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**[2020] 118 taxmann.com 112 (Mumbai - Trib.) [23-07-2020]**

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**TRANSFER PRICING:** Where assessee was engaged in providing back office support services, while comparable company was a Knowledge Process Outsourcing (KPO) service provider, it was not comparable to assessee

**TRANSFER PRICING:** Where in assessee's business model, assessee rendered services by employing own employees using own infrastructure as against comparable company's business model where services were outsourced, it was not comparable to assessee

**TRANSFER PRICING:** Where some of companies had suffered loss in current assessment year, but average of two years showed robust positive figure, these companies could not be said to be persistently loss making company and to be accepted as comparables



**[2020] 118 taxmann.com 112 (Mumbai - Trib.)**

**IN THE ITAT MUMBAI BENCH 'J'**

**Morgan Stanley Advantage Services (P.) Ltd.**

**v.**

**Deputy Commissioner of Income-tax, range 9(2)\***

**SHAMIM YAHYA, ACCOUNTANT MEMBER**

**AND PAWAN SINGH, JUDICIAL MEMBER**

**IT APPEAL NO. 6523 (MUM.) OF 2014**

**[ASSESSMENT YEAR 2008-09]**

**JULY 23, 2020**

**I. Section 92C of the Income-tax Act, 1961 - Transfer pricing - Computation of arm's length price (Comparables, functional similarity - Business support services) - Assessment year 2008-09 - Whether where assessee was engaged in providing back office support services, while comparable company was a Knowledge Process Outsourcing (KPO) Service provider, it was not comparable to assessee - Held, yes [Para 13] [In favour of assessee]**

**II. Section 92C of the Income-tax Act, 1961 - Transfer pricing - Computation of**

arm's length price (Comparables, factors to determine - Employee lost filter) - Assessment year 2008-09 - Whether where comparable company had a business model where services were outsourced as against business model of assessee where services were rendered by employing own employees and using one's own infrastructure, it could safely be concluded that said comparable was functionally different and as such liable to be excluded from final list of comparables - Held, yes [Para 13] [In favour of assessee]

III. Section 92C of the Income-tax Act, 1961 - Transfer pricing - Computation of arm's length price (Comparability factors - Loss making company) - Assessment year 2008-09 - Whether where some of companies had suffered loss in current assessment year, but average of two years showed robust positive figure, these companies could not be said to be persistently loss making company - Held, yes - Whether since these comparables had been duly accepted as comparable in earlier assessment year by Transfer Pricing Officer himself, taking a contrary stand by Transfer Pricing Officer without giving a specific reasoning was not sustainable - Held, yes [Para 16] [In favour of assessee]

## **CASE REFERRED TO**

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*Maersk Global Centers (India) (P.) Ltd. v. ACIT* [2014] 147 ITO 83/43 taxmann.com 100 (Mum.) (SB) (para 4), *Rampgreen Solutions (P.) Ltd. v. CIT* [2015] 377 ITR 533/60 taxmann.com 355/234 Taxman 573 (Delhi) (para 8), *CIT v. PTC Software (I) (P.) Ltd.* [2017] 395 ITR 176/(2016) 75 taxmann.com 31 (Bom.) (para 8) and *Dy. CIT v. JSW Steel Ltd.* [IT Appeal No. 6264 (Mum.) of 2018 dated 14-5-2020) (para 18).

**Sunil Moti Lala** for the Appellant. **A. Mohan** for the Respondent.

## **ORDER**

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**Shamim Yahya, Accountant Member** - This appeal by the assessee is directed against the order of the learned Commissioner of Income Tax (Appeals) ('Id. CIT(A) for short) dated 29-8-2014 and pertains to the assessment year (A.Y.) 2008-09.

2. Although the assessee has raised various grounds, the issue relates to transfer pricing adjustment of Rs. 1,44,87,25,823/- done by the authorities.

3. The assessee is a subsidiary of Morgan Stanley Incorporated USA and is a captive service provider, providing back office support services to its associated enterprises globally. During the year under consideration, it had provided aforesaid support services to its associated enterprises and received a fee of Rs. 1,44,87,25,823/-. This the assessee benchmarked under the transactional net margin method. It selected 18 companies as comparable and computed the margin on the basis of 2 years average margin. As per the assessee's computation the margin of comparables came to 23.93%. This was less than the assessee's margin from international transactions, i.e., 26.81%. Hence, the assessee claimed the value of transaction, i.e., the international transaction to be at arm's length price. The transfer pricing officer disregarded the

computation of margins based on 2 years data. Consequent upon this, the assessee submitted single year data of 7 comparables with the mean of 16.91%. The Transfer Pricing Officer characterized the assessee as Knowledge Process Outsourcing (KPO) services and rejected the assessee's transfer pricing study. He accepted/included Vishal Information Technologies Ltd. as comparable and rejected the remaining 6 of assessee's comparables. The Transfer Pricing Officer carried out his own search and included 5 additional comparables. The margin as per the Transfer Pricing Officer came to 51.73%. Accordingly, the transfer pricing officer made the transfer pricing adjustment.

