessee in the TP study. Accordingly, the TPO determined the ALP at 27.70- percent based on the profit margins computed for the 10 selected companies after making an adjustment of (0.84) percent towards working capital differences. Subsequently, the TPO passed an order under section 92CA of the Act, making an adjustment to the ALP amounting to Rs.61,981,771/-

4.1 The AO on taking the above into consideration concluded the assessment proceedings as per the provisions of Sec.144C of the Act, and accordingly, forwarded a draft assessment order (DAO) in the draft assessment order, the AO had proposed the following adjustments.

Sl.No	Additions/Disallowance	Amount(RS.)
1	TP adjustment	61,981,771
2	Excess claim under section 10A of the Act	1,846,246
Total additions/disallowances		63,828,017

On considering the above, the AO computed the total income of the assessee at Rs.87,773,397/- and determined the total tax payable at Rs.33,530,390/- (including interest under section 234B,234C and 234D of the Act).

5. The assessee filed its objections with the Dispute Resolution Panel (DRP) against the said draft assessment order on March 24, 2014. The DRP vide its directions dated November 26, 2014 has upheld the

rejection of TP documentation and the filters applied by the TPO. Further, the DRP has suo-moto modified the export filter to 75 percent sales as against 25 percent to sales adopted by the TPO.

5.1 Further, as requested by the assessee, the DRP directed to reject the following companies in the DRP directions.

Acropetal Technologies Ltd.

Eclerx Services Ltd.

ICRA Online Ltd

Informed Technologies India Ltd.

Infosys BPO Ltd.

5.2 The DRP has suo-moto directed to reject Sundaram Business Services Ltd.

6. With regard to the adjustment made by the AO of Rs.1,846,246 in the DAO for the deduction claimed u/s 10A of the Act, the DRP directed the AO to reduce the telecommunication expenses incurred in foreign currency from both export turnover as well as total turnover. Pursuant to the above directions , the AO passed the final assessment order under section 143(3) r.w.s.144C of the Act, dated December 30,014 (received on January 6, 2015) determining the total income of the assessee at Rs.100,873,056/- and raised a tax demand of Rs.42,605,150/-. In the final assessment order the AO has made the following adjustments.

Sl.No	Additions/Disallowance	Amount(RS.)
1	TP adjustment	76,342,156
2	Excess claim under section 10A of the Act	585,520
Total additions/disallowances		76,927,676

6.1 Aggrieved by the said final assessment order, the assessee has filed this appeal before the ITAT raising the following grounds;

“a. The assessment order dated 30-12-2014 passed by the AO/TPO pursuant to the directions passed by the DRP is not in accordance with the law and is contrary to the facts and circumstances of the present case and in any case in violation of the principle of equity and natural justice.

Transfer Pricing adjustment

b. The DRP and the AO erred in fact and in law in confirming the action of the TPO in making an adjustment amounting to Rs.76,342,156/-to the ALP of the international transactions of the assessee.

c. The DRP and the AO have erred in upholding the action of the TPO in rejecting the TP documentation maintained and the detailed bench marking analysis conducted by the assessee, which has been prepared by the assessee in the matter as contemplated under the relevant provisions of the Act and the IT Rules, 1962.

d. The DRP and the AO have erred in upholding the action of the TPO in disregarding the multiple/prior year

data considered by the assessee in determining the ALP and adopting the financial data for a single year (i.e the financial year-200910 of the comparable despite the fact that same was not available to the assessee at the time of preparing the TP documentation.

e. The DRP and the AO have erred in upholding the action of the TPO in rejecting certain comparables identified by the assessee in its TP study using unreasonable comparability criteria and contrary to facts as evidenced by the audited financial statements of the said companies, despite the arguments submitted by the assessee.

f. The DRP and the AO have erred in upholding the action of the TPO in finalizing the transfer pricing order with companies as comparable to the assessee despite such companies failing the test of comparability on some or all the factors such as functional dissimilarity, product led revenues, differing turnover/scales of operation, asset base, risk profile etc. and failure of TPO's own filters.

g. The DRP and the AO have erred in upholding the action for the TPO in adopting/modifying the filters adopted for conducting TP analysis, without appreciating the TP documentation prepared by the assessee.

h. The DRP and the AO have erred in upholding the computation of operating margins of the comparable companies and the assessee by the TPO thereby ignoring the factual errors and ignoring of certain items which ought to have been considered as operating or non-operating items, as the case may be.

i. The DRP and the AO have erred in upholding the action of the TPO in not granting the working capital/risk adjustment as claimed by the assessee.

j. The DRP and the AO/TPO erred in law and on facts in upholding the arm's length margin arrived at by the learned TPO without granting the benefit of the proviso to section 92C(2) of the Act.

