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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Judgment reserved on: 06.11.2023
Judgment pronounced on: 12.12.2023

+ **ITA 56/2022**

PR. COMMISSIONER OF INCOME TAX-1, DELHI Appellant

Through: Mr Vipul Agrawal, Sr. Standing
Counsel with Mr Gibran Naushad and
Ms Sakshi Shairwal, Jr. Standing
Counsels.

versus

FUTURE FIRST INFO. SERVICES PVT. LTD. Respondent

Through: Ms Ananya Kapoor, Adv.

CORAM:

HON'BLE MR. JUSTICE RAJIV SHAKDHER

HON'BLE MR. JUSTICE GIRISH KATHPALIA

[Physical Hearing/Hybrid Hearing (as per request)]

GIRISH KATHPALIA, J.

1. By way of this appeal brought under Section 260A of the Income Tax Act (hereinafter referred to as “the Act”), the revenue raised following proposed questions:

- A. *Whether on facts & in the circumstances of the case and law, the Hon'ble ITAT erred in law & on facts in deleting addition made by the AO on account of ALP adjustment of international transaction from associated enterprises?*
- B. *Whether the Hon'ble ITAT was justified in laying down stringent standards of comparability and attempting to identify exact replica of the taxpayer for comparability analysis, whereas the Indian Law*



and the international jurisprudence recognize the reality that there cannot be an exact comparable in a given situation without any difference without appreciating that such astringency will defeat the purpose of flexibility provided in comparability analysis for determination of ALP?

- C. *Whether Hon'ble ITAT was correct in excluding comparable none of the pre-conditions mentioned in Rule 10(B)(2) of the Income Tax Rules is satisfied by ITAT?*
- D. *The Hon'ble ITAT has erred in law and on facts in directing the TPO to exclude M/s Infosys BPO Ltd as comparable ignoring the fact that Organization of Economic Cooperation and Development (OECD) Guidelines advocate use of TNMM Method as it allows comparability of the functions rather than strictly focusing on product/service comparability?*
- E. *Whether the Hon'ble ITAT has erred in law and on facts in directing the TPO to exclude M/s Infosys BPO Ltd, Acropetal Technologies Ltd. and e-Clerx Ltd as comparable ignoring the fact the organization of economic cooperation and development (OPEC) guidelines advocate use of TNMM Method as it allows capability of the functions rather than strictly focusing on products/service comparability?*
- F. *Whether the Hon'ble ITAT has erred in law and on facts in deleting disallowance u/s 40A(ia) as assessee deducted sought tax in violation of u/s 197(1) of the Act?*
- G. *Whether the Hon'ble ITAT has erred in deleting the addition of Rs.1,03,53,150/- made by the AO u/s 40A(2) in spite of the fact that assessee, during the course of assessment proceedings, failed to justify the service being rendered by the director Shri Sunil Baijal to the company for which he was earning such a huge amount of remuneration?*

By way of order dated 21.03.2022, the predecessor coordinate bench held that in view of the judgment in the case of **S.A. Builders Ltd. vs Commissioner of Income Tax (Appeals) Chandigarh & Anr.**, (2007) 288 ITR 1, the proposed question no. G. does not arise, so notice to respondent was issued confined to proposed questions no. A to F. Upon respondent entering appearance through counsel, we heard learned counsel for both sides.



2. Briefly stated, circumstances relevant for present purposes are as follows.

2.1 The respondent/assessee being a subsidiary of GHF Holdings Ltd. Mauritius is engaged in providing information technology enabled services (ITeS) to its associated enterprise (AE) through online software, live information services and research on international database.

2.2 On 18.09.2009, the respondent/assessee filed its return of income declaring its income as Rs.8,34,16,421/-. The case having been selected for scrutiny, notice under Section 143(2) of the Act was issued.

2.3 By way of order dated 26.12.2012, the Transfer Pricing Office (TPO) under Section 92CA(3) of the Act benchmarked the transaction of the respondent/assessee using Transactional Net Margin Method (TNMM) with Profit Level Indicator (PLI) of Operating Profit to Operating Cost (OP/OC) with nine comparables with a margin of 22.72% and proposed the adjustment of Rs.3,42,98,762/-.

