

**IN THE INCOME TAX APPELLATE TRIBUNAL  
Hyderabad ' B ' Bench, Hyderabad**

**Before Smt. P.Madhavi Devi, Judicial Member  
& Shri S.Rifaur Rahman, Accountant Member**

ITA No.310/Hyd/2015  
(Assessment Year: 2010-11)

M/s. Excellence Data Research Pvt. Ltd Hyderabad PAN: AABCE 4933 C (Appellant)	Vs.	Asstt. Commissioner of Income Tax, Circle 17(1) Hyderabad (Respondent)
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ITA No.292/Hyd/2015  
(A.Y 2010-11)

Asstt. Commissioner of Income Tax, Circle 17(1) Hyderabad (Appellant)	Vs.	M/s. Excellence Data Research Pvt. Ltd Hyderabad PAN: AABCE 4933 C (Respondent)
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For Assessee : Shri K.R. Vasudevan  
For Revenue : Smt. Nivedita Biswas, DR

Date of Hearing : 13/07/2016  
Date of Pronouncement : 12/09/2016

**ORDER**

**Per Smt. P. Madhavi Devi, J.M.**

**ITA No.310/Hyd/2015:**

This is assessee's appeal for the A.Y 2010-11 against the assessment order passed by the AO u/s 143(3) r.w.s. 92CA(4) r.w.s. 144C(1) of the I.T. Act.

2. Brief facts of the case are that the assessee company which is providing back office data creations, content development services with its AE, filed its return of income for the aym2010-11 on 13.10.2010 declaring Nil income after claiming deduction u/s 10A of the Act, amounting to Rs.5,24,16,660/-. Observing that the assessee company, has entered into international transactions for an amount of Rs.40.01 crores during the relevant period, the AO made reference to the TPO for determination of the ALP u/s 92CA(4) of the Act. The TPO vide his order dated 31.10.2013 proposed an adjustment on account of provisions of ITES for Rs.7,69,69,407 and interest receivable of Rs.88,17,946 totalling to a sum of Rs.8,57,87,353 u/s 92CA(3) of the I.T. Act and also held that as per the proviso to subsection (4) of section 92C, no deduction is allowable u/s 10A on the enhanced Arms Length Price adjustment. Aggrieved, the assessee preferred its objection before the DRP and the DRP vide its order dated 8.12.2015, determined the average margin of the comparables for excluding three comparables i.e. Infosys BPO Ltd, TCS E-Serve Ltd and M/s. E-clerx Services Ltd. The DRP also directed the AO to exclude Accentia Technologies Ltd from the list of comparables, if on verification it is found that the extraordinary event of amalgamation during the year is found to have

impact on the profits of the Company. After excluding the above 3 companies from the list of 11 comparables, the average margin of the 8 comparables came to 20.69%. After verification of extraordinary event and its impact, profit in the case of Accentia Technologies Ltd, that the TPO could not find any effect of amalgamation on the margins of the comparables. He, therefore, held that Accentia Technologies Ltd not to be excluded from the set of comparables. He, therefore, after determining the Arms Length adjustment at Rs.5,03,47,511. Thereafter the procedure to consider the working capital expenditure relating to PLR @ 12.25% found that the working capital adjustment has come to -2%. After such adjustment, the Arms Length margin came to 22.69%. Further, as regards interests outstanding receivable on Rs.88,17,946, the DRP had directed to adopt interest @ LIBOR + two percentage on the inter company receivables as against 12% adopted by the TPO. AO observed that during the year, the LIBOR rate for 1 year was 1.34% and he accordingly worked out the interest at 3.34 and recomputed the interests @ 3.4% on the outstanding at Rs.24,54,328 and treated the adjustment u/s 92CA of the I.T. Actg. As regards the assessee's claim of deduction of Rs.54,24,16,660 u/s 10A of the Act, the AO observed that the assessee has not computed the deduction as

provided for in sub-section (4) of section 10A and also has not adopted the correct turnover as provided in clause (iv) to Explanation-2 of sub section. He therefore, added the T.P. adjustment be the income of the assessee and further reduced a sum of Rs.40,44,693 being internet expenses/telephone charges for the purpose fo computation of income u/s 10A of the Act. Aggrieved, the assessee is in appeal before us.

3. The assessee has raised as many as 20 grounds of appeal and has also filed an application for admission of additional grounds of appeal which is numbered as Ground Nos.6.1 and 6.2. At the time of hearing the learned Counself or the assessee submitted that Ground Nos. 1 to 3 are general in nature, hence no need for adjudication. He also submitted that Ground Nos. 7, 9, 10 & 13 are not pressed. These grounds are accordingly rejected as not pressed.

