

INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "I-1": NEW DELHI

BEFORE SHRI BHAVNESH SAINI, JUDICIAL MEMBER
AND
SHRI PRASHANT MAHARISHI, ACCOUNTANT MEMBER

ITA No. 6648/Del/2016
(Assessment Year: 2012-13)

McKinsey Knowledge Centre India Pvt. Ltd, 3 rd Floor, Block-III, Vatika Business Park, Sector-49, Sohna Road, Gurgaon PAN:AACCM2356G (Appellant)	Vs.	DCIT, Circle-16(2) New Delhi (Respondent)
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Assessee by :	Shri Porus Kaka, Senior Advocate Shri Dinesh Chawla, Adv
Revenue by:	Shri Amrendra Kumar, CIT DR
Date of Hearing	19/04/2017
Date of pronouncement	11/05/2017

ORDER

PER PRASHANT MAHARISHI, A. M.

1. This is an appeal filed by the assessee [hereinafter referred to as ' Appellant' also] against the assessment order [hereinafter referred to as the 'order' also] of the Id Deputy Commissioner of Income Tax , Circle 16(2), New Delhi [hereinafter referred to as the 'AO'] dated 25/11/2016 u/s 143(3)(ii) r.w.s 144C(5) of the Income tax Act [In short 'the Act'] passed in pursuance of direction dated 29/09/2016 by the Learned Dispute Resolution Panel- 2, New Delhi [hereinafter referred to as 'The DRP'] against the draft assessment order dated 14/03/2016 incorporating transfer pricing adjustment determining the Arm's length price [The ALP'] of International Transactions u/s 92CA made by Id Deputy Commissioner of Income Tax , Transfer

pricing officer -2 (2) (2), New Delhi [Hereinafter referred to as 'The TPO'] vide order dated 29/01/2016 for AY 2012-13.

2. The assessee has raised the following grounds of appeal:-

“On the facts and circumstances of the case and in law, the learned Assessing Officer ("AO") has erred in passing the assessment order under section 143(3) read with section 144C of the Income-tax Act, 1961 ("the Act") after considering the adjustments proposed by the learned Deputy Commissioner of Income Tax, Transfer Pricing Officer-2(2)(2), New Delhi ("TPO") in his order passed under section 92CA(3) of the Act and subsequently confirmed by the Hon'ble Dispute Resolution Panel ("DRP").

Each of the ground is referred to separately, which may kindly be considered independent of each other.

That, on the facts and circumstances of the case and in law:

1. *The learned TPO/AO/DRP have erred in making an addition of INR 126,607,828 to the total income of the Appellant in respect of international transaction pertaining to provision of research & information ("R&I") services by the Appellant to its associated enterprises ("AEs") and notional interest on inter-company receivables arising therefrom (hereinafter referred to as "impugned transaction").*
2. *The learned TPO / AO / DRP have erred in not accepting the economic analysis undertaken by the Appellant in accordance with provisions of the Act read with the Income-tax Rules, 1962 ("the Rules") and modifying the same for determination of arm's length price ("ALP") of the impugned transaction to hold that the same are not at arm's length.*
3. *The learned TPO/ AO/ DRP failed to understand and appreciate the functions performed, assets employed and risks assumed by the Appellant and its AEs, thereby comparing companies engaged in different filed with the Appellant*
4. *The learned TPO/ AO / DRP erred in passing order on incorrect factual assumption which is incorrect as per the records and submission made by the Appellant.*
5. *The learned TPO / AO / DRP have erred in:*
 - a. *Not accepting the use of multiple year data, as adopted by the Appellant in its Transfer Pricing ("TP") documentation; and*
 - b. *Determining the arm's length margins / prices using data pertaining only to financial Year ("FY") 2011 -12 which was not available to the Appellant at the time of complying with the Indian TP documentation requirements*
6. *The learned TPO / AO / DRP have erred in rejecting certain comparable companies selected by the Appellant in respect of impugned transaction pertaining to provision of R&I services, namely:*
 - a. *Indus Technical & Financial Consultants Limited; and*
 - b. *Certain other companies carrying out functionally similar operations in overseas jurisdiction*
7. *The learned TPO / AO / DRP have erred in adding certain comparable companies in respect of impugned transaction pertaining to provision of R&I services, namely:*

- a. *Aditya Birla Capital Advisors Private Limited;*
 - b. *Axis Private Equity Limited; and*
 - c. *Credit Information Bureau (India) Limited*
8. *The learned TPO / AO / DRP have erred in erroneously rejecting the comparable companies selected by the Appellant and adding certain companies to the final set of comparable companies on an ad-hoc basis, thereby resorting to cherry picking of comparables to determine ALP of the impugned transaction.*
 9. *The learned TPO / AO / DRP have erred in rejecting certain comparable (which were loss making) and selecting certain companies (which are earning super normal profits) as comparable to the Appellant.*
 10. *The learned TPO / AO / DRP have erred by not considering gains/ losses arising out of foreign exchange fluctuations while computing operating margins of comparable companies even though the same is considered as operating while computing operating margin of the assessee.*
 11. *The learned TPO / AO / DRP have erred in treatment of operating and non-operating items while computing the margins of the Appellant and comparable companies, and passed an order which also suffers from several computational errors in computation of margins of a comparable company (viz. Axis Private Equity Limited).*
 12. *The learned TPO / AO / DRP have erred in not making suitable adjustments to account for differences in the working capital position of the Appellant vis-a-vis the comparable companies, which is contrary to his finding that the operating margins of the comparables should be adjusted for the differences in level of working capital.*
 13. *The learned TPO / AO / DRP have erred in not making suitable adjustments to account for differences in the risk profile of the Appellant vis-a-vis the comparable companies.*
 14. *The learned TPO / AO / DRP have erred in holding inter-company receivables arising from provision of R&I services to constitute a separate international transaction under section 92B of the Act. The learned TPO / AO / DRP have further erred in proceeding to benchmark the said transaction pertaining to inter-company receivables by rejecting economic analysis carried out in TP documentation and purported application of Comparable Uncontrolled Price ("CUP") method.*
 15. *The learned AO has grossly erred in initiating penalty proceedings under section 271(1)(c) of the Act.*
 16. *The learned AO has erred in levying interest under section 234D of the Act while completely disregarding the provisions of the Act and the judicial precedence."*
3. Briefly stated, the facts are that assessee is a resident company engaged in the business of providing IT enabled services such as data processing, customization of