2.4 Accordingly draft assessment order dated 13.03.2013 was passed by the Assessing Officer incorporating the addition on account of Arms Length Price (ALP) determined by the Assessing Officer besides the additions, namely, disallowance of rent paid by the respondent/assessee without deducting TDS and payment made to person specified under Section 40A(2)(b) of the Act.



2.5 Vide Assessment Order dated 29.04.2013, in consonance with the Draft Assessment Order total income of the respondent/assessee was assessed to be Rs. 13,57,28,290/-.

2.6 The respondent/assessee challenged the Assessment Order by way of appeal before the Commissioner, Income Tax (Appeals). Vide order dated 18.11.2016, the CIT(A) partly allowed the appeal of the respondent/assessee, thereby directing the AO/TPO to re-compute the average PLI with final set of comparables, verify the disallowance related to rent expenses; and the addition pertaining to Section 40A(2)(b) of the Act was deleted by CIT(A).

2.7 Both sides preferred appeal before the Tribunal. By way of the order dated 10.05.2021 impugned in the present appeal, the Tribunal dismissed the appeal filed by the revenue and partly allowed the appeal filed by the assessee. The Tribunal deleted the additions made by the Assessing Officer on account of rent expenditure as well as disallowance of payment made to persons covered under Section 40A(2)(b) of the Act and upheld the exclusion of the comparables, namely Infosys BPO, Acropetal Technologies Limited and e-Clerx Services Limited.

2.8 Hence the present appeal.

3. During final arguments, both sides confined themselves largely to the exclusion of e-Clerx Services Limited as a comparable.



3.1 On behalf of the appellant/revenue, it was contended that the respondent/assessee as well as e-Clerx being involved in Knowledge Process Outsourcing (KPOs), e-Clerx was wrongly excluded from comparison by the learned Tribunal. Learned counsel for appellant/revenue submitted that the decision of a co-ordinate bench of this court in the case of **Rampgreen Solutions Pvt. Ltd. vs CIT**, (2015) 60 taxmann.com 355 (Delhi) has been challenged before the Supreme Court so the same cannot be relied upon. It was argued that for the purposes of Arms Length Pricing, the Tribunal instead of laying down stringent standards of comparability ought to have recognized that there cannot be an exact comparable with no difference in a given situation. It was also contended on behalf of appellant/revenue that the other two comparables namely Infosys BPO Ltd. and Acropetal Technologies Ltd. were recognized for being used in TNMM in the guidelines of Organization of Economic Cooperation & Development, so those also ought not to have been excluded by the Tribunal. Learned counsel for appellant/revenue referred to the judgment of a co-ordinate bench of this court in the case **Chryscapital Investment Advisors (India) Pvt. Ltd. vs DCIT**, 2015 SCC OnLine Del 9065 and contended that the mere fact that an entity earns high profits or losses does not *ipso facto* lead to its exclusion from the list of comparables for the purposes of determination of Arms Length Pricing and in such circumstances an inquiry under Rule 10B(3) of the Income Tax Rules must be carried out to determine as to whether the material differences between the assessee and the said entity can be eliminated and unless such differences cannot be eliminated the entity should be determined as comparables.



3.2 On the other hand, learned counsel for respondent/assessee pointed out various differences between the respondent/assessee and e-Clerx as regards the structure and functionalities of the two entities. It was pointed out by learned counsel for respondent/assessee that unlike e-Clerx, the primary function of the respondent/assessee is simply punching in data through freshly employed graduates with no trading experience, without even entering any market risk. It was argued that the distinction between a BPO and a KPO is a vital aspect in the present case to be kept in mind. Learned counsel for respondent/assessee referred to the view taken by other co-ordinate benches of this court by way of rejecting Infosys BPO Ltd. as comparable for the reason of it being a giant corporation in comparison with the litigating assessees of those cases.

4. Admittedly the respondent/assessee is engaged in providing ITeS to its AE through the use of information technology infrastructure including online software, live information services and research on international database. It is also not disputed that in the present case, the most appropriate method for determination of Arms Length Price would be TNMM. As reflected from record, the TPO carried out his own search and zeroed down on nine comparables, out of whom three remain the subject matter of the present appeal. The present appeal seeks to claim that those three comparables namely Infosys BPO Ltd., Actopetal Technologies Ltd. and e-Clerx Services Ltd. were wrongly rejected as comparables by the Tribunal by way of the impugned order. We have examined the challenge to the functional similarity of each of the said comparables with the respondent/assessee.



5. In Transfer Pricing Study Report, work profile of the respondent/assessee is described as follows.

“Futures First was incorporated to utilize the large talent base available in India at relatively lower cost. Futures First provides IT enabled services to its AEs through the use of IT infrastructure. It effectively utilizes IT infrastructure which include use of online software, live information services, research on international databases such as Bloomberg and Reuters and high speed international networks to perform its functions. Futures First provides these services to a group entity Linus which in turn provides services to Indus Derivatives. Futures First activities are detailed below for the Trading Support Function.

- *Research to facilitate trading support activities: Futures First has a support team involved in provision of financial and economic research. These research services facilitate employees to enter buy-sell details. These analysts perform company and industry analysis, secondary data analysis, capital market analysis, commodity demand and supply research etc. The functions of this team are similar to research services provided by Knowledge Process Outsourcing (KPO) companies in India.*

- *Trading support functions: AEs have provided Futures First with adequate online trading tools and knowledge of trading strategies so that these support activities and buy-sell details can be entered by employees without prior experience of trading or financial markets. This can be judged from the fact that over 90% of Futures First employees are either fresh graduates or have no trading experience. The employees analyze data on various online tools and use their knowledge skills to enter buy-sell details. The employees are trained with rules which help them to enter these details. Futures First employs over 370 employees who support execution of main activities of AEs which are performing derivative trades in equities futures (primarily in U.S. and European Stock Indices), commodities futures (e.g. oil, gold, cocoa, coffee, sugar and corn commodity futures) and interest rate futures (e.g. Euro, Sterling and Canadian currency derivatives). Futures First enters buy-sell details for tick trading which essentially means buying and selling on very low margins. These details are primarily system and software driven and the role of employee in India is limited to entering the buy-sell details based on broad guidelines provided by AEs. In addition each employee is allocated only one or two products for which he enters buy-sell details within specified limits.*



- *IT support tools: Futures First has a small support team involved in provision of technical support. These tools help employees in provision of stated support function.*

- *Other related functions: Finance, Accounting, Treasury and Legal Function: The management of Futures First is responsible for managing the finance, treasury, accounting and legal functions relating to Future First operations. In certain areas wherever necessary. Futures First is guided by the AEs. Futures First is also responsible for all local statutory compliance.*

Human Resource Management Function: The HR function at Futures First is coordinated by its local management, which has primary responsibility for recruitment, development and training of the personnel including the emolument structure. In this respect, where appropriate, it is guided by AE policies.

*Marketing of Trading Services: **Futures First does not perform any marketing activity as its role is limited to providing services to its AE. As trading support function is the primary function of Futures First and research and IT support activities are performed primarily to facilitate the support activities, we believe other activities subsumes into support function.***

(emphasis is ours)

6. As reflected from record, the rejected comparable Infosys BPO Ltd. is a giant corporate with turnover of Rs.1081.53 crores as compared to the respondent/assessee whose turnover is only Rs.12.71 crores; net worth of Infosys BPO Ltd. is Rs.661.94 crores which is 99.39 times of the respondent/assessee; even the employees strength of Infosys BPO Ltd. is 44 times more than that of the respondent/assessee. Besides, unlike the respondent/assessee, the excluded comparable Infosys BPO Ltd. has its brand value and ownership of intellectual property rights which aggrandise the status of that company. Further, admittedly, in the respondent/assessee's own case for subsequent assessment year AY 2010-11, the said entity Infosys BPO Ltd. was rejected as comparable in view of the aforesaid dissimilarities. These and various other aspects related to the Infosys BPO



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Ltd. were considered by a co-ordinate bench of this court in the case of **PCIT vs M/s Sanvih Info Group Pvt. Ltd.**, ITA 420/2019 decided on 16.05.2019 in which after examining the judgment in the case of **Chriscapital** (supra), it was observed that none of the remaining comparables involved in the said case was a giant corporation like Infosys. Same is in the present case as well, in the sense that none of the said nine comparables is of the size of Infosys. Besides, Infosys BPO Ltd. is even functionally dissimilar to the respondent/assessee in the sense that it is largely engaged in the area of software development, assuming all risks leading to higher profits, which is not in the case of respondent/assessee. That being so, we find no error in decision of the Tribunal in rejecting Infosys BPO Ltd. as a comparable.