4. As regards Ground No.4 against the order of the AO/DRP in considering foreign exchange loss amounting to Rs.1,12,94,338 incurred by the assessee as operative in nature while computing the net margin of the assessee under the TNNM method, the learned Counsel for the assessee failrly admitted that this issue is covered against the assessee by the orders of this Tribunal. We find that the DRP at Page No.10 and Para 17

has followed the decision of the Coordinate Benches of this Tribunal in rejecting the assessee's objections. For the sake of ready reference the relevant paragraph is reproduced hereunder:

*“17.0 Ground of objection No.13 – Foreign Exchange income/expenses should be considered as non-operating for computation of margins-The assessee submitted that foreign exchange gain/loss should be considered as non-operating for computation of margin of the assessee and the comparables. In this regard, the assessee contended the stand taken by the learned TPO and places reliance on the decision of Mumbai Tribunal in case of DHL Express (India) Pvt. Ltd (ITA No.7360/Mum/2010) wherein it was held that foreign exchange fluctuations do not form part of the operational income because these items have nothing to do with the main operations of the assessee.*

*Decision: The TPO has clearly stated in the TP order that the foreign exchange loss forms part of the operating margins for the reason that as per the requirements of AS-11 issued by ICAI, foreign exchange gain/loss of any nature relating to any item whatsoever is required to be charged off to the P&L a/c. This position has been consistent with the extant practice. He also stated that the Hon'ble jurisdictional ITAT in the cases of Foursoft Ltd and Capital IQ Information Systems Pvt. Ltd have held that foreign exchange fluctuation is part of the operating margin, more so when such fluctuations have been considered as part of operating margins in the cases of comparables. He also noted that even various other Tribunals (Mumbai and Bangalore) have held that foreign exchange fluctuation is operating in nature. In view of the overwhelming judicial decisions, the TPO's action is confirmed and the objection is rejected”.*

In view of the above and also in view of the decision in the case of Hyundai Motors wherein following the decision relied upon by the DRP, we have dismissed the assessee's grounds therein. Respectfully following the Coordinate Bench decision cited (Supra) in the order of the DRP, this ground of appeal of the assessee is rejected.

5. As regards Ground No.5, it is against the order of the AO/DRP in considering the operating margin of the assessee at an overall entity level instead of considering the segmental results of the AE, while computing the net margins of the assessee under the TNNM method, the learned Counsel for the assessee submitted that this issue is covered in favour of the assessee by the decision of the Coordinate Bench of this Tribunal in the case of M/s. Astrix Laboratories Ltd vs. ACIT in ITA No.2181/Hyd/11 & 312/Hyd/12, dated 29.01.2016 for the A.Y 2007-08 respectively. The learned DR however, supported the orders of the authorities below. We find that the assessee has raised objection before the DRP that the margin has to be paid at segmental level and adjustment should be made only to AEs. The DRP has only confirmed the order of the TPO holding that the TPO has countered the objections of the assessee. In the case of M/s Astrics Lab Ltd, this Tribunal at para 26 of its order has

directed the AO/TPO to take into account the turnover of the transaction with the AE only for the purpose of determining the ALP. For the sake of ready reference, Para 26 is reproduced hereunder:

*“26. As regards the assessee’s ground No.3 and 4, we find that the assessee has also transactions with non-AEs and the TPO has taken the total turnover including transactions with non-AE companies, for the purpose of determination of ALP. It has been held in a catena of cases that it is only the transactions or the turnover involved in the transactions with AEs alone, which have to be considered for computation of ALP. The AO/ TPO are accordingly directed to take into account the turnover of the transactions with AE only for the purpose of computing the ALP. Accordingly, grounds No.3 and 4 are treated as allowed for statistical purposes”.*

Respectfully following the decision of the Coordinate Bench to which both of us are signatory, we direct the AO/TPO of the assessee herein also to take into account the turnover of the transactions with AE only for the purpose of computing the ALP. Ground No.5 is treated as allowed for statistical purposes.

6. As regards Ground No.6, the assessee is challenging the inclusion of the following companies in the final list of comparables:

- a) Accentia Technologies Ltd

- b) Cosmic Global Ltd
- c) TCS e-Serve International Limited &
- d) Crossdomain Solutions Pvt. Ltd.

In addition to the above, assessee vide additional grounds of appeal (6.1 and 6.2) is also challenging the comparability of Cosmic Global Ltd and Crossdomain Solutions Pvt. Ltd as comparables with the assessee. It is stated in the application for admission of additional grounds that the assessee had selected these companies as the comparables to the assessee as one of the relevant material was not available in the public domain at the time of preparation of TPO order, but since it has come to the notice of the assessee that the Hon'ble Tribunal in various decisions have held that these companies are functionally different from I.T. Technology Enabled Service Providers and also comparables to the assessee in I.T., assessee is raising the objection before us.

