

Co. whose directors were facing charges of fraud couldn't be accepted as comparable for TP study

Summary – The Ahmedabad ITAT in a recent case of Lubrizol Advanced Materials India (P.) Ltd., (the Assessee) held that where assessee, engaged in manufacturing cassia gum powder, rendered marketing support services to its AE, company involved in high end niche market segment of financial contents and company which outsourced its ITES to third party vendors, could not be accepted as valid comparables while determining ALP

Facts

- The assessee was engaged in manufacturing guar gum and cassia gum powder. It had provided marketing support services to its AEs in furtherance to a service agreement.
- The relevant method used was TNMM. The assessee justified its operating profits calculated at the rate of 4.53 per cent by including seven entities in the array of comparables.
- In transfer pricing proceedings, the TPO rejected some comparables selected by assessee and adopted certain new comparables. On the basis of new set of comparables, the TPO computed mean margin of 28.06 per cent.
- He thus made certain addition to the assessee's ALP.
- The DRP confirmed addition made by TPO.
- The assessee filed instant appeal raising objections to some of comparables selected by the TPO.

Held

- The assessee's first substantive argument raised in the course of hearing challenges inclusion of five entities in the array of comparables. They are C S Software Enterprise Ltd., ICRA Online Ltd., Informed Technologies India Ltd., Maple E-Solutions and Vishal Information Technologies Ltd. It submits that the first company ICRA had been selected at the assessee's behest and no objection in this regard seeking its exclusion was raised before any of the lower authorities. The assessee points out that this entity is engaged in engineering design services and computer software. The revenue's submission invoke estoppel principle. It pleads on merits that this entity's annual report clarifies that CS Software Enterprise Ltd provided information technology enabled services in a single segment. The assessee relied on law laid down in *Dy. CIT v. Quark Systems (P.) Ltd.* [\[2010\] 38 SOT 307 \(Chd.\) \(SB\)](#) holding that there is no estoppel in arguing exclusion of a comparable already included in an assessee's TP study.
- It further submits that this entity is in engineering design services and computer software. However, it fails to rebut the fact highlighted at the Revenue's behest demonstrating that this comparable company is providing information technology enabled services as per its annual report. The assessee's legal plea on estoppel principle is accepted and the same is declined on merits in view of

annual report hereinabove. A accordingly, lower authorities were justified in treating CS Software Enterprise as a valid comparable selected by the assessee itself.

- The assessee's next argument seeks exclusion of ICRA Online Ltd. The submission of assessee is that this company's revenue has been increased at the rate of 4.55 times (in thousand) from Rs. 6,414.70 to Rs. 35014.96 in assessment year 2005-06 and BPO segment results jumping from Rs. 963.29 to Rs. 10,951.43/-. The paper book indicates fluctuation in operating profits @ -13.08 per cent, -1.47 per cent, 7.66 per cent, 29.8 per cent and 6.02 per cent for assessment years 2003-04 to 2007-08; respectively.
- The assessee relies upon case law *Actis Advisors (P.) Ltd. v. Dy. CIT* [IT Appeal 5277 (Delhi) of 2011 for assessment year 2007-08 holding that disproportionate fluctuations in profits and loss would not result from a company business operations but are attributable to extraordinary reasons. The Revenue's arguments mainly highlight this entity employee's cost factor in justifying comparability thereof. It fails to rebut the assessee's contentions with regard to fluctuating profit margins in light of tribunal's decision. The assessee's plea is accepted accordingly and this entity ICRA Ltd. is excluded from the array of comparables.
- The assessee's next argument challenges comparability of Informational Technology India Pvt. Ltd. It contends that this entity is functionally different as its annual accounts in management discussion and analysis report indicate the same to be engaged in IT enabled knowledge base back office processing centre. Its case is that this entity provides services in the niche market of financial contents with its customers.
- There is merit in assessee's arguments. It is evident from annual report of this compare entity, that it is indeed involved in high end niche market segment of financial contents which cannot be equated with routine marketing support services in which the assessee was involved.
- Accordingly, it is held that this entity is not an appropriate comparable in given peculiar set of facts of the instant case. The same shall stand excluded from the array of comparables.
- The assessee's next grievance seeks exclusion of M/s. Maple E-Solutions from the array of comparables. It cites case law of *Capital IQ Information Systems India (P.) Ltd. v. Dy. CIT* [\[2013\] 57 SOT 14 \(URO\)/32 taxmann.com 21 \(Hyd. - Trib.\)](#) pertaining to assessment year 2007-08 in question holding therein that directors of this entity i.e. Rastogi Group had faced serious indictment. Therefore, the financial results demonstrating profitability could not be accepted as comparable instances. The same view stands followed in various other decisions of the Tribunal. The revenue relies upon yet another decision of the tribunal in *Vodafone India Services (P.) Ltd. v. Dy. CIT* [\[2013\] 36 taxmann.com 127/\[2014\] 146 ITD 78 \(Mum. - Trib.\)](#) accepting Maple E-Solutions as comparables in case of ITES/BPO functions. The assessee states that this decision has not examined fraud indictment of above stated directors.
- There is force in this submission. A perusal of this decision reveals that the co-ordinate bench has considered issue of merger and not that of the above stated indictment. Thus the assessee's

argument is accepted and it is held that this entity M/s. Maple E-Solutions Ltd. is not a valid comparable.

- The assessee's last objection was inclusion of Vishal Information Technologies. The assessee pleads that this entity had outsourced its ITES services to third party vendors.
- The revenue fails to counter this submission. It is thus concluded that the lower authorities have wrongly included Vishal Information Technologies as a valid comparable.
- In view of above impugned addition is set aside and the Transfer Pricing Officer is directed to re-compute the assessee's ALP accordingly.
- As regards the assessee's submission challenging action of the lower authorities denying (+/-) 5 per cent relief under section 92C(2) as standard deduction. Special Bench of the Tribunal in *IHG IT Services India (P.) Ltd. v. ITO* [[2013](#)] [144 ITD 16/33 taxmann.com 1 \(Delhi - Trib.\)](#) held that after the retrospective amendment to the second proviso to section 92C(2) by the Finance Act, 2012, there remains no ambiguity that the benefit of tolerance margin is available only when the variation between the arm's length price as determined under section 92C(1) and the price at which the international transaction has actually been undertaken does not exceed the tolerance margin. Once it exceeds the tolerance margin, no benefit under the proviso would be available to the assessee and the arm's length price as determined under section 92C(1) shall be considered.
- The assessee fails to point out any distinction on facts or law. Thus, action of the lower authorities by deciding the issue in hand against the assessee by following the Special Bench decision hereinabove is upheld. The assessee's second substantive ground is rejected.
- The assessee's appeal is thus partly allowed.