electronic data, back-office operations and acting as a support centre to provide research, analysis and information to various McKinsey and other corporate entities across the globe. For the assessment year 2012 – 13, it filed its return of income declaring income of Rs. 319140070/- on 29/11/2012. Assessee also filed form 3CEB on 29/11/2012 to show that it has entered into international transactions with its associated enterprises for provision of research and information services of Rs. 1788476202/- and provision of IT support services of Rs. 64779181/-. Therefore, the Ld. assessing officer made reference u/s 92CA to the Ld. Transfer Pricing Officer to determine arm's length price of the international transaction of the assessee with its associated enterprises.

4. According to the transfer pricing documents maintained by assessee, the international transaction of provision of research and information services as well as of provision of IT support services were benchmarked using the transactional net margin method (TNMM) as the most appropriate method (MAM) and profit level indicator (PLI) was determined as operating profit/operating cost (op/oc).
5. Assessee's services are governed by the Master service agreement dated 1/4/2010 with its AE/ Parent company where in assessee is responsible for providing services of research and Information and IT Support services at remuneration of cost + 15 %.
6. For its research and information services of Rs. 1788476202/-, assessee selected 18 comparables whose average of adjusted operating margins was 14.50% on operating cost. Assessee earns operating margin of 15% on operating cost from research and information services transaction, which is higher than the adjusted arithmetic mean of the margins of the comparable companies that is 14.50%. Hence,

assessee submitted that research and information service transaction between assessee and its associated enterprise are at arm's length.

7. For its provision of IT support services of Rs. 64779181/–, the assessee selected nine comparable companies having average of adjusted operating margin of 14.98% on operating cost. Appellant company earns operating margin of 15% on operating cost from IT support services transactions, it was said that as the operating margin of the assessee is higher than the adjusted automatic mean of the margins of the comparable companies of 14.98%. Hence, IT support services transaction between assessee and its associated enterprises are at arm's length.
8. On examination of the transfer-pricing document of the assessee, the Ld. Transfer Pricing Officer mentioned that assessee has used one source global business browser that also contained information about the global companies and therefore according to the Ld. Transfer Pricing Officer, it is not suitable as the assessee is an Indian entity. Further, he discussed the accept /reject matrix applied by the assessee and then proposed new filters, rejected foreign entities as comparable and selected additional comparables. Ultimately, the Ld. Transfer Pricing Officer selected eight comparables whose average PLI of OP/OC was computed at 36.48%. Based on this arm's length price of total operating cost of Rs. 1591939738/– at 36.48% was computed at Rs. 2172679354/- against the transfer pricing received by the taxpayer of Rs. 1830740209/- and therefore shortfall was determined at Rs. 341939154/-. The Ld. Transfer Pricing Officer further proposed an adjustment on account of outstanding receivables and interest thereon amounting to Rs. 1490875/–. In the result total adjustment on account of the arms length price of the provision of research and information services was at Rs. 343430020/-. In the result Ld. Transfer Pricing Officer passed order under section 92CA of the income tax act 1961 on

29/01/2016 proposing the above addition. Consequently, the Ld. assessing officer passed draft order under section 143 (3)/144C (1) of the income tax act, 1961 on 14/03/2016 determining the total income of the assessee at Rs. 662570090/- against the returned income of Rs. 319140070/- proposing a transfer pricing adjustment amounting to Rs. 343430020/-. Assessee being aggrieved with the order of the Ld. Transfer Pricing Officer as well as the Ld. assessing officer preferred objections before the Ld. Dispute Resolution Panel. The Ld. Dispute Resolution Panel vide direction dated 29/09/2016 rejected the objection of the assessee with respect to exclusion of three comparable companies and accepted the exclusion of one comparable company. Further with respect to the company is rejected by the Ld. Transfer Pricing Officer; it gave direction with respect to the one company for its inclusion and with respect to another company for verification of our on examination of financial data. Pursuant to the direction of the Ld. Dispute Resolution Panel, the Ld. Transfer Pricing Officer vide its order dated 10/11/2016 revise the original adjustment of Rs. 343430020/- to Rs. 126607828/-. Consequently, the Ld. assessing officer passed final assessment order under section 143 (3) read with section 144C of the Income tax act, 1961 on 25/11/2016 wherein the returned income of the assessee of Rs. 319140070/- was assessed at Rs 445747898/ - incorporating therein addition as per the transfer pricing adjustment of Rs. 126607828/-. Assessee being aggrieved with the order of the Ld. assessing officer has preferred appeal before us as per grounds of appeal incorporated above.