7. After hearing the learned DR, we admit the additional grounds of appeal. Brief facts relating to this issue are that during the transfer pricing study, the assessee has returned the operative cost at 9.91% and the result of the AE transaction at 11%. He has drawn our attention to the page 11 of the TPO's order wherein the table of the final comparables selected by the TPO is given. He submitted that the assessee has raised its



objection against the Accentia Technologies Ltd and Crossdomain Solutions Pvt. Ltd. As regards Accentia comparable is concerned that the said company has functional difference from the assessee as the said company develops for the business products outsourcing. The learned Counsel for the assessee also relied upon the annual report of Accentia to substantiate his argument that the services provided by Accentia including software and hardware products. He also drawn our attention to the extracts of the annual reports which show that the Accentia owns intellectual property and there were extra ordinary events during the year such as strategic and amalgamation during the financial year 2009-10. He submitted that in the assessee's case for A.Y 2009-10, assessee has rejected the said company on the ground that the Accentia has made abnormal profits due to extra ordinary event. He also placed reliance upon the decision of the ITAT in the case of Hyundai Motor India Engineering in ITA No.1743/Hyd/2015, wherein after discussing the issue at length, has directed the AO to exclude this company as a comparable. The learned DR, on the other hand, supported the orders of the authorities below and submitted that the decision of the ITAT in Hyundai Motor Engineering Ltd which is engaged in the business of automobiles with the assessee herein is in

ITES services. Therefore, according to him the said decision cannot be applied herein. Further, he submitted that the TPO has considered all the relevant facts before holding that the said company is comparable to the assessee.

8. Having regard to the rival contentions and the material on record, we find that the DRP has directed the AO to consider whether the extra ordinary event of amalgamation during the year is found to have an impact on the profits of the company. We find that instead of carrying out the exercise, the AO has simply followed the order of the TPO in holding that the fact of amalgamation on the margin of the said company has no effect on the margin of the said company. This, in our opinion, is not a correct approach of the AO. Where a direction has been given by the DRP to follow a certain procedures, the AO has simply followed the TPO order. Therefore, order of the AO on this issue needs to be set aside. In the case of Hyundai Motors which is also engaged in rendering of ITES to its AEs, the Tribunal has taken note of the same at para 9.1 and 9.3 of its order. Therefore, the decision of the Tribunal in the said case is applicable to the case on hand, more particularly since the comparables adopted by the TPO in the said case are the same

in the assessee's case also. In the case of Hyundai Motors at Page 20, para 18, the Tribunal has held as under:

*“18. As regards M/s. Accentia Technologies Ltd., is concerned, we find that the DRP has directed to exclude this company by placing reliance upon the order of the ITAT in the assessee's own case for the A.Y. 2009-10 by holding that this company operates in a different business strategy of acquiring companies for inorganic growth as its strategy and considering the profit margins of the company and insufficient segmental data, held that this company cannot be selected as a comparable. It was also held by the DRP that on the very same reason of acquisition of various companies, being an extraordinary event, it had an impact on the profit of the company and the said company was directed to be excluded.*

*18.1. For the relevant A.Y. 2010-11, the Ld. Counsel for the assessee has drawn our attention to the information available on Accentia Technologies Ltd., to demonstrate that the said company is into diversified knowledge process outsourcing activities. It is seen there from that the said company is involved in Healthcare documentation as well as receivables, management services including installation and maintenance of all software, hardware and band width infrastructure required for the same, deployment of man power and service delivery in all these areas. It is also seen that it is engaged in legal process outsourcing. From Schedule-IV showing the fixed assets of the assessee, it is also seen that the said company owns goodwill/brand/IPRs (Intellectual Property Rights). From the notes to the accounts, it is also seen that a subsidiary of the company Asscent Infoserve Pvt. Ltd., has been amalgamated with the company consequent to which, assets and liabilities of the erstwhile company were transferred and vested in the company w.e.f. 1st April, 2008 and the scheme has been given effect to in the accounts of the year. Therefore, it is clear that there is an extraordinary event in the case of Accentia Technologies Ltd., during*

*the relevant financial year particularly since the approval for amalgamation has been given by the Hon'ble High Court of Mumbai vide orders dated 21<sup>st</sup> August, 2009 and by the Hon'ble Karnataka High Court vide orders dated 6th February, 2010. This event would definitely have an effect on the profit margins of the said company and therefore, has to be excluded from the list of comparables as rightly done by the DRP. Therefore, we do not see any reason to interfere with the order of the DRP on this company also. Accordingly, ground No.3 of the Revenue is dismissed”.*

Since the order of the Tribunal in the case of Hyundai Motors for the same A.Y, we direct the AO/TPO to exclude this company from the final list of comparables.

9. As regards the comparability of Cosmic Global it is the case of the assessee that this company is primarily engaged in the activities pertain to transactions, medical transcription and consultancy services and is significantly different from ITES activities performed by the assessee. He has drawn our attention to the Annual Report of Cosmic Global Ltd wherein the major revenue from medical transcription and consultancy services and translation charges as against a meager Rs.26,97,430 from the accounts. According to the assessee, the Cosmic Global Ltd earns only 4.66% of total sales from ITES activities and in the assessee's own case for the A.Y 2009-10, this company was rejected by the ITAT due to insignificant revenue from ITES

segment. Without prejudice to the above argument, the learned Counsel for the assessee also submitted that the Cosmic Global Ltd cannot be compared to the assessee as no segmental split of financial information is available for the financial year 2010. In support of the above contention the learned Counsel for the assessee also placed reliance upon the decision of the ITAT in the case of Hyundai Motor India Engineering cited supra. The learned DR supported the orders of the authorities below.