4. Upon the assessee appeals, the Id. CIT(A) held that the Transfer Pricing Officer was not correct in treating the assessee as KPO, still he has upheld the benchmarking process undertaken by the transfer pricing officer. In this regard, the Id. CIT(A) referred to the decision of Special Bench of the ITAT in the case of *Maersk Global Centers (India) (P.) Ltd. v. ACIT* [2014] 147 ITD 83/43 taxmann.com 100 (Mum.). The Id. CIT(A) upheld the selection of four of the comparables by the Transfer Pricing Officer and he rejected the other two, accepting the assessee's submission that they were functionally different. Accordingly, this lead to computation of arithmetic mean of 44.60 %. The detailed chart of computation under consideration is as under:

Sr. No.	Name of the comparable	As per assessee		As per TPO	As per CIT(A)
		Margin (Avg of two years)	Margin (for the relevant year)		
		(a)	(b)	(c)	(d)
1.	Eclerx Services Ltd.	-	-	65.88%	65.88%
2.	Vishal Information Technologies Ltd. (Common comparable)	49.57%	51.72@	50.68%	50.68%
3.	Crossdomain Solutions	-	-	26.96%	26.96%
4.	Datamatics Financial Services	-	-	34.87%	34.87%
5.	Allsec Technologies	27.91%	-14.13%	-	-
6.	R Systems International Ltd.	13.91%	10.34%	-	-
7.	CG Vak Software & Exports Ltd.	4.38%	-11.98%	-	-
8.	Cosmic Global Ltd.	14.02%	23.30%	-	-
9.	Spanco Telesystems and Solutions Ltd.	21.97%	5.86%	-	-
10.	Tricom India Ltd.	57.80%	53.25%	-	-
11.	Acropetal Technologies (Seg.)	-	-	35.30%	-
12.	Mold-Tek Technologies	-	-	96.66%	
13.	Ace Software Exports Limited	0.44%	-	-	-

14.	Apex Advanced Technology (P.) Ltd.	29.88%			
15.	Caliber Point Business Solutions Ltd.	23.28%			
16.	Flextronics Software Systems Ltd.	7.69%			
17.	Maple Esolutions Ltd.	32.71%			
18.	Triton Corp. Ltd.	27.54%			
	Arithmetical mean	23.93%	16.91%	51.73%	44.60%

5. Against the above order, the assessee has filed appeal before us.

6. The assessee is aggrieved with regard to rejection of some of its comparables and inclusion of some of the comparables by the revenue. The submission of the learned counsel of the assessee in this regard is as under.

7. The learned counsel of the assessee submitted that assessee has been duly accepted by the revenue earlier and also by the tribunal as dealing in back office support services.

The margin of the assessee for assessment years 2005-06 and 2006-07 was accepted by the revenue and for A.Y. 2007-08 it was duly upheld by the ITAT. The learned counsel of the assessee pleaded that following need to be excluded, being K.P.O's:

- ◆ Eclerx Services Ltd.
- ◆ Vishal Information Technologies Ltd.
- ◆ Crossdomain Solutions
- ◆ Datamatics Financial Services.

The learned counsel of the assessee further submitted that following are to be included, as they have been wrongly excluded by the TPO:

- ◆ Allsec Technologies
- ◆ R Systems International Ltd.
- ◆ CG Vak Software & Exports Ltd.

8. As regards the rejection and comparables, it is the contention of the learned counsel of the assessee that assessee is engaged in back office support functions which has been accepted in the earlier assessment years. The entities dealing with the knowledge and processing outsourcing are not comparable to the assessee and hence need to be excluded. The learned counsel of the assessee submits that the Id. CIT(A) has rejected the Transfer Pricing Officer's characterization of the assessee as KPO. Hence, KPO selected by the Transfer Pricing Officer cannot be considered as comparables. The learned counsel further submits that the Hon'ble Delhi High Court in the case of *Rampgreen Solutions (P.) Ltd. v. CIT* [2015] 60 taxmann.com 355/234 Taxman 573/[2015] 377

ITR 533 (Delhi) has categorically expressed reservation on the observation of the Special Bench relied upon by the learned CIT(A). Further, he has submitted that the decision of Hon'ble Delhi High Court in *Rampgreen Solutions (P.) Ltd. (supra)* has been followed by the Hon'ble Bombay High Court in the case of *CIT v. PTC Software (I) (P.) Ltd.* [2017] 395 ITR 176/[2016] 75 taxmann.com 31 (Bom.) and the of case of the assessee by ITAT in the earlier years. It is further the submission of the learned counsel of the assessee that the Eclerx Services Ltd. has extraordinary event of acquisition transaction and hence should be excluded. As regards the Datamatics Financial Services, the learned counsel of the assessee submits that it fails export filter of 75%, and accordingly should be excluded.