9. Though assessee has raised 16 grounds of appeal in all however, the Ld. senior advocate appearing on behalf of the assessee submitted that in substance assessee is pressing ground No. 7 of the appeal for exclusion of 3 comparable companies which are functionally not similar to the functions of assessee. He further submitted

that ground No. 10 of the appeal is whether the gains or losses arising out of the foreign exchange fluctuation shall be considered as part of operating profit or losses while computing the operating margin of the comparables. He submitted that this issue is squarely covered in favour of the assessee as per Para No. 64 – 68 of the order of the coordinate bench in assessee's own case for assessment year 2011 – 12. It was further submitted that ground No. 11 of the appeal is consequential in nature as, if the comparables contested in ground No. 7 are accepted for exclusion, then ground No. 11 does not survive. It was further stated that ground No. 14 of appeal is with respect to decision of the intercompany receivable arising from provisions of research and information services to constitute a separate international transactions under section 92B of the income tax act, he submitted that this issue is already decided against the assessee in its own case for earlier years and therefore same is covered against the assessee. For this, he referred to page No. 58 – 63 of the order of the coordinate bench in assessee's own case for assessment year 2011 – 12 wherein interest on late realization of invoices is considered an international transaction and it was directed to the assessing authority to charge interest on late realization of the invoices. Furthermore, ground No. 15 and 16 of the appeal are consequential in nature. From this aspect, he proposed to contest the three comparables covered in ground No. 7 of the appeal of the assessee.

10. Coming to the issues in appeal, he submitted that assessee is a company, which provides research and information services to its group associate for assistance in their projects. Its response to the information required to queries request placed by the consultant by accessing various Internet-based databases such as Bloomberg, Reuters, OneSource, Dow Jones, dialogue, and DataStream. He further submitted that assessee operates in two streams of services. First segment is research and

information segment and second segment is IT supports services. He submitted that transfer pricing adjustment are proposed with respect to international transaction of 1st segment only and with respect to 2nd segment, the Ld. Transfer Pricing Officer has accepted the benchmarking analysis of the assessee. Therefore, it submitted that first segment of research and information services are further divided in 3 segments such as knowledge on-call group, practice research group and analytics group. He referred to Para No. 3.4 of order of Ld. Transfer Pricing Officer wherein the detailed work profile and functional analysis of this segment is considered. Further submitted that assessee is raising invoices based on cost +15% in terms of its agreement with its associated enterprise. He further referred to page No. 6 of order of Ld. Transfer Pricing officer wherein employee profile of company is considered. He made a specific reference that Ld. Transfer Pricing Officer has considered employee profile of the McKinsey India and not of assessee and therefore whole discussion about employee profile and its correlation with employee details of assessee becomes irrelevant. After referring to functional profile of assessee and drawing our attention to various reasons stated by Ld. Transfer Pricing Officer, he referred to page No. 483 to page No. 560 wherein the sample copies of request received by assessee from its associated enterprise along with deliverable provided to them. In nutshell, he explained nature of services assessee is providing in this segment.

11. Based on above submission, he stated that out of five comparable companies assessee is objecting to inclusion of three comparables as under.
 - i. Aditya Birla capital advisors private limited
 - ii. Axis private equity Ltd
 - iii. credit information bureau (India) Ltd

12. With respect to Aditya Birla capital advisors private limited, he referred to page No. 445 of paper book where annual accounts of comparable company for year ended on 31 March 2012 are placed. He submitted that this company is engaged in business of managing venture capital funds as investment manager and therefore it is functionally not comparable. He also referred to annual accounts submitted at page No. 456 onwards of Axis private equity Ltd to submit that it is also investment manager of various funds and therefore cannot be compared with functions of assessee. For credit information bureau (India) (CIBIL) Ltd, he submitted that annual report provided by Ld. Transfer Pricing Officer was with respect to financial year 2012 – 13 and not for 2011 – 12, which are placed at page No. 273 onwards and submitted that this company is engaged in business of credit rating. Therefore, he submitted that in case of 2 comparables are functionally different and in case of 3rd comparable no information was provided to the assessee relevant to financial year for which issue is concerned and therefore all 3 comparables are required to be removed from comparability analysis.
13. The Ld. departmental representative, CIT – DR, submitted that functional profile of assessee is required to be seen. He referred to order of coordinate bench in assessee's own case for assessment year 2011 – 12 wherein from page No. 10 to page No. 21 of that order wherein after considering services of research and information services, ultimately coordinate bench has held that assessee is rendering knowledge process outsourcing services under this segment involving huge expertise and skills. Therefore he submitted that Ld. Transfer Pricing Officer did not have advantage of order of coordinate bench and therefore has accepted functional profile of assessee as it is and therefore now coordinate bench as well as Hon'ble high court has held that assessee is engaged in services as KPO,

therefore now matter should go back to Ld. Transfer Pricing Officer to verify and examine comparability analysis from that angle. He vehemently contested that if matter is not sent back to file of Ld. Transfer Pricing Officer once again then it would lead to deciding case of assessee on incorrect characterization of services rendered by assessee. He further submitted that despite being held to be KPO, selection of comparables was carried out by assessee on basis of BPO and Ld TPO carried same impression. On merits of comparables regarding its exclusion or inclusion, he relied upon order of Ld. Transfer Pricing Officer and Ld. Dispute Resolution Panel.

14. In rejoinder, Ld. senior advocate submitted that it is immaterial whether assessee is classified as KPO or BPO even though coordinate bench has already decided this issue based on order of Hon'ble high court in assessee's own case for earlier year wherein claim of eligibility of deduction under section 10 A of income tax act was decided. He submitted that Hon'ble Delhi High Court in 361 ITR 85 (Delhi) in Li & Fung India private limited versus CIT has held that even in case of TNMM strict criteria is of independent enterprise, carrying out a comparable transaction, with caveat that this will only be a guide. Indeed, emphasis is very clear on finding a comparable transaction. Therefore he submitted that functional analysis of both the associated enterprise and independent enterprise is required to be determined if the transactions are comparable. Further submitted that even in case of TNMM, standard of comparability for application is not less than application of any other transfer pricing method. He further referred to decision of Hon'ble Delhi High Court in case of Rampgreen solutions (P) Ltd versus CIT (Delhi) 377 ITR 533 and submitted that even in case of TNMM comparability analysis for identifying comparables cannot be different then other transfer pricing methods. Hence,

according to him de hors whatever is held by the courts, for transfer pricing analysis comparables should be selected who are having service of same character performing similar functions and having similar level of assets and risks.

