

## ITAT rejects comparables as they were inappropriate due to diverse activities, brand value and economy of scales

**Summary –** The Hyderabad ITAT in a recent case of CYIENT Ltd., (the Assessee) held that where TPO made addition to assessee's ALP in respect of rendering software development services to its AE, since two comparables selected by TPO were inappropriate due to various factors such as brand value, economy of scales, goodwill, diversified activities, owning of intangibles etc., impugned addition was to be set aside

### Facts

- The assessee-company was a global technology services and solutions company specialized in geospatial, engineering design and IT solutions.
- It had various subsidiaries located in USA and Europe to provide software development services to its client.
- In transfer pricing study, the assessee selected itself as the tested party and adopted Transaction Net Margin Method (TNMM) as most appropriate method with operating profit to operating cost as the profit level indicator (PLI). Assessee selected 16 comparable companies from the databases with weighted average margin of 12 per cent. As margin of assessee was shown at 15.45 per cent, the price charged by assessee was claimed to be within the arm's length.
- The TPO, though, accepted TNMM as the most appropriate method, for benchmarking the transactions pertaining to sales of services and payment towards consultancy services, but, he nevertheless found the approach adopted by assessee in selecting comparables unacceptable.
- The TPO embarked upon a selection process himself by applying certain additional filters and the search process yielded 19 comparable companies with arithmetic mean of 26.09 per cent.
- The TPO thus made certain addition to assessee's ALP.
- As far as the payment towards consultancy services (intra group services) was concerned. TPO opined that assessee could not substantiate whether there was any need for consultancy services and if required whether such services were actually rendered.
- The TPO thus proceeded to determine ALP of the payment made towards consultancy services at Rs. Nil. However, since adjustment on account of the said transaction had already got merged in the adjustment proposed by him under section 92CA, no separate adjustment was made by him.
- The DRP granted partial relief to assessee.
- On appeal:

### Held

- As regards payment of consultancy charges to foreign subsidiaries in USA, it is evident from record that in the preceding assessment years, *i.e.*, assessment years 2006-07 and 2007-08 though the

international transactions of assessee were examined by TPO, but similar payments made to foreign subsidiaries were accepted by him without making any adjustment.

- Further, from the finding of the co-ordinate bench, it is clearly evident that the payments made by assessee to its foreign subsidiaries were towards software development services rendered by them on the portion of work sub-contracted by assessee to them. Thus, if the so called consultancy charges paid in the impugned assessment year are of identical nature, then, it cannot be treated as consultancy charges simpliciter. Further, it is relevant to note that though similar payments were made even in the subsequent assessment year 2009-10 but TPO had not determined the ALP of such payments at *NIL*.
- In view of the aforesaid factual position, since the issue raised by assessee goes to the root of the matter which was not raised before DRP in the interest of fair play and justice, the issue is remitted back to the file of TPO to decide afresh after examining the agreements between assessee and its subsidiaries and other evidences brought on record by assessee.
- As far as addition made to ALP was concerned, assessee has objected to selection of Infosys Technologies Ltd. and Wipro Ltd. on ground that turnover of these companies are huge and these companies are in a different league.
- As can be seen from records, the difference in turnover between assessee in comparison to Infosys Technologies Ltd. and Wipro Ltd. is more or less in the same range as the difference between the turnover of assessee and companies having very low turnover selected by TPO. Thus, on the basis of turnover alone, these two companies cannot be treated as uncomparable considering the fact that assessee has no problem with selection of companies with very low turnover.
- However, it is worth mentioning, Infosys Technologies Ltd. and Wipro Ltd are uncomparable to assessee for various other factors such as brand name, economy of scales, goodwill, diversified activities, owning of intangibles. It is accepted fact that these two companies are leading software companies and have carved out a separate place for themselves. They are in their own league and cannot be compared to any other software development company.
- The Delhi High Court in case of *CIT v. Agnity India Technologies (P.) Ltd.* [\[2013\] 219 Taxman 26/36 taxmann.com 289](#) has also observed that big companies like Infosys cannot be considered as comparable to other software development companies. Different Benches of Tribunal have also expressed similar view while examining the comparability of Infosys Technologies Ltd. and Wipro Ltd. In view of the aforesaid, TPO is directed to exclude these two companies from the list of comparables. Accordingly, TPO is directed to compute ALP afresh in terms of observations made above.