10. Having regard to the rival contentions and the material on record, we find that in the case of Hyundai Motor India Engineering for the A.Y 2010-11, this Tribunal has considered similar circumstances to exclude the said company from the list of comparable of the assessee therein. At Para 10.3 and 10.4 of its order, the Tribunal has held as under:

*“10.3. Having regard to the rival contentions and the material on record, we find that the assessee had raised objections against this company in the earlier A.Y. 200910 on a similar ground i.e., the income from translation services which is outsourced is much higher and therefore, should not be considered as a comparable. The Tribunal, by relying on the decision of the Tribunal at Delhi in the case of Mercer Consulting (India) P. Ltd., ITA.No.966/Del/2014 dated 06.07.2014 has held as under:*

*“(4) Cosmic Global Ltd.*

14. The main objection of assessee with reference to the inclusion of this company is with reference to outsourcing of its main activity. Even though this company was selected as comparable in assessee's TP study, it has raised objection before the TPO that this company's employee cost is less than 21.30% and most of the cost is with reference to the outsourcing charges or translation charges, and as such this is not a comparable company. The TPO, though considered these submissions, rejected the same, on the reason that this does not impact the profit margin of the company. Opposing the view taken by the TPO, it is submitted that this company cannot be selected as comparable, as similar issue was discussed by the coordinate Bench of the Tribunal(Delhi) in the case of Mercer Consulting (India) P. Ltd. (supra), vide paras 13.2 to 13.3 which read as under-

"13.2. Now coming to the factual matrix of this case, we find from the material on record that outsourcing charges of this case constitute 57.31 % of the total operating costs. This does not appear to us to be a valid reason for eliminating this case from the list of comparables. On going through the Annual accounts of Cosmic Global Limited, a copy of which has been placed on record, we find that its total revenue from operations are at RS.7.37 crore divided into three segments, namely, Medical transcription and consultancy services at Rs. 9. 90 lacs, Translation charges at Rs.6.99 crore and Accounts BPO at Rs.27.76 lac. The Id.AR has made out a case that outsourcing activity carried out by this company constitutes 57% of total expenses. The reason for which we are not agreeable with the Id. AR is that we have to examine the revenue of this case only from Accounts BPO segment and not on the entity level, being also from Medical transcription and Translation charges. When we are examining the results of this company from the Accounts BPO segment alone, there is no need to examine the position under other segments. The entire outsourcing is confined to Translation charges

*paid at Rs.3.00 crore, which is strictly in the realm of the Translation segment, revenues from which are to the tune of Rs.6.99 crore. If this segment of Translation is not under consideration for deciding as to whether this case is comparable or not, we cannot take recourse to the figures which are relevant for segments other than accounts BPO. Thus it is held that this case cannot be excluded on the strength of outsourcing activity, which is alien to the relevant segment.*

*13.3. However, we find this case to be incomparable on the alternative argument advanced by the Id. AR to the effect that total revenue of the Accounts SPO segment of Cosmic Global Limited is very low at Rs.27.76 lacs. We have discussed this aspect above in the context of CG-VAK's case and held that a captive unit cannot be compared with a giant case and thus excluded CG-VAK with turnover from Accounts SPO segment at Rs.86.10 lacs. As the segmental revenue of SPO segment of Cosmic Global Limited at Rs. 27.76 lac is still on much lower side, the reasons given above would fully apply to hold Cosmic Global Limited as incomparable. This case is, therefore, directed to be excluded from the list of comparables”.*

*In view of the detailed analysis of the coordinate Bench of the Tribunal in the above referred case, in this case also we accept the contentions of assessee and direct the Assessing Officer/TPO to exclude this comparable for the same reasons.*

*10.4. We find that in the A.Y. 2010-2011 also as observed by us above, the facts are similar and the segmental revenue is on the lower side. Further, though the assessee had accepted this company as comparable before the TPO, it had raised detailed objection before the DRP and the DRP ought to have considered the objections of the assessee as the assessee is entitled to raise the objection before the appellate authority for factual differences to be*

*considered. Further, since the Tribunal in assessee's own case for the earlier year held this company to be not comparable to the assessee.*

*Respectfully following the decision of the Coordinate Bench in the assessee's own case for A.Y 2009-10, we direct the AO/TPO to exclude this comparable from the final list for the same reason”*

As the facts and circumstances before us are also similar and are for the same A.Y 2010-11, we respectfully following the decision of the Coordinate Bench direct the AO/TPO to exclude this company from the prime list of companies.

11. TCS e-Serve International Ltd: As regards the comparability of this company with the assessee, the learned Counsel for the assessee submitted that the TCS international also provides software testing, verification and validation which are different from ITES services providers by the assessee. It is also submitted that the segmental information of TCS International are not available in the annual report. The exceptional circumstances of the company reported in annual report such as acquisition of India based captive business outsourcing arm, resulting in acquisition of an aggregate amount of \$ 2.5 billion over a period of 9.5 years and its impact on the financial implications of the company also brought to our notice. It is submitted that these peculiar circumstances have been considered by the Coordinate



Bench of this Tribunal in the case of Hyundai Motor India Engineering for exclusion of the list of comparables. We find that in the case of Hyundai Motors at Para 11 of its order read as under:

*“11. We find that the assessee had raised its objections in detail against the adoption of these two companies as comparables both before the TPO as well as DRP, but its objections were rejected. Before us also, the Ld. Counsel for the assessee reiterated these objections and relied upon the T.P. order in the case of M/s. IGS Imaging Services (India) P. Ltd., for A.Y. 2010-2011, where TPO has excluded both of these companies by holding that they are engaged in BPO activity and that they have reported exceptional circumstances in their annual report for the relevant financial year.*

*11.1. The Ld. D.R. on the other hand, supported the orders of the authorities below.*

*11.2. Having regard to the rival contentions and the material on record, we find that during the relevant financial year, the TCS e-Serve International Ltd., had acquired the Citi group India based Captive business processing outsourcing (BPO) arm for an all-cash consideration and in return, had acquired the business of an aggregate amount of \$ 2.5 billion over a period of 9.5 years. This definitely is an exceptional circumstance which has been taken note of by the TPO in the case of M/s. IGS Imaging Services (India) P. Ltd., to exclude the same from the list of comparable. This exceptional circumstance was not taken note of by the TPO and the DRP failed to appreciate the objection of the assessee in proper perspective. Any circumstance which would influence or result in abnormal result in the financials of a company have to be adjusted or where no adjustment can be done to make it comparable to the tested party, such a company has to be excluded from the list of*

*comparables. This Tribunal in a number of decisions held that exceptional circumstance is a reasonable filter to exclude a company from the list of comparables. Therefore, we direct the A.O./TPO to exclude this company from the final list of comparables.*

*11.2.1. As regards TCS e-Serve Limited is concerned, we find that it possesses brand value as is evident from the Schedule-N (Operation and Other expenses) to the P & L A/c of the annual report for the financial year 2009-10 of Rs.46,065 thousands and also that it possesses intangibles in the form of software licenses which have not been taken note of by the authorities below while adopting its margin. It is also the case of the assessee that this company has a turnover of Rs.1405.10 crores which is 25 times of the turnover of the assessee and hence, is not comparable to the assessee. The Ld. Counsel for the assessee had also placed reliance upon the TPO's order in the case of M/s. IGS Imaging Services India Ltd., to hold that there are exceptional circumstances during the relevant financial year due to which this company is not comparable to the assessee. The Ld. Counsel for the assessee also submitted that the segmental details of this company are not available and hence, has to be excluded on this count also.*

*11.2.2. We find that the assessee's contentions about the presence of 'brand value' and owning of 'intangibles' is supported by the evidence on record. However, as regards the extraordinary event or exceptional circumstance there is no material placed before us by the Ld. Counsel for the assessee. Therefore, merely because the TPO in another case has held that there is an extraordinary event for which this company has to be excluded from the list of comparables, it cannot be excluded. Such claim has to be supported by evidence on record. As regards the functional dissimilarity and huge turnover and brand value is concerned, we find that this Tribunal in assessee's own case for A.Y. 2009-10 while*

*considering the comparability of the assessee with Infosys BPO Ltd., has taken note of the possession of the brand value and intangibles which influenced the financial results of this company. The Hon'ble Delhi High Court in the case of CIT vs. Agnity India Technologies P. Ltd., (2013) 219 Taxman 26 (Del.), held that huge turnover companies like Infosys and Wipro cannot be considered as comparable to smaller companies like assessee therein. In the case before the Hon'ble High Court (supra), the turnover of the assessee was about Rs.15.79 crores as against the turnover of Rs. 1016 crores of the Infosys. Considering these facts, the Hon'ble High Court had directed for exclusion of Infosys BPO because of its brand value and also on the grounds of functional dissimilarity and huge turnover. Though, the company before us is TCS e-Service Ltd., and not Infosys BPO, we find that the turnover of the assessee company for this assessment year is around Rs.50 crores as against the turnover of TCS e-Serve Limited of Rs.1405.10 crores. Therefore, following the turnover filter as well as taking note of the fact that it owns and possesses brand value and intangibles as compared to the assessee which does not own such assets, we direct that this company be excluded from the list of final comparables. Accordingly, assessee's grounds of appeal No.6 is partly allowed”.*

Respectfully following the decision of the Bench, these two comparables TCS e-Serve International Ltd and TCS e-Serve Ltd directed to be excluded.

12. As regards Crossdomain Solutions Ltd, the learned Counsel for the assessee fairly admitted that in the case of Hyundai Motors, comparability of this company has been upheld by the Tribunal. Therefore, he has no objection to the said company being included in the final list of comparables. We find that at

Para 8 of the orders in the case of Hyundai Motors, the Tribunal has held as under:

*“8. At the time of hearing, the learned Counsel for the assessee submitted that the company Crossdomain Solutinos P. Ltd., has been considered as a comparable to the assessee in assessee's own case for the earlier assessment year and the ITAT has upheld the contention of the Revenue that the said company is comparable. He therefore, fairly admitted that this issue is covered against the assessee in assessee's own case. In view of the said submission of the assessee, we see no reason to interfere with the order of the A.G. in considering Crossdomain Solutions P. Ltd., as a comparable to the assessee. As regards the other three comparables challenged by the assessee and the T.P. adjustment proposed by the TPO, the brief facts are as under :*