15. We have carefully considered rival contentions and perused orders of Ld. Transfer Pricing Officer as well as direction of Ld. Dispute Resolution Panel. Firstly, we deal with argument of Ld. CIT DR who has vehemently submitted that assessee is a KPO and comparables have been selected by assessee on basis of it being characterized as BPO. It is an admitted fact that coordinate bench in its order dated 15/12/2016 for assessment year 2011 – 12 in ITA No. 154/del/2016 has held that research and information services provided by the assessee are falling into bracket of KPO services. The mandate of provisions of income tax act and rules with respect to comparability analysis are laid down in rule 10 B (2), wherein it is laid down that:-

“(2) For the purposes of sub-rule (1), the comparability of an international 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 ;

(c) 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.”

In rule No. 10B(1) various methods of carrying out benchmarking determination of arm's length price are mentioned. In view of this, it is apparent that for all methods mentioned in rule 10 B (1), four criteria laid down in rule 10 B (2) shall be followed. On examination of income tax act and income tax rules , it is evident that for comparability analysis, information technology enabled services are not bifurcated in strict compass of business process outsourcing (BPO)/ knowledge process outsourcing (KPO) or any other characterization except in case of 10 TC wherein safe harbour rules are provided. Therefore, in our opinion for comparability analysis strictly rule 10 B is required to be complied with. In view of this, though assessee is characterized as knowledge process outsourcing service provider, we would be restricting ourselves in comparing specific characteristics of services, FAR analysis of assessee, contractual terms and economic analysis. While doing so, we are guided by decision of Hon'ble Delhi High Court in Rampgreen solutions private limited versus CIT 377 ITR 533 wherein it is held that:-

“43. In our view, the aforesaid approach would not be apposite. In so far as identifying comparable transactions/entities is concerned, the same would not differ irrespective of the transfer pricing method adopted. In other words, the comparable transactions/entities must be selected on the basis of similarity with the controlled transaction/entity. Comparability of controlled and uncontrolled transactions has to be judged, inter alia, with reference to comparability factors as indicated under rule 10B(2) of the Income-tax Rules, 1962. Comparability analysis by the transactional net margin method may be less sensitive to certain dissimilarities between the tested party and the comparables. However, that cannot be the consideration for diluting the standards of selecting comparable transactions/entities. A higher product and functional similarity would strengthen the efficacy of the method in ascertaining a reliable arm's length price. Therefore, as far as possible, the comparables must be selected keeping in view

the comparability factors as specified. Wide deviations in profit level indicator must trigger further investigations/analysis.

44. Consideration for a transaction would reflect the functions performed, the significant activities undertaken, the assets, or resources used/consumed, the risks assumed. Thus, comparison of activities undertaken/functions performed is important for determining the comparability between controlled and uncontrolled transactions/entity. It would not be apposite to ignore functional dissimilarity only for the reason that its impact may be reduced on account of using arithmetical mean of the profit level indicator.”

Similar guidelines for also laid down by the Hon’ble Delhi High Court in case of Li and Fung India (P) Ltd versus CIT in 361 ITR 85 as under:-

“34. The OECD Guidelines, which are instructive in such cases, clarify that any attempt to use the transactional net margin method should begin by comparing the net margin which the tested party makes from a controlled transaction with the net margin it makes from an uncontrolled one (an "internal comparable"). If this proves impossible, possibly if there are no transactions with uncontrolled parties, then the net margin that would have been made by an independent enterprise in a comparable transaction (an "external comparable") serves as a guide to determine the arm's length price. Here, the strict criterion is of an independent enterprise, carrying out a comparable transaction, with the caveat that this will be only a guide. Indeed, the emphasis is very clearly on finding a comparable transaction. In addition, a functional analysis of both the associated enterprise and the independent enterprise is required to determine if the transactions are comparable. It might of course be possible to adjust results for minor functional differences, provided that there is sufficient comparability to begin with. The standard of comparability for application of the transactional net margin method is not less than that for the application of any other transfer pricing method.”

In view of this, we do not find it necessary to accede to the request of Ld. CIT DR to set aside the issue back to the file of the Ld. Transfer Pricing Officer because originally the assessee has also selected comparables based on the criteria laid down under rule 10 B (2) of the income tax rules and while accepting the comparables, the Ld. Transfer Pricing Officer has also looked into the broader functional comparability of the comparables selected and further It is also not apparent from the order of the Ld. Transfer Pricing Officer or from the transfer pricing study report of the assessee that any of the parties have taken the criteria of BPO versus KPO in selection of the comparables.

16. Now coming to the functional profile of research and information services provided by assessee, which is divided into 3 broad subgroups of knowledge on-call, practice research, and analytics. This is in terms of agreement dated 01/04/2010 titled as Master service agreement dated 01/04/2010 between assessee and its associated enterprise wherein assessee is responsible for providing research and information services to its associated enterprises.
 - i. In first subgroup of knowledge on-call assessee provides research and information reports. The services offered includes financial analysis, fact packs, press search, document search etc by employing around hundred personnel with experience scale of 0 to 2 years.
 - ii. In practice research group assessee is focused on domain specific research support with team size of over 240 people, which provides sector data and analysis, capital market insights, perspectives and industry trends.
 - iii. In analytics group, assessee primarily focuses on data intensive analysis requiring expertise in analytical tools and techniques., database management, etc.