Adjustments under section 10A of the Act

k. The DRP and the AO have erred in law and on facts in concluding that the telecommunication expenditure and expenditure incurred in foreign currency are to be excluded from the export turnover for the purpose of computation of relief under section 10A of the Act”.

The assessee also filed **Additional grounds** which are as under;

“a. Without prejudice to the grounds raised in the appeal set, after realizing the fact that the assessee renders similar service to both its Associated Enterprises (AE) and its non-AEs for the subject year (this is apparent from the transfer pricing order), the learned Transfer Pricing Officer (TPO) ought to have applied internal transactional net margin method (internal TNMM) for determining the ALP of the assessee. The learned Dispute Resolution Panel (DRP) has erred in upholding the approach followed by the TPO and;

b. The DRP has erred in suo-moto rejecting Sundaram Business Services Limited as a comparable to the assessee by applying an inappropriate filter even after learned TPO having found that it is comparable to the assessee for the subject year”.

7. First we shall adjudicate the Additional grounds. The learned counsel for the assessee submitted that several rulings of the Hon'ble Tribunal, subsequent to the petitioner finalizing its TP study have accepted internal ALP in case the assessee renders similar services to both Associated Enterprises (AE) and non-AE's. The counsel relied on the decision in the case of Mylan Labs Ltd. I(TP)A No.179/Bang/2015 and 214/Bang/2015.

7.1 We find that in IT(TP)A No.214/Bang/2015 and IT(TP)A No.179/Bang/15 in the case of M/s Mylan Labs Ltd. at para-10 it has been held as follows;

“10. The TPO had applied external TNMM on entity level and on this issue, the Third Member decision of the Mumbai Bench of the Tribunal in the case of M/s. Technimont ICB Pvt. Ltd. v. Addl. CIT in ITA No.4608/Mum/2010 for AY 2005-06, order dated 17.7.2012 is relevant. In para 10 of the said order, the Tribunal held as under:-

“10. Clause (i) of Rule 10B(e) stipulates that net profit margin from an international transaction with an AE is computed in relation to cost incurred or sales effected or assets employed etc.

Clause (ii) is material for the present purpose. It provides that the net profit margin realized 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. The 'base' of this provision takes one back to clause (i) which refers to cost incurred or sales effected or assets employed or to be employed. On splitting clause (ii) into two parts, it divulges that the reference is made to internal and external comparables. One part of clause (ii) refers to the net profit margin realised by the enterprise from a comparable uncontrolled transaction' and the other part talks of the net profit margin realised by an uncontrolled enterprise from a comparable uncontrolled transaction'. It transpires that whereas the first part refers to the profit margin from internal comparable uncontrolled transactions, the second part refers to profit margin from an external comparable uncontrolled transaction. Thus it is discernible that what is to be compared under this method is profit from a comparable uncontrolled transaction. The word 'comparable' may encompass internal comparable or external comparable. There is cue in the rule itself as to preference to be given to internal comparable uncontrolled transactions vis-à-vis externally comparable uncontrolled transactions. It is because the delegated legislature has firstly referred to the net profit margin realized by the enterprise (internal) from a comparable uncontrolled transaction and, thereafter, it points towards net profit margin realized by an unrelated enterprise (external) from a comparable uncontrolled transaction. Thus where potential comparable is available in the

shape of an uncontrolled transaction of the same assessee, it is likely to have higher degree of comparability vis-à-vis comparables identified amongst the uncontrolled transactions of third parties. The underlying object behind computing ALP of an international transaction is to find out the profits which such enterprise would have earned if the transaction had been with some third party instead of related party. When the data is available showing profit margin of that enterprise itself from a third party, it is always safe and advisable to have recourse to such internal comparable case. The reason is patent that the various factors having bearing on the quality of output, assets employed, input cost etc. continue to remain by and large same in case of an internal comparable. The effect of difference due to such inherent factors on comparison made with the third parties, gets neutralized when comparison is made with internal comparable. Ex consequenti, it follows that an internal comparable uncontrolled transaction is more noteworthy vis-à-vis its counterpart i.e. external comparable.”

