Abnormal cost incurred by a startup is to be excluded for benchmarking it with other Cos which aren't startups

Summary – The Delhi ITAT in a recent case of HCL Technologies BPO Services Ltd., (the Assessee) held that In course of transfer pricing proceedings, while computing operating cost, abnormal costs incurred on account of start up of business like salary, rent and depreciation etc. have to be excluded

Facts

- The assessee was engaged in the business of software development and had set up a Business Process Outsourcing (BPO) unit for rendering IT enabled services during the previous year relevant to assessment year 2003-04. The relevant previous year was the first full year of operation of the BPO unit of the assessee.
- The assessee's case was that during the previous year 2002-03, the assessee was a start up enterprise and thus, due adjustment ought to be made of the start-up/one-time costs incurred, which inevitably led to losses. It was further submitted that operating profit/loss of the assessee was required to be adjusted to exclude items of abnormal cost/short fall in revenue to determine the normal profit that could have been earned by it for the purpose of benchmarking with other companies which were not in start-up stage.
- The TPO having rejected assessee's explanation, made certain adjustment to assessee's ALP on basis of mean margin earned by comparables selected by him.
- The DRP confirmed said adjustment.
- On appeal:

Held

- There is force in the argument of assessee that while calculating operating cost, the abnormal cost incurred on account of start-up should be excluded. Thus, the TPO/Assessing Officer has to be directed to adjust operating cost by excluding abnormal cost incurred on account of start-up company like salary, rent and depreciation. This matter is restored to the file of TPO/Assessing Officer to re-determine the operating cost on the above lines to arrive at operating profit.
- The appeal is allowed for statistical purposes.

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