17. Our and above examination of the agreement it is also pertinent to examine what services are actually performed by the assessee. We also perused for ascertaining correct function being performed by assessee based on sample copies of service request and its deliverables placed before us at page No. 483 – 560. At page No. 483 research request is been received by assessee for knowing current top 5 global retail markets as well as top 5 global retail markets in 2015. Further, it was also requested to know top five markets for retail private-label credit cards for same two times. The above services were rendered by assessee, which is placed at page No. 484 of paper book wherein data was sourced from global insight WIS and such data was sorted by assessee based on sales on country and region wise. At page No. 485 to 488 excel sheet is submitted, which has country wise bifurcated retail trade industry with respect to 2005 to 2015. At page No. 491, another request was placed where data was to be sourced from global insight/WMM for all countries regarding import and export. In nutshell, a compilation of data was to be provided. At page No. 492, assessee provided this information being total imports of goods and services, export of goods and services in foreign exchange reserves from 1990 – 2020 sourced from WMM in excel file. Such details were also included page No. 493 to page No. 549. Another request was shown to us to assessee wherein information of market Had quieter location stock exchange is required with respect to listed companies from Bloomberg. Assessee provided this information from Bloomberg and one source database. Such reports were provided at page number 554 to 560. From these sample requests, it is noted that assessee is subscriber to some database and information is retrieved from these database, indexed in required format, and provided. No further addition in form of opinion, etc, is given. Therefore, it is apparent that assessee is engaged in data retrieval from

various software, which is publicly available on payment of subscription. This functional profile is not disputed by revenue.

18. The Ld. Transfer Pricing Officer at page number 4 of his order, further discusses detailed work profile and he has held that research and information services over years, assessee had been showing good margins at net level in this segment. Thereafter he discussed history of margins are not by assessee from year 2008 – 09 to 2000 1011 wherein margins have fluctuated from 131.48%, 53.34%, 15.17% to 15% in current year. According to Ld. Transfer Pricing Officer, drop in margin is because of reason that Indian company is now being remunerated at cost +15% in terms of agreement dated 01/04/2010. Further, Ld. Transfer Pricing Officer made reference to McKinsey India website and noted what types of work and employees does and what type of skill he should possess to get employment with McKinsey India. Based on this he further looked at employee profile and held that that companies indulge in providing high-end services in terms of research and information segment assessee is offering knowledge-based services and hence it is required to be benchmarked with comparables engaged in research-based services. As already held by coordinate bench in assessee's own case in assessment year 2011 – 12 that assessee is providing knowledge-based research and information services. There cannot be a serious question about whatever has been mentioned by Ld. Transfer Pricing Officer except grievance of assessee that he has looked at website of McKinsey India and not of assessee. In view of this, we do not find it necessary to dwell further on functional analysis of business information and research segment of services of assessee. In addition, therefore it is now necessary to go to comparable straightway.

19. The first comparable contested by assessee is Aditya Birla capital advisors private limited whose adjusted margin is taken by Ld. Transfer Pricing Officer at 27.82%. Before Ld. Transfer Pricing Officer wide letter dated 18/01/2016 assessee has objected for selection of this comparable stating that this company is engaged in business of private equity advisory and investment management for Indian and offshore investors across capital markets, investment management, mergers and acquisitions, performance enhancement, organizational development and shareholder value creation. It was further submitted that this comparable is managing investment of private equity funds of Aditya Birla group in name of fund 1 and Sunrise fund. The assessee further referred to website of company to show that assessee is engaged in business of private equity advisory and investment management for Indian and offshore investors. In view of this, it was submitted that that functional profile of assessee with this company is incorrect. The Ld. Transfer Pricing Officer rejected contention of assessee and referred to website of Aditya Birla private equity. On basis of this, he held that writ company is not a functionally dissimilar company and process all filters applied by TPO. We have carefully considered rival contentions and perused annual accounts of company placed before us at page No. 445 – 455. According to director's report of that company it manages two Aditya Birla private equity funds namely fund - 1 and Sunrise fund. During year it is managing investment agreement to Rs. 2 20 crores in fund No. 1 and 298.62 crores in Sunrise fund. On looking at note No. 11 to profit and loss account, revenue from operation of assessee is management fees from these two funds. According to note No. 16, it is also apparent that company is an investment manager and providing financial advisory services. In revenue recognition, It recognizes its revenue from management fees in accordance with investment

management agreement with fund and for this reason, it also incurs distribution cost. On looking at profit and loss account, revenue stream of company does not show any income, Specifically, from advisory services, but total income is from management fees. It is apparent that assessee is a fund manager. The coordinate bench had occasion to consider same comparable in assessee's own case for assessment year 2011 – 12 , wherein it was directed to exclude above comparable as under:-

“(i) Aditya Birla Capital Advisors Pvt. Ltd.,

26.1. The TPO proposed this company as comparable which was objected by assessee on ground that it was a company rendering asset management services and, hence, functionally dissimilar. The TPO treated it as comparable, which was approved by DRP. The assessee is aggrieved against such inclusion.

26.2. After considering rival submissions and perusing relevant material on record, we find that this company, as noted by TPO himself on page 20 of his order : `offers Investment Management and advisory services as Aditya Birla Private Equity to domestic and global investors'. This company is `managing a series of private equity funds to invest in and harvest business growth opportunities'. When we view Annual report of this company, a copy of which is placed on page 246 of paper book, it turns out that: "The company's focus continues on alternative assets excluding Realty and Hard Infrastructure investments. At current activity levels, Company has raised and managements two sector- agnostic domestic funds, namely, Aditya Birla Private Equity Fund-I and Aditya Birla Private Equity - Sunrise Fund'. Break-up of "Revenue from Operations" given on page 253 of paper book gives

description of nature of its revenues, namely: "Management Fees." Thus, it is apparent that nature of business of this company, being raising of funds and deploying the same, is entirely different from what the assessee is doing in this segment, namely, rendering services in the nature of Knowledge on call, Practice research and Analytics. This company is, therefore, directed to be excluded from the list of comparables."