7. As regards the other rejected comparable, namely Acropetal Technologies Ltd., the TPO took segmental information for income from engineering design services and treated it as IT enabled services. The Acropetal has high on-site development expenses whereas the respondent/assessee is engaged only in offshore activities, therefore, the two are not comparable on functional level. The TPO failed to analyse as to how the engineering design services of Acropetal can be compared with low end IT enabled services of the respondent/assessee. Even the segmental detail of Acropetal has not been discussed by the TPO. Therefore, we find no error in the decision of the Tribunal in rejecting Acropetal Technologies Ltd. as a comparable.

8. Lastly in the list of the rejected comparables, comes e-Clerx Services



Ltd. This company, as per record, is a leading Knowledge Process Outsourcing (KPO) company, founded in the year 2000, providing data analytics and data process solutions to some of the largest brands in the world. Over the years, e-Clerx consistently achieved profitable growth and by the year 2008-09, it reached employee strength of about 2000. The e-Clerx has made an inherent niche high-end, KPO data analytics business, scalable - by combining people, process re-engineering and automation in a potent mix to build proprietary, platform based services. The e-Clerx focuses on automation and process re-engineering in order to eliminate wasteful steps, and to automate repetitive ones, so as to minimize the need for human intervention and present their clients costs savings, which exceed those from simple wage arbitrage, which in turn reduces the need for costly, high skilled resources and gives it ability to scale solutions quickly, both for existing clients and also for new ones. In contrast, as detailed above, the respondent/assessee has employed fresh young graduates, engaged in simply punching in the data. Another significant aspect is that e-Clerx carries out its substantial business on outsourcing model, which makes it different from the respondent/assessee. The high end KPO services provider cannot be compared with the ITeS, which fall under the category of BPO services provider, as explained by a coordinate bench of this court in the case of **Rampgreen Solutions** (supra) thus:

“34. We have reservations as to the Tribunal's aforesaid view in Maersk Global Centers (India) Pvt. Ltd. (supra). As indicated above, the expression 'BPO' and 'KPO' are, plainly understood, in the sense that whereas, BPO does not necessarily involve advanced skills and knowledge; KPO, on the other hand, would involve employment of advanced skills and knowledge for providing services. Thus, the expression 'KPO' in common parlance is used to indicate an ITeS provider providing a completely different nature



of service than any other BPO service provider. A KPO service provider would also be functionally different from other BPO service providers, inasmuch as the responsibilities undertaken, the activities performed, the quality of resources employed would be materially different. In the circumstances, we are unable to agree that broadly ITeS sector can be used for selecting comparables without making a conscious selection as to the quality and nature of the content of services. Rule 10B(2)(a) of the Income Tax Rules, 1962 mandates that the comparability of controlled and uncontrolled transactions be judged with reference to service/product characteristics. This factor cannot be undermined by using a broad classification of ITeS which takes within its fold various types of services with completely different content and value. Thus, where the tested party is not a KPO service provider, an entity rendering KPO services cannot be considered as a comparable for the purposes of Transfer Pricing analysis. The perception that a BPO service provider may have the ability to move up the value chain by offering KPO services cannot be a ground for assessing the transactions relating to services rendered by the BPO service provider by benchmarking it with the transactions of KPO services providers. The object is to ascertain the ALP of the service rendered and not of a service (higher in value chain) that may possibly be rendered subsequently.”

Therefore, as regards rejection of e-Clerx as comparable in the present case, we find no error in the decision of the Tribunal.

9. As regards the proposed ground related to Section 40A(ia) of the Act, as mentioned above, no arguments were advanced. Perhaps that was for the reason that regarding this issue the CIT(A) had given direction to the Assessing Officer to verify whether the copies of deduction of tax at lower rate were filed before the Assessing Officer before passing of the assessment order and if that be so, then no disallowance could be made. Before the Tribunal the counsel for revenue stated that the Assessing Officer would give effect to the order of the CIT(A). Accordingly, this ground was treated



as infructuous by the Tribunal. This question thus does not arise for our consideration.

10. The findings as regards rejection of the above-mentioned three comparables being findings of fact and there being no proposed question alleging any perversity, we do not find any substantial question of law to be answered by us. Therefore, the appeal is dismissed.

**GIRISH KATHPALIA
(JUDGE)**

**RAJIV SHAKDHER
(JUDGE)**

DECEMBER 12, 2023/as