**9.** For the inclusion of assessee's comparables, the learned counsel of the assessee submits that these comparables have been accepted as a comparable in earlier assessment years. The learned counsel of the assessee submitted that the assessee seeks that the transfer pricing officer be directed to exclude KPO comparables and include assessee's comparables, as the rejection is not based upon cogent reasoning.

**10.** We have carefully considered the submissions and perused the records. The assessee in the present case is a subsidiary of Morgan Stanley International Holdings Incorporated USA. The assessee provides back office support functions to its associated enterprises. The transactions of IT Enabled Support Services to its associated enterprises and the arms length price computed by the assessee was accepted by the revenue in A.Y. 2005-06 and A.Y. 2006-07. The same was also upheld by the ITAT for assessment year 2007-08. For the current assessment year, the Transfer Pricing Officer characterized the assessee's functions as knowledge process outsourcing KPO. Thereafter, the Transfer Pricing officer made general comments on the selection systems adopted by the assessee. He proceeded to reject the same. He did not specify as to which of the comparables is being rejected for which specific reasons thereof. Thereafter, the transfer pricing officer mentioned his own criteria and proceeded to select comparables and accordingly made the transfer pricing adjustment.

**11.** Upon the assessee's appeal, the Id. CIT(A) has accepted that the characterization by the transfer pricing officer of the assessee's functions as knowledge process outsourcing was not correct. Thereafter, the Id. CIT(A) contradicted himself by stating that the functions of the assessee are in alignment with the knowledge process outsourcing comparable dealt with by the transfer pricing officer. In this regard, the learned CIT appeals relied upon the ITAT decision in the case of *Maersk Global Centers (India) (P.) Ltd.* Thereafter, the learned CIT(A) upheld the assessing officer's action of selection of four of the comparables and accepted the assessee's contention in rejection of the two comparables.

**12.** Now in appeal before us, the submission of the learned counsel of the assessee is that assessee's functions are that of ITES which has been duly accepted by the revenue as well as by the ITAT in earlier years. Hence, the re-characterisation of the assessee's functions as knowledge process outsourcing is not sustainable. We are in full agreement with this contention. Furthermore, we find that the Id. CIT(A) has clearly contradicted himself by stating both that assessee is not a KPO and at the same time accepting the comparables selected by the Transfer Pricing Officer from the database for knowledge process outsourcing companies.

13. As regards the rejection of four companies, it is the submission of learned counsel of the assessee that the functions of Eclerx Services Ltd. and Vishal Information Technologies Ltd. (earlier Coral Hub Ltd.) has been held to be not comparable to the assessee by the ITAT for the assessment year 2007-08. In this regard, we find that ITAT in the aforesaid order has observed as under:

32. As noted earlier the Id. AR for the assessee submitted that the assessee submits that Eclerx Services Ltd. has not considered as a comparable in earlier years. Eclerx Services Ltd. is a Knowledge Process Outsourcing (KPO) Service provider which is not comparable to assessee; assessee is engaged in providing back office support services. In support of his submission, the Id. AR of the assessee relied upon the decision of Delhi High Court in *Rampgreen Solution (P.) Ltd. v. CIT* (2015) 377 ITR 533 (Delhi). The TPO included this comparable by taking his view that this company is in date process and analytical services. The Id. CIT(A) confirmed the action of the TPO by taking his view that this comparable company is into the health care receivable management and therefore renders ITeS services. The Hon'ble Delhi Court in *Rampgreen Solution (P.) Ltd. (supra)* held entities rendering voice call center services for customer support and a KPO service provider employ IT-based delivery systems, but characteristics of services, functional aspects, business environment, risks and quality of human resource employed are materially different; and therefore, benchmarking international transactions on basis of comparison of PLI of high-end KPO service providers with PLI of Voice Call Centers, would be unreliable. Further, Mumbai Tribunal in *Wills Processing Services (India) Ltd. v. ACIT (supra)* on considering similar contentions excluded this comparable.