{ Underline supplied by us }

According to us, though comparable is not engaged in business of raising of funds and deploying same, but it is engaged in advising functions of raising of funds and deploying same. Based on work profile of assessee and details of services provided as stated in Para No. 17 above, it cannot be stated that functions performed by assessee in research and information services are anywhere similar to functions of a fund manager. In view of decision of coordinate bench in assessee's own case for assessment year 2011 – 12 and also on basis of our analysis of functions of assessee vis – a – vis comparable , we direct Ld. Transfer Pricing Officer/AO to exclude Aditya Birla capital advisors private limited for comparability analysis.

20. The next comparable contested is Axis private equity Ltd, whose adjusted margin was 46.49%. The assessee objected a comparable stating that it is functionally dissimilar as it is engaged in business of capital raising solutions and earning supernormal profits. Detailed arguments were stated at page number 605 -608 of paper book The Ld. Transfer Pricing Officer rejected objection of assessee as according to him companies into services relating to research and analytics in area of finance investments and equity due to which expressed eyes and data it provided ultimate services. According to him, profile of assessee matches with this

comparable. We have carefully considered rival contentions. We have also perused annual accounts of assessee for financial year 11-12. According to director's report of company, it is stated that company is acting as an investment manager of excess infrastructure fund of 389.10 crores. It was further mentioned that company has return of a sum of Rs. 3 150 2075/- towards the expenses incurred for raising funds for 2nd closing of the excess infrastructure fund wherein the fundraising plan on account of adverse market conditions for fundraising is were dropped. Therefore it is apparent that function of the assessee is of investment manager and risk associated with this business also included incurring of huge expenditure which may go futile. The company's revenue stream is also management fees. According to the background of the company at schedule K also shows that it is carrying on the activities of managing directly or indirectly investments, managing mutual funds, venture capital funds, offshore funds, pension funds, provident funds, insurance funds or any other funds. The accounting policy of fundraising expenses also shows that the company incurs fundraising expenses, which were recovered in the end after the fundraising exercises completed and fund established. Therefore, it is apparent that it has a different risk profile too. As per the balance sheet Abstract at page No. 482 services of the company are classified as asset management services. Based on the work profile of the assessee and details of services provided as stated in Para No. 17 above, it cannot be stated that the functions performed by the assessee in research and information services are anywhere similar to the functions of a fund manager. In view of our analysis of the functions and risk profile of the assessee vis-a vis comparable, we direct the Ld. Transfer Pricing Officer/AO to exclude Axis private Equity limited for comparability analysis.

21. With respect to the third comparable the claim of the assessee is that credit information bureau India Ltd is a company, which is engaged in the business of credit rating and for this reason only, the functions of this company compared with the assessee company are quite distinct. The next argument of the assessee was that this company is earning super normal profit is 63.87% is the PLI determined of the company. Assessee further objected that the annual report of this company is not available in public domain and the balance sheet provided by the Ld. assessing officer is pertaining to financial 2012 – 13. These objections are stated at page No. 608 – 609 of the paper book. The Ld. Transfer Pricing Officer held it to be comparable, as it is engaged in providing services which are similar to that that of the assessee and are based on its core functions relating to research and analysis of the credit information being gathered from a strong base of banks, financial institutions, credit card companies, etc therefore according to the Ld. Transfer Pricing Officer, it is a robust comparable. Before us, assessee submitted the same arguments, which was submitted before the Ld. Transfer Pricing Officer strongly objected that in absence of the financial statement of this comparable not provided by the Ld. Transfer Pricing Officer on this ground itself It is required to be excluded. He further submitted that in the earlier years. The coordinate bench has already excluded a credit rating agency ICRA Ltd holding it not functionally comparable with the assessee. He referred to the annual accounts provided at page No. 273 – 444 of the compilation. We have carefully considered the above submission and we are of the view that that CIBIL is a credit rating company that is based on tranche union score version 2.0, which is a powerful predictor of risk of the borrower. It gives the credit rating of the borrower to the credit institution to help them analysis whether the borrower is worth lending or not. We have also carefully perused the orders of the

coordinate bench for the earlier years. In the case of the assessee ICRA Ltd has been excluded as comparable as it is providing credit rating services. We are of the opinion that in absence of the financial for the relevant year It is not possible for the Ld. Transfer Pricing Officer or for the assessee to find out the functions performed, assets employed and risk assumed by the comparable company. It was also not stated before us that the functions performed by this comparable company in the subsequent year (FY 12-13) are same as they were performed in earlier year (FY 11-12). Further, from the information available from the annual report of the comparable company for the subsequent year It was also noted that it is engaged in the business of credit rating and the coordinate bench in earlier years have excluded one of the credit rating companies from the comparability analysis on functional dissimilarity. Therefore, in view of the combine facts of non-availability of the information of the relevant year, the order of the coordinate bench in earlier years holding a credit rating company dissimilar to the assessee functionally, we do not have any option other than that to direct the Ld. Transfer Pricing Officer to exclude this comparable. We direct accordingly.

22. In view of this ground No. 7 of the appeal of the assessee is allowed.
23. As we have allowed. Ground No. 7 of the appeal of the assessee, consequently, we dismiss ground No. 1 to 6, 8, 9 and 11 to 13 of the appeal of the assessee are dismissed.
24. Ground No. 10 of the appeal of the assessee is that gains losses arising out of foreign exchange fluctuation while computing operating margins of the comparable companies shall be considered as part of operating profit or losses. This issue is squarely covered in the favour of the assessee by the order of the coordinate bench in assessee's own case for assessment year 2011 – 12 as under:-

“D. FOREX LOSS

64. The only issue raised by the Revenue in its appeal is against the treatment of foreign exchange (forex) gain/loss as an item of operating nature in the computation of the ALP of both the transactions. The Id. DR. submitted that such forex gain/loss was rightly considered by the TPO as non-operating in the computation of the ALP and hence such a view should not have disturbed. This was opposed by the Id. AR, who contended that forex gain/loss relates to the trading transactions of the assessee and hence the same was operating in the computation of OP/OC under the TNMM.

