

## Employment of more engineers won't show Co. as technical service provider for transfer pricing purpose

**Summary – The Delhi ITAT in a recent case of Dassault Systems India (P.) Ltd., (the Assessee) held that where TPO made addition to assessee's ALP taking it as a technical service provider, mere fact that out of total staff of 69 employees there were 37 engineers, was not enough to conclude that assessee rendered technical services**

### Facts

- The assessee company was engaged *inter alia* in the business of sales, services and support of software products etc.
- During relevant year, assessee entered into various international transactions which were categorized as business support services.
- The assessee benchmarked its international transactions adopting TNMM. It used 6 comparables having arithmetic mean of net cost profit of 4.72 per cent.
- Since assessee had shown its net cost profit at 18.84 per cent during relevant year, international transactions were claimed to be entered into at ALP.
- In transfer pricing proceedings, TPO re characterised activity of assessee with its AE as technical support services.
- Thereupon, TPO on basis of average profit earned by its own set of comparables, made certain addition to assessee's ALP.
- The DRP set aside objections raised by the assessee.
- The assessee filed instant appeal contending that FAR analysis had not been correctly understood by the revenue and revenue had taken into consideration irrelevant facts to arrive at a conclusion that assessee was acting as technical service provider.

### Held

- In the light of the facts and on considering the arguments of the parties before the Bench, it is held that the plea of the assessee that it is conducting its affairs in India based simpliciter on the letter of the C.F.O namely 'H' as the only document available cannot be accepted. No doubt the transfer pricing issues may still be called to be in the nascent stage as far as the tax collectors and the tax payers are considered however withholding material informations can only compound the problem. It is beyond the realms of credulity even to imagine, let alone to hold that a conglomerate of this stature can function without having any written agreements setting out the respective duties and responsibilities of the assessee *vis-à-vis* the holding companies at geo-platforms for whom services are stated to be performed as a result of direct sales by the AEs or indirect sales through value added resellers (VARs).

- The documentary framework on the basis of which rendering of services which would trigger the generation of bills must be available as it cannot be presumed to have left this vital area to the undefined whimsical fancies of the parties. In the facts of the present case it is evident that complete facts have not been placed on record by the tax payer. Accordingly, the conclusion arrived at on the basis of limited information provided may have resulted in incorrect characterization of the assessee.
- In view thereof it is appropriate to restore the issue back to the TPO as the revenue also has not called for the relevant evidences like the memorandum of association and article of association. It is hoped that the opportunity so provided is utilized by the assessee in its own interests by placing the evidences in support of its claims before the tax authorities as in the absence of relevant information the revenue cannot be faulted with for arriving at a conclusion at variance with the assessee's claims.
- It is also necessary to observe that the conclusion of the revenue in regard to the employment of 37 engineers out of a total staff of 69 by assessee cannot also *per se* lead to the conclusion that technical services were necessarily being provided. Similarly, the remuneration paid to them for the services rendered by itself also cannot be said to be a reflection on their nature of services being performed. Both the parties before the Bench have submitted that employment of engineers is a necessity for the assessee as the product of the AE is a highly complex sophisticated software which can be used in manufacturing and designs etc in the field of Aerospace, Architecture and Construction, Automotive, Consumer Goods, Consumer Packaged Goods, Hightech, Industrial Equipment, Life Sciences, Power Process and Petroleum, Shipbuilding and Services where as the assessee has contended. However, the conclusion on this common stand of necessity of having engineers in its employment differs. Whereas the tax payer states that the product being marketed must be understood by the business service provider the revenue claims that technical services are being provided.
- In order to address the above controversy it is opined that documentation addressing the functions performed by the tax payer as the necessary evidences need to be considered. The claims and counter claims of the need to have expert technical staff/engineers considering the nature of product marketed by the tax payer does to an extent support the tax payers claim as the person providing business support services necessarily needs to first understand the product being marketed and also be capable of explaining/demonstrating its capabilities/utility and working to the potential customer.
- The knowledge on the part of the service provider to judge whether technical service is necessitated or not in a situation to deal with the consumer's complaint of a product mal-functional can necessarily be judged only by a competent person who may then need to send forth a report that technical support to address the glitch or malfunction is required. However one is also alive to the claims of the revenue that site visits to address the glitches/malfunction etc. would come in the realm of technical service which necessarily can be performed by engineers only. Thus the functions

taken on by the tax payer need to be addressed. It is seen that the tax payer has been required by the TPO to address the duties assigned to the personnel and it is seen that the same has not been addressed.