38. The Id. AR submitted as we recorded earlier that Coral Hubs Ltd. was outsourcing its significant part of its operation as evident from its low employee cost and have substantial different business model compared to assessee and prayed for exclusion. The Id. DR has supported the inclusion. The TPO while making benchmarking taking his view that this comparable company is in the business of IT enabled services to overseas markets and included in the list of comparable. The Id. CIT(A) confirmed the action of TPO holding that the TPO conducting benchmarking after calling information under section 133(6) and is benchmarking analysis are correct. We have noted that, though the Id. AR has relied upon a number of decisions of Tribunal/co-ordinate bench. We have noted that in a recent decision of Tribunal in *Wills Processing Services (I) (P.) Ltd. (supra)* on comparability, the Tribunal held as under:

We though in light of our aforesaid observations had partly disagreed with certain grounds as had been averred by the Ld. AR to facilitate exclusion of the aforesaid comparable, however as observed by us hereinabove that the aforesaid comparable viz. Coral Hub Limited (earlier known as Vishal Information Technology Limited) had a business model where services are outsourced, as against the business model of the assessee where services are rendered by employing own employees and using one's own infrastructure, on the basis of which we are of the considered view that it can safely be concluded that the said comparable was functionally different, and as such was liable to be excluded from the final list of comparables. That our aforesaid view stands fortified by the aforesaid order passed by the

Tribunal while disposing of the appeal of the assessee's own appeal for A.Y. 2005-06, as well as the judgment of the Hon'ble High Court of Delhi in the case of *Rampgreen Solutions (P.) Ltd. (supra)*. Thus as there has been no material shift in the facts involved in the case of the assessee for the year under consideration, as observed by us hereinabove, we are thus of the considered view that as the business model of the aforesaid comparable, viz. *Coral Hub Ltd. (supra)* is substantially different from that of the assessee, therefore the same cannot be accepted as a comparable and hence is directed to be excluded from the list of comparables."

**14.** Accordingly, following the aforesaid decision of the tribunal, we hold that the Eclerx Services Ltd. and Vishal Information Technologies Ltd. (earlier Coral Hub Ltd.) are liable to be rejected as invalid comparable.

As regards the other comparables namely Crossdomain Solutions and Datamatics Financial Services, we find that the Transfer Pricing officer and the Id. CIT(A) have found their functions to be similar to that of KPO and that of Eclerx and Vishal technologies. Since, the ITAT has duly upheld the rejection of the aforesaid companies, i.e., these two companies are also liable to be rejected. Furthermore, Datamatics Financial Services also fails the export filter of 75% which has been adopted by the transfer pricing officer. Hence, in the background of aforesaid, we hold that following comparable are to be rejected:

- ◆ Eclerx Services Ltd.
- ◆ Vishal Information Technologies Ltd.
- ◆ Crossdomain Solutions
- ◆ Datamatics Financial Services.

**15.** Now we deal with the following comparables which were selected by the assessee, but have been rejected by the Transfer Pricing officer:

- ◆ Allsec Technologies
- ◆ R Systems International Ltd.
- ◆ CG Vak Software & Exports Ltd.

**16.** The Transfer Pricing Officer has not mentioned the specific reasoning in rejecting the above comparable. While discussing his general reasoning for election/rejection, the transfer pricing officer mentioned that he is only accepting comparables where the current year data are available. In this regard, we note that though initially the assessee had submitted two-year data, subsequently, it has duly submitted the current year data. The transfer pricing officer has also mentioned that he is rejecting the persistent loss making companies. Though some of these companies have suffered loss in the current assessment year the average of two years showed the robust positive figure. Hence, it cannot be said that these are persistently loss making company. Furthermore, we note that these comparables have been duly accepted as comparable in earlier assessment year by the officer himself. Hence, taking a contrary stand by the transfer pricing officer without giving a specific reasoning is not sustainable. Accordingly, we direct for inclusion

of these comparables.

**17.** Accordingly, the transfer pricing officer shall make the computation afresh in light of above directions as above.

**18.** Before parting, we note that this appeal was heard in 3-2-2020. The pronouncement is delayed due to lockdown in view of Covid-19 pandemic. The pronouncement is as per rule 34(5) of the Appellate Tribunal Rules and the Hon'ble Bombay High Court decision *vide* order dated 15-4-2020 and 15-6-2020 extending the time bound periods specified by the Hon'ble High Court by removing the period under lockdown. This aspect is also dealt with in detail in ITAT, Mumbai order in the case or *Dy. CIT v. JSW Steel Ltd. vide* [IT Appeal No. 6264 (Mum.) of 2018, dated 14-5-2020].

**19.** In the result, the appeal stands allowed for statistical purposes.

SB

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\* In favour of assessee.