65. We find merit in the contention raised on behalf of the assessee about the inclusion of foreign exchange gain/loss in the operating revenue/costs of the assessee as well as that of the comparables. When we advert to the nature of such foreign exchange gain earned by the assessee, it has not been controverted by the Id. DR that the same is in relation to the trading items emanating from the international transactions. If the foreign exchange gain/loss directly results from the trading items, we fail to appreciate as to how such foreign exchange fluctuation loss can be considered as non-operating.

66. The Special Bench of the Tribunal in ACIT Vs Prakash I. Shah (2008) 115 ITD 167 (Mum)(SB) has held that the gain due to fluctuations in the foreign exchange rate emanating from export is its integral part and cannot be differentiated from the export proceeds simply on the ground that the foreign currency rate has increased subsequent to sale but prior to realization. It went on to add that when goods are exported and invoice is raised in currency of the country where such goods are sold and subsequently when the amount is

realized in that foreign currency and then converted into Indian rupees, the entire amount is relatable to the exports. In fact, it is only the translation of invoice value from the foreign currency to the Indian rupees. The Special bench held that the exchange rate gain or loss cannot have a different character from the transaction to which it pertains. The Bench found fallacy in the submission made on behalf of the Revenue that the exchange rate difference should be detached from the exports and be considered as an independent transaction. Eventually, the Special Bench held that such exchange rate fluctuation gain/loss arising from exports cannot be viewed differently from sale proceeds.

67. In the context of transfer pricing, the Bangalore Bench of the Tribunal in SAP Labs India Pvt. Ltd. Vs ACIT (2011) 44 SOT 156 (Bangalore) has held that foreign exchange fluctuation gain is part of operating profit of the company and should be included in the operating revenue. Similar view has been taken in Trilogy E Business Software India (P) Ltd. Vs DCIT (2011) 47 SOT 45 (URO) (Bangalore). The Mumbai Bench of the Tribunal in S. Narendra Vs Addtl. CIT (2013) 32 taxman.com 196 has also laid down to this extent.

68. The reliance of the Id. DR on Safe Harbour rules to contend that foreign exchange gain or loss be taken as non-operating, is not sustainable. There is no doubt that in such rules, forex gain/loss has been treated as non-operating. However it is relevant to note that such rules are not applicable to the assessment year under consideration. Even the reliance of the Id. DR on certain decisions taking cognizance of safe harbour rules for the period anterior to their insertion in other contexts does not improve the case of the

Department because the Hon'ble Delhi High Court in Pr. CIT VS. Cashedge India Pvt. Ltd., vide its judgment dated 4.5.2016 in ITA 279/2016, has held that : `So far as the question of fluctuation of foreign exchange was concerned, the ITAT ruled that the relevant provision, i.e. `Safe Harbour Rules' had not been notified for the concerned assessment year and were, therefore, inapplicable'. Thus the Hon'ble High Court did not disturb the operating nature of forex gain/loss as held by the tribunal. In view of the foregoing discussion, we are of the considered opinion that the amount of foreign exchange gain/loss arising out of revenue transactions is required to be considered as an item of operating revenue/cost, both for the assessee as well as the comparables. The ground taken by the Department is, therefore, dismissed.”

25. Ld. departmental representative could not controvert the above fact of the issue already decided in favour of the assessee in earlier years. In view of this respectfully following the decision of the coordinate bench we also hold that foreign exchange gain or loss shall form the part of the operating margin of the assessee. In the result ground No. 10 of the appeal of the assessee is allowed.
26. Coming to ground No. 14 of the appeal of the assessee, which challenges that the inter company receivable arising from the provisions of research and information services constitute a separate international transactions under provisions of section 92B of the income tax act. As discussed earlier, this issue is squarely covered against the assessee in its own case for assessment year 11 – 12 in ITA No. 154/del/2016 as under:-

“C. INTEREST ON RECEIVABLES

56. The next issue raised by the Id. AR is against the transfer pricing adjustment on account of interest on receivables. Briefly stated the facts of the case are that on examination of the assessee's balance sheet, it was noticed by the TPO that payments against the invoices raised by the assessee were not received within the stipulated time as provided in the Agreement. On being called upon to explain that why the delayed payments be not treated as unsecured loans advanced to the AEs, the assessee submitted that it was not an international transaction warranting benchmarking. The TPO rejected this contention and held that interest was chargeable at arm's length level in respect of delayed receipt of invoice values. The DRP affirmed the view of the TPO, against which the assessee has come up in appeal before us.

57. The Id. AR submitted at the outset that the Delhi bench of the tribunal in Ameriprise India Pvt. Ltd. vs. ACIT in ITA No.2010/Del/2014 (authored by the AM of this order) has held such interest on receivables as an international transaction. He submitted that in certain other orders, a contrary view has been taken. It was, therefore, contended that a reasonable view be taken. In the opposition, the Id. DR supported the impugned order.

58. We have heard the rival submissions and perused the relevant material on record. It is seen that similar issue cropped up in the case of Ameriprise (supra) and also Techbooks International Pvt. Ltd. vs. DCIT in ITA No.240/Del/2015. In the former case, the bench, after taking note of the view taken in Techbooks (supra) noted that the Finance Act, 2012 has inserted Explanation to section 92B with retrospective effect from 1.4.2002. Clause (i) of this Explanation, which is otherwise also for removal of doubts, gives meaning to the expression 'international transaction' in an inclusive manner. Sub-clause (c) of clause (i) of

this Explanation, which is relevant for our purpose, provides as under:-
Explanation.--For the removal of doubts, it is hereby clarified that-- (i) the expression "international transaction" shall include-- (a) (b) (c) capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;....