*9.1. The assessee M/s. Hyundai Motor India Engineering P. Ltd., is engaged in providing/rendering R & D support service in respect of CAD and CAE, in designing automobile parts and in modeling and iterative simulation. It receives the basic design from its group company. It entered the following international transactions with its AEs.*

AE	Nature of transaction	Amount (in Rs.)
Hyundai Corporation      Autoever	Purchase of computers	2,02,32,916
Hyundai Corporation      Autoever	Purchase of computer software	32,78,246
Hyundai Motor Company	Provision of ITES	29,70,07,503
KIA Motor Corporation	Provision of ITES	16,13,19,523
Hyundai Corporation      Autoever	Reimbursement of expenses paid	7,72,927

		48,25,10,845
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*As per the audited statement of accounts, the financials of the tax-payer/assessee are as under:*

Nature of transaction	Nature of International transaction	MAM	PLI	Margin of tax payer	Margin of comparables
Provision of ITES	458,326,756	TNMM	OP/OC	11.47	9.97
Purchase of computers	20,232,916	TNMM	OP/OC	11.47	9.97
Purchase of computer software	3,178,246	TNMM	OP/OC	11.47	9.97
Reimbursement of expenses paid	772,927	NA	NA	NA	NA

*9.2. On going through the T.P. document of the assessee, the TPO was of the opinion that the search process of the assessee suffers from defects which has resulted in selection of inappropriate comparables and rejection of comparables that are appropriate comparables. He, therefore, rejected the T.P. document of the assessee and proceeded to make independent analysis by aggregating all the transactions under TNMM.*

*9.3. The TPO conducted the FAR analysis and as regards the ITES services carried out by the assessee, he adopted the TNMM as the most appropriate method for determining the arms length price. Thereafter, he conducted fresh search on the databases 'Prowess' and 'Capitaline' and selected the following 11 companies as final comparables and arrived at the average margin of the comparables at 28.39%.*

S.No	Nature of the company	OR	OP/OC
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1	Accentia Technologies Ltd	93,12,44,808	49.02
2	Acropetal Technologies Ltd (Seg.)	46,39,36,810	10.12
3	Axis-I.T. & T Ltd	20,29,67,892	11.89
4	Cosmic Glkopal Ltd	5,86,37,419	16.59
5	Eclerx Services Ltd	2,57,02,10,000	42.17
6	Infosys BPO Ltd	11,30,05,01,306	31.63
7	TCS e-Serve International Ltd	1,49,29,56,000	51.51
8	TCS e-Serve Ltd	14,05,10,05,000	67.58
9	Jeevan Softech Ltd (Seg.)	1,74,43,000	8.04
10	Microgenetics Systems Ltd	2,40,42,539	6.60
11	Crossdomain Solutions Pvt Ltd	37,69,57,428	17.13
		Total	312.28
		Average	28.39

9.4. The assessee raised its objections to the adoption of the above comparables. However, TPO did-not accept the assessee's contentions and after giving the risk and working capital adjustment, he adjusted the arms length price at 26.81 % and short fall of Rs.10,38,23,246 is treated as adjustment under section 92CA of the LT. Act, 1961. On the basis of the T.P. order, the A.O. proposed the draft assessment order. Aggrieved by the same, assessee raised its objections before the DRP which was partly allowed. In consonance with the directions of the DRP, the final assessment order dated 17.10.2014 was passed against which, both the Assessee as well as the Revenue are in appeal before us. Let us now deal with the objections of the

*assessee on each of the three companies challenged by the assessee as not comparable before us”.*

13. Since the assessee is not agitating the comparability of this company before us, we reject the assessee’s ground of appeal against this company. In the result, assessee’s ground of appeal No.6, 6.1 and 6.2 are treated as partly allowed.

14. As regards Ground No.8, assessee is seeking inclusion of 11 companies in its ground of appeal, but at the time of hearing the learned Counsel for the assessee submitted that the assessee is serious about inclusion of item (1) and (2) i.e. Ace BPO Services Ltd and R Systems International Ltd. Further, he has also submitted that if Ground No.6 is allowed, then the ground become academic as held by the Tribunal in the case of Hyundai Motor India Engineering.

15. Having regard to the rival contentions and the decision of the Coordinate Bench in the case of Hyundai Motor India Engg. there is no reason to adjudicate the ground at this stage. Accordingly Ground 89(i) and 8(ii) are rejected.

16. As regards Ground No.11, the learned Counsel for the assessee submitted that the negative working capital adjustment should not be made as the assessee is fully funded by the AE

and does not bear any working capital, more particularly as it is being compensated with a cost + basis. The learned Counsel placed reliance upon the decision of the Coordinate Bench of this Tribunal in the case of Adaptec India P Ltd in ITA No.206/Hyd/2014 wherein it was held that the negative working capital should not be made in the case of capital services provided. Without prejudice to the above, it is further submitted that the TPO had taken incorrect amount as its account receivable/payable and arrive at negative capital working of minus(2) whereas correct working capital working is 0.12% only.

17. Ground No.12 is dismissed as infructuous.

18. As regards Ground Nos. 14 to 17, we find that the assessee has not charged interest on outstanding receivables from its AEs as well as non AEs. The TPO considered the receivables as well as international transactions and made an adjustment of Rs.24,54,328 on account of amount realized with delay during the year and on account of outstanding as on 31.03.2010. It is the case of the assessee that the receivables have become international transactions only by virtue of the amendment made vide Finance Act 2012 and hence making an adjustment for the year 2010-11 is not warranted. Further he also stated that the



average database and the cost of the comparable companies is 94 as against the 83 days in the case of the assessee. Therefore, this adjustment is not warranted in the case of the assessee. Without prejudice to the above arguments, the learned Counsel for the assessee submitted that the TPO has charged interest for the period beyond 31.03.2010 and further that the litigation of interest has been charged on the entire outstanding receivables as on 31.03.2010 without considering the actual delay. In support of his contention that the receivable cannot be equated with capital funds as provided for in the Explanation by the amendment by the Finance Act of 2012, he placed reliance upon the decision of the Coordinate Bench of this Tribunal in the case of Pegasystems Worldwide India Private Limited in ITA Nos.1758 and 1936/Hyd/2014. As regards the contention that interests can be charged only by the year end i.e. 31.3.2010, he placed reliance upon the decision of the Tribunal at Mumbai in the case of Tecnimont ICB Private Ltd in ITA No.487/Mum/2014. The learned DR however, supported the orders of the authorities below and relied upon the order of the DRP, it held that the TPO is given valid reasons to counter the objections of the assessee.

19. Having regard to the rival contentions, we find that in the case of Pegasystems Worldwide (Supra) wherein the Tribunal at para 17 held as under:

*“17. Ground No. 7 pertains to interest on outstanding receivables and 8 on incorrect computation of interest. Assessee raised the issue on separate adjustment made for receivables. TPO noticed that Assessee has receivables of Rs. 21,07,53,864/- at the end of the year. Assessee was asked to submit the details of raising the invoice and subsequent receipts. TPO proposed to charge interest at 12% on the outstanding receivables. While replying that assessee is a fully funded entity of the AE and the amounts outstanding are on services but not loan or advances given. It also does not have any working capital risk and there is no interest payment also. It relied on the order of the ITAT in the case M/s. Evonik Degussa India Private Limited in ITA No. 7653/Mum/2011, wherein it was held that TP adjustment cannot be done on hypothetical issues. Assessee also further relied on the decision of Logix Micro Systems Ltd v. ACIT [42 SOT 525] (Bang) wherein ITAT held that a reasonable period should be provided as interest free period and no interest should be calculated for such period. However, while calculating the interest of 12%, TPO neither considered the above decisions nor gave any interest free period. Not only that even though Assessee realized the amounts in later year, i.e., after 31-03-2010, interest was charged for whole of the period. As can be seen from the table in page 45 of the TP order, TPO charged interest for the supposed delay not only during the year but also for the period beyond the assessment year concerned. Thus, he made a proposal to make adjustment of Rs. 1,26,40,592/- as an adjustment u/s. 92CA and total income was enhanced accordingly. Before the DRP, Assessee objected to the same and submitted that:*

- The outstanding receivables relate to the provision of services and not in the nature of any advance/loans. These are closely linked to the provision of services and hence have to be aggregated for the purpose of economic analysis.*
- The company has been fully funded by its AE since its inception for all its working capital requirements and receivables are running accounts. Any fund requirement being made good by the AEs.*

*17.1. It is also submitted that company does not bear working capital risk. It relied on the same objections as relied before TPO. DRP however, vide its para 17, rejected Assessee's contentions but accepted alternate plea of charging interest at LIBOR Plus 2½ points*

on the inter-company receivables from the overseas AE. Assessee is aggrieved.

17.2. Ld. Counsel submitted that the issue of charging of interest beyond the period was not adjudicated and DRP reduced the rate of interest from 12% LIBOR plus 2.5 points. It was submitted that Assessee was a debt free company, AE takes care of funding, no interest was charged and there is no liability of interest and therefore, notional interest income cannot be brought to tax. Assessee relied on the principles laid down by Co-ordinate Bench at Mumbai in the case of Lintas India Pvt. Ltd., in ITA No. 2024/Mum/2007 dt. 09-11-2012 and also Mastek Ltd., Vs. ACIT in ITA No. 3120/Ahd/2010 then referring to the provisions of the Act the explanation brought by amendment in 2012 Finance Act. It was submitted that even though retrospective, it does not cover Assessee's transaction as the word 'capital financing' used there particularly refers to loans or advances given for capital financing, whereas in Assessee's case, these are outstanding services rendered but not capital financing. The words are to be interpreted invoking the principles ejusdem generis and so the outstanding receivables cannot be equated to capital financing as amended by the provisions of the Act. It was further submitted that working capital adjustments are being made while analyzing the operational performance of the companies, therefore, outstanding amount gets adjusted in working capital adjustments and another separate addition is not required under the TP provisions. Thus, it was contended that the outstanding amounts are not to be considered for adjustment.