- Further, the assessee's memorandum of association be also taken into consideration as the said document not only addresses the name and place of the registered office but also enshrines the Objects of its Incorporation. It is the basic document which brings the company into existence as it contains the Objects of the incorporation of the company. Similarly the articles of association also need to be considered as these would contain the rules/bye-laws and regulations for internal management of a company, and would throw light on how the day to day business of the assessee is to be conducted. The relationship between the holding companies, between the company and its members including their relationship *inter-se* *vis-à-vis* the tax payer needs to be addressed. These basic documents have not been taken into consideration and the production of the same is directed before the TPO.
- Addressing the invoice placed on record claimed to be explaining the manner in which billing is done it is opined that the evidence relied upon is incomplete. Nothing has been placed on record by the tax payer *qua* the sample invoices filed so as to explain how they create both the liability to pay and the entitlement to receive payment as supporting documents assigning duties, responsibilities standards against which these are to be judged have not been placed before the authorities. An invoice without supporting documents justifying the narration and the manner how amounts have been set out therein would be a document having no evidentiary value.
- It is only a relevant evidence if the person relying on the same can explain the contents of its narration when questioned so as to address the narrations set out therein fixing liability to pay and the entitlement to receive the payment on the part of the other person. The same needs to be addressed by a documentary framework governing the *inter-se* roles and responsibilities of the parties. The same is found missing. In the course of the hearing as already attempted to dwell on the probable possible documents which may address the issue in the face of general assertion on the part of the parties before the Bench.
- Giving consideration to the arguments in the light of the responses to the question in the hearing attempted to address that the probable document at the first instance which may trigger and set into motion the rendering of the services by the tax payer *vis-à-vis* direct and also indirect sales is probably the requisition of services to be performed, which may refer to a pre-existing rules and practices and may be always or sometimes modified as per the peculiar needs of the purchaser of the product. This would necessitate the existence of some document which sets out the duties and responsibilities of the concerned parties wherein the standards and procedures to be adhered to would have been set out on the basis of which performance of services claimed to have been performed are judged resulting in the generation of the internal bill which is honoured by the other party.

- One is alive to the claims and counter claims of the parties that there may be an element of technical services in the business support services as site visits to address glitches and malfunctioning of the product may also have been provided as claimed by the revenue. However to arrive at any possible conclusive finding conclusions *dehorse* material facts on record is not appropriate. The tax payer needs to explain how billing has been done whether it is by way of man hours for site visits if so what function was performed during the site visits it is only then it can be decided whether a technical function was being performed or was it a routine business support services to get feed back etc. after the sales.
- Thus, the function responsibilities and the duties undertaken by the employees is an important area for consideration. Considering which it may turn out that part of the services performed are technical support services and part of the services performed are business support service as the claim that computer asset ratio of the company is less for a technical service provided may not be a relevant factor for deciding the issue as in the absence of any material whatsoever of the nature of services rendered the possibility of the engineers visiting the premises of the customers and performing technical support services on their computers cannot be ruled out.
- In view of the above, it is appropriate to restore the issue back to the file of the TPO with the direction that the assessee shall place a copy of the articles and memorandum of association before the TPO and address the primary object for which the assessee was incorporated. The assessee shall also categorically take a stand whether there is any other agreement linked to address its stated claim of providing sales and support services sales made through AEs or VARs. The taxpayer shall ensure that it is made available to the TPO. All the relevant evidences including the specific document on the basis of which the services have been called upon for rendering and the basis on which the invoices have been raised needs to be made available to the revenue. The evidence placed on record in the absence of any explanation as to how the figures have been arrived at in the invoice cannot be said to be sufficient and cogent evidence.
- Needless to say that the TPO after a FAR analysis characterizing the assessee shall carry out the exercise of search for comparables in order to decide whether the transaction is at arms length or not.
- In view of the above conclusion, appeal of the assessee is allowed for statistical purposes.