59. On going through the relevant part of the Explanation inserted with retrospective effect from 1.4.2002, thereby also covering the assessment year under consideration, the Bench found that apart from any long-term or short-term lending or borrowing, etc., or any type of advance payments or deferred payments, 'any other debt arising during the course of business' has also been expressly recognized as an international transaction. That being so, the payment/non-payment of interest or receipt/non-receipt of interest on the loans accepted or allowed in the circumstances as mentioned in this clause of the Explanation, also becomes international transactions, requiring the determination of their ALP. If the payment of interest is excessive or there is no or low receipt of interest, then such interest expense/income need to be brought to its ALP. The expression 'debt arising during the course of business' in common parlance encompasses, inter alia, any trading debt arising from the sale of goods or services rendered in the course of carrying on the business. Once any debt arising during the course of business has been ordained by the legislature as an international transaction, it is, but, natural that if there is any delay in the realization of such debt arising during the course of business, it is liable to be visited with the TP adjustment on account of interest income short

charged or uncharged. Thus, the contention taken by the assessee before the TPO that interest on receivables is not an international transaction, was found by the Bench to be bereft of any force.

60. We find that the Hon'ble Bombay High Court in the case of CIT vs. Patni Computer Systems Ltd., (2013) 215 Taxmann 108 (Bom.) dealt, inter alia, with the following question of law:-

19 "(c) Whether on the facts and circumstances of the case and in law, the Tribunal did not err in holding that the loss suffered by the assessee by allowing excess period of credit to the associated enterprises without charging an interest during such credit period would not amount to international transaction whereas section 92B(1) of the Income-tax Act, 1961 refers to any other transaction having a bearing on the profits, income, losses or assets of such enterprises?"

61. While answering the above question, the Hon'ble High Court noticed that an amendment to section 92B has been carried out by the Finance Act, 2012 with retrospective effect from 1.4.2002. Setting aside the view taken by the Tribunal, the Hon'ble High Court restored this issue to the file of the Tribunal for fresh decision in the light of the legislative amendment.

62. The foregoing discussion divulges that non-charging or under-charging of interest on the excess period of credit allowed to the AE for the realization of invoices amounts to an international transaction and the ALP of such an international transaction is required to be determined.

63. The Delhi Bench in Ameriprise (supra) and Techbooks (supra) did not approve the reasoning about such interest subsuming in working capital

adjustment. It found that the working capital adjustment is in respect of international transaction of rendering services to the AE. Interest for the credit period allowed as per the Agreement is factored in the price charged for the rendering of services. In the oppugnation, the non-realization of invoice value beyond the stipulated period is a separate international transaction, whose ALP is required to be determined. Granting of working capital adjustment has been held to be confined to the international transaction of rendering of services, whose ALP is separately determinable. On the other hand, the international transaction of interest receivable from its AEs for late realization of invoices beyond such stipulated period is a separate international transaction. Allowing working capital adjustment in the international transaction of rendering services has been held to have no impact on the determination of ALP of the international transaction of interest on receivables from AEs beyond the stipulated period allowed as per the Agreement. In our considered opinion, whereas, the international transaction of purchase/sale of goods from/to AE contemplates comparison of the price charged/paid for such goods by impliedly including the interest for the period allowed for realization of invoices as per the terms of the agreement, the international transaction of charging interest on late recovery of trade receivable covers the period which starts with the termination of the period of credit allowed under the agreement, which is subject matter of the international transaction of purchase/sale of goods. There is one more fallacy in the argument about the subsuming of interest income in the working capital adjustment. It is simple that working capital adjustment is ordinarily computed by considering the average of the opening and closing values of inventories, receivables and

payables. A transfer pricing adjustment on account of interest on delayed realization of invoice value has nothing to do with the closing or opening values. It depends on the period of realization on transaction-to-transaction basis. To put it differently, suppose an invoice is raised on 1st May; period allowed for realization is two months; and the invoice is actually realized on 31st December. Notwithstanding the fact that interest on such late realization would become chargeable for a period of 6 months (from 1st July to 31st December), but the amount of invoice will not be receivable as at the end of the financial year on 31st March. As such, this receivable would not have an impact on the working capital adjustment in any manner, but would call for addition on account of the late realization of invoice value for a period of six months. Following the orders in Ameriprise (supra) and Techbooks (supra), we uphold the view taken by the TPO on this issue. Interest on late realization of invoices is directed to be charged in line with the directions given in the above orders of the Delhi Bench of the tribunal.”

Ld. departmental representative could not controvert the above decision. Hence, respectfully following the decision of coordinate bench, we decide ground No. 14 of the appeal of the assessee against assessee holding that intercompany receivables arising from provision of services do constitute a separate international transaction under section 92B of the act. In the result ground No. 14 of the appeal of the assessee is dismissed.

27. Ground No. 15 of the appeal of the assessee is against initiation of the penalty proceedings under section 271 (1) (C) of the act. We are of the opinion that this ground is premature at this stage. Hence, we dismiss it.

28. Ground No. 16 of the appeal of the assessee is against levy of interest under section 234D of the income tax. No specific arguments were advanced before us and therefore we dismiss ground No. 16 of the appeal of the assessee.
29. In the result appeal of the assessee is partly allowed.
30. Order pronounced in the open court on 11/05/2017.

-Sd/-

(BHAVNESH SAINI)
JUDICIAL MEMBER

-Sd/-

(PRASHANT MAHARISHI)
ACCOUNTANT MEMBER

Dated: 11 /05/2017
A K Keot

Copy forwarded to

1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR
ITAT, New Delhi