17.3. We have considered the issue and examined the rival contentions. In the case of Evonik Degussa India P. Ltd., in ITA No. 7653/Mum/2011, it was already held the TP adjustment cannot be made on hypothetical and notional basis, until and unless there is some material on record that there has been under charging of real income. Thus on the facts and circumstances of the case, we are of the opinion that addition on account of notional interest relating to alleged delayed payment in collection of receivables from the AEs is uncalled for on the facts of the present case. Even though DRP tried to distinguish the above decision on facts, as seen from the facts in both the cases, we are of the opinion that the above decision will equally apply to Assessee's case. Assessee has outstanding service charges receivables and as seen from the order of TPO, the outstanding is only from 31-07-2009. There seems to be no such delay in earlier months. Assessee has no interest liability at all so notional interest cannot be brought to tax under the provisions of TP. As rightly pointed out by the Ld. Counsel, the outstanding receivables on account of services cannot be equated with capital financing as provided for in the Explanation by the amendment by Finance Act, 2012 retrospectively. Even otherwise, as rightly held by the Logix

*Micro Systems Ltd v. ACIT [42 SOT 525] (supra), TPO should have allowed some interest free period for receiving the outstanding service charges. While acknowledging the order of the ITAT, TPO did not even bother to exclude the reasonable period and levied interest not only from the date of invoice to the date of realization during the year but also for the period beyond 31-03-2010 in later year. We were informed that no such addition was made in the later year on Assessee's receivables. We are of the opinion that both on the facts of the case and principles of law, there is no need for bringing to tax the notional interest on the outstanding receivables. Accordingly, we allow the grounds 7 & 8 of Assessee and direct AO/TPO to delete the said addition made”.*

Since in the case before us, the facts and circumstances are similar and more particularly the TPO has not taken into consideration that the fact that the assessee has also not charged the interest not receivable from the non AE, we comply the assessee's plea on this ground. Accordingly Ground No. 14 to 17 are allowed.

20. As regards Ground No.8, we direct the AO/TPO to rework the profit margin of the assessee in accordance with the proviso to section 92C and this ground is accordingly treated as allowed for statistical purposes.

21. Ground No.19 being the computation of interests, we direct the AO/TPO to give consequential relief to the assessee, if any.

22. In the result, assessee's appeal is partly allowed.

**ITA No292/Hyd/2015 (Revenue's Appeal)**

23. As regards Revenue's appeal, the Revenue is aggrieved by the directions of the DRP to delete M/s. E-Clerk Services Ltd from the final list of comparables and also in directing the AO to reduce the telecommunication charges and other expenditure, both from the export turnover as well as from the total turnover for computation of deduction u/s 10A of the Act. As regards the exclusion of M/s. E-Clerx Services Ltd, we find that the DRP has followed ITAT order wherein it was held that the said company has been regarded as KPO and not comparables to the ITES. The learned DR relied upon the order of the TPO, while the learned Counsel submitted that M/s. E-Clerx Services Ltd is functionally similar with the assessee and no segmental information is available. It is submitted that E-Clerx is an India Process Outsources Company engaged in providing data analytical and data management and process improvement solution, wherein it would collate raw data and analyze such data with the purpose of drawing conclusion about that information. He submitted that the Special Bench of the Tribunal in the case of Global (P) Ltd has held that the business activities and functions performed by the E-Clerx for the financial year 2007-08 are not comparable to low end service providers. According to him the business activity

and functions performed, E-Clerx has broadly not took for the financial year 2009 and therefore, for the relevant A.Y also the said company cannot be comparable entity. He has also submitted that there has been extra ordinary event during the financial year 2009-10 of abnormal growth as admitted by E-clerx, its in the annual report on account of various factors. Thus, according to him, the said company has been rightly directed to be excluded by the DRP.

24. Having regard to the rival contentions and the material on record, we find that in the assessee's own case for the assessment year 2009-10, it has been held not comparable to the assessee on activities and there is no change in the activities of E-Clerx for the relevant A.Y for the very same reason we uphold the finding of the DRP to exclude this company from the list of comparables.

25. As regards Ground Nos. 2 & 3, we find that the alternate contention of the assessee that the telecommunication charges and other expenditure should be excluded from the export turnover as well as total turnover is concerned, we find that the order of the DRP is in accordance with the decision of the Hon'ble Karnataka High Court in the case of Tata Elxis and

respectfully following the same, we see no reason to interfere with the order of the DRP.

26. In the result, Revenue's appeal is dismissed.

27. To sum up, assessee's appeal is treated as partly allowed and Revenue's appeal is dismissed.

Order pronounced in the Open Court on 12<sup>th</sup> September, 2016.

Sd/  
**(S. Rifaur Rahman)**  
**Accountant Member**

Sd/-  
**(P. Madhavi Devi)**  
**Judicial Member**

Hyderabad, dated 12<sup>th</sup> September, 2016.

Vnodan/sps

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3. *DRP, Hyderabad*
4. *DCIT (T.P)-II Hyderabad 500004*
5. *The DR, ITAT, Hyderabad*
6. *Guard File*

By Order