11. It has also been brought to our notice that in the subsequent year i.e. AY 2011-12, the TPO has accepted the internal comparability.

12. The Id. DR relied on the order of DRP.

13. We are in conformity and are inclined to follow the decision of the Third Member, ITAT Mumbai Bench in the case of M/s. Tecnimont ICB Private Ltd. (supra) wherein it is held that “..... The underlying object behind computing ALP of an international transaction is to find out the profits which such

enterprise would have earned if the transaction had been with some third party instead of related party. When the data is available showing profit margin of that enterprise itself from a third party, it is always safe and advisable to have recourse to such internal comparable case.”

14. Hence we are of the opinion that the TPO had erred in choosing an external comparable, when there was an internal comparable uncontrolled transaction which the assessee had taken in its TP study. The assessee’s appeal is allowed”.

Respectfully following the decision of the Co-ordinate Bench authored by JM in this appeal, we direct the TPO to choose internal comparable in controlled transaction as against an external comparable. Hence, we conclude our decision as follows;

8. Ground no.1 & 2 are general in nature and needs no adjudication. Ground no.3,4 & 5 are not pressed. Ground no.7,8 & 9 are infructuous and ground no.6 & 10 are allowed.

8.1 With respect to ground no.11, we hereby summarize the proceeding as follows;

8.2 During the course of assessment proceedings for AY: 2010-11 the international transactions entered into by the company were referred by the AO to the TPO for determination of arm’s length price. On conclusion of the transfer pricing proceedings, the TPO passed an order dated January 30,2014 proposing an adjustment of Rs.61,981,771/- under section 92CA of the Act.

8.3 Taking the above order into consideration, the AO concluded the assessment proceedings and passed a draft assessment order on February 20, 2014 (served on Feb. 24, 2014) in the DAO, the AO reduced telecommunication expenses of Rs.13,090,703/- and travelling expenses incurred in foreign currency of Rs.731,249 from the adjusted export turnover and added similar amounts to the adjusted total turnover of the company. Based on such adjustment, the AO re-computed the relief under section 10A of the IT Act at Rs.25,131,114/- as against a claim of Rs.26,977,360/- thereby resulting in an upward adjustment of Rs.1,846,246/- to the total income of the company. The AO was of the view that the aforementioned expenses need to be reduced only from the ET and no such reduction was warranted from the TT. As per the AO, even though the subject issue of reduction of expense from both ET and TT has been decided by the jurisdictional Karnataka High Court in favour of the assessee, since the revenue has preferred an appeal against the said decision and the issue has not reached finality, the adjustment has been proposed.

8.4 M/s e4e filed its objections before the DRP on March 24, 2014. The DRP vide its directions dated Nov. 26, 2014 partly confirmed the additions made by the AO in the DAO. The DRP rejected some of the comparable companies adopted by the TPO and consequent to such rejection, the adjustment under section 92CA of the Act increased to

Rs.76,342,156/-. Based on the decision of the KHC in the case of Tata Elxsi Ltd., the DRP directed the AO to reduce the telecommunication expenses and travel expenses incurred in foreign currency from both the IT & TT. As M/s e4e is not a 100 percent export oriented unit, such adjustment from both the ET and TT reduced from the addition on account of re-computation of relief under section 10A of the Act, to Rs.585,520/-.

8.5 Subsequently, a final assessment order was passed on December 30,2014 (served on Jan 6, 2015) As per the final assessment order the AO determined the total income of e4e at Rs.100,873,056 and thereafter raised a demand for tax of Rs.42,605,150/-.

8.6 Against the final assessment order both assessee and the department are in appeal. The assessee has raised ground no.11. The ground raised in the department appeal in IT(TP)A No.220(B)/2015 is as follows;

“1. The directions of the DRP are opposed to law and facts of the case.

2. On the facts and in the circumstances of the case the DRP erred in law in directing the AO to exclude reimbursement of specific expenditure both from the export turnover as well as from total turnover for the purpose of computation of deduction u/s 10A, without appreciating the fact that the

statute allows exclusion of such expenditure only from export turnover by way of specific definition of export turnover as envisaged by Sub-clause(4) of Explanation 2 below Sub-section (8) of Section 10A and the total turnover has not been defined in this section.

3. On the facts and circumstances of the case the DRP erred in directing the AO to compute deduction u/s 10A in the above manner by placing reliance on the decision of Hon'ble High Court of Karnataka in the case of M/s Tata Elxsi Ltd. which has not become final since the same has not been accepted by the Department and SLPs are pending before the Hon'ble Supreme Court.

4. For these and other grounds that may be urged at the time of hearing, it is prayed that the directions of the DRP in so far as it relates to the above grounds may be reversed.

5. The assessee craves leave to add, alter, amend and/or delete any of the grounds mentioned above”.

9. The learned counsel for the assessee submitted before us that the telecommunication expenses and travel expenses incurred in foreign currency should not be reduced from both ET and TT as the same have not been incurred towards rendering of technical services outside India as contemplated under section 10A of the Act.

9.1 The learned counsel for the assessee submitted that the second limb of the definition of ET under section 10A of the Act, provides for exclusion of expenditure incurred in foreign currency in connection with providing **'the'** technical services outside India. The presence of the word

'the' before the term 'technical service' indicates that the assessee needs to provide a particular or specific technical service outside India and expenses incurred in foreign currency in providing those technical services are to be excluded. Accordingly, this clause of exclusion of foreign currency expenditure would be applicable only if the assessee is providing technical services outside India. The above argument has been upheld in the following decisions;

Jurisdictional Bangalore Bench of the ITAT in the case of Infosys Technologies Ltd. (108 TTJ 282).

Jurisdictional Bangalore Bench of ITAT in the case of Robert Bosch Engineering and Business Solutions Ltd. in ITA No.412/Bang/2011).

Chennai Bench of ITAT in the case of iNautix Technologies Pv.Ltd. (ITA Nos.541/Mds/2006, 1439/Mds/2007, 20191/Mds/2010 to 2093/Mds/2010).

Chennai Bench of ITAT in the case of Cognizant Technologies Solutions India Pvt.Ltd. (ITA No.209/Mds/2007); and

Hyderabad Bench of ITAT in the case of Patni Telecom Pvt.Ltd. (308 ITR 414).

9.2 We have heard both parties.

Following the Patni Telecom Pvt. Ltd., we are of the opinion, that e4e is not involved in rendering technical services outside India, but it in the business of export of BPO services as contemplated under the provisions of section 10A of the Act from its offshore centre in India. It is not engaged in rendering onsite services and therefore,

telecommunication expenses and travel expenses incurred in foreign currency should not be excluded from the ET and TT in computing the eligible relief under section 10A of the Act.

9.3 Further, BPO services, undertaken for the purposes of export cannot be equated to providing technical services outside India solely for the purpose of excluding travel expenses incurred in foreign currency from the ET as envisaged in the definition of 'export turnover' as provided in section 10A of the IT Act. Accordingly, the adjustment made by the AO is to be quashed in entirety. We direct the AO to re-work the same. Since we have decided ground No.11, in assessee's appeal the grounds raised by revenue in IT(TP)A No.220(B)/2015 are dismissed.

10. In the result, the appeal of the assessee is allowed for statistical purposes and the revenue's appeal is dismissed.

Order pronounced in the open Court on the 4th day of November, 2015.

Sd/-
(JASON P BOAZ)
ACCOUNTANT MEMBER

D a t e d : 04-11-2015

Place: Bangalore

am*

Copy to :

- 1 Appellant
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Sd/-
(ASHA VIJAYARAGHAVAN)
JUDICIAL MEMBER

By order

AR, ITAT, Bangalore