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IN THE HIGH COURT OF DELHI AT NEW DELHI

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ITA 217/2017

PR. COMMISSIONER OF INCOME TAX-6, NEW DELHI

..... Appellant

Through: Mr.Puneet Rai, Sr.SC with
Mr.Ashivini Kumar and
Mr.Rishabh Nangia, Jr.SCs.

versus

MERCER CONSULTING INDIA PVT. LTD. (FORMERLY
KNOWN AS M/S MERCER INDIA PVT. LTD.)

..... Respondent

Through: Ms.Ananya Kapoor, Adv for
Mr.Salil Kapoor, Mr.Vibhu
Jain, Mr.Sumit Lalchandani and
Mr.Utkarsh Gupta, Advs.

CORAM:

HON'BLE MR. JUSTICE YASHWANT VARMA

HON'BLE MR. JUSTICE PURUSHAINDRA KUMAR

KAURAV

ORDER

14.03.2024

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1. The Commissioner seeks to assail the judgment rendered by the Income Tax Appellate Tribunal ["ITAT"] dated 25 July 2016 and has posited the following questions for our consideration:-

“2.1 WHETHER on facts and in the circumstances of the case Ld. ITAT is legally justified in holding that provisions of section 92(3) of the Act prohibit the determination of the arm's length price of intra-group services by ignoring provisions of Explanation to section 92(1) and 92B of the Act?

2.2 WHETHER on facts and in the circumstances of the case Ld. ITAT is legally justified in holding that adjustment on account of determination of arm's length price of intra-group services has to be reduced from the cost base of the assessee by ignoring the provisions of transfer pricing under Chapter X of the Act which do not stipulate any corresponding adjustment to the cost base and downward revision of declared profit?

2.3 WHETHER on facts and in the circumstances of the case Ld. ITAT is legally justified in holding that in case of determination of



arm's length price of several categories of international transactions separately the transfer pricing adjustment in respect of one transaction will require adjustment to second category of transaction resulting in reduced profit, even though, no such adjustment is permitted under the provisions dealing with the transfer pricing under Chapter X of the Act?

2.4 WHETHER on facts and in the circumstances of the case Ld. ITAT was legally justified in aggregating the international transactions when they were reported in segregated manner by the Assessee?"

2. We note that while considering the aforesaid aspects, the ITAT has observed as follows:-

“5. As a corollary to the ALP of the intra group services received by the assessee being treated as NIL, the price paid for these intra group services is required to be taken out from the computation of remuneration receivable in respect of IT enabled services rendered by the assessee. This is so for the reason that the pricing of IT enabled services is on the cost plus 20% basis, which has been upheld to be at arm's length price by the DRP, and, therefore, anything removed from the cost will also have to be removed from the computation of amount receivable for the IT enabled services rendered by the assessee. Of course, as far as TPO is concerned, the action at that level was, from this perspective, could have been justifiable inasmuch as the ALP margin was taken at 29.53%, as against 20% taken by the assessee, and, therefore even after removing something from the cost base, due to increase in the mark-up rate, ALP of the services rendered could still be higher vis-a-vis the amount chargeable after including intra group services in the cost base. Once DRP deletes the adjustment in the mark-up rate on cost plus basis, such a possibility ceases to exist. Therefore, in the present circumstances, any ALP adjustment in the consideration for intra group service, which is includible in the cost base, paid by the assessee will actually result in erosion of tax base. The reduction in ALP of consideration of such intra group services by Rs 100 will also result in under realisation of revenue for IT enabled service by Rs 120 (i.e. recovery of cost of Rs 100 plus profit mark up of Rs 20). In effect thus, the taxability in the hands of the assessee, in such a situation, will go up by Rs 100 as an ALP adjustment, but then income of the assessee from IT enabled service revenue, will also stand reduced by Rs 120. Section 93(2) is quite clear and categorical in this regard. It states that "(t)he provisions of this section shall not apply in a case where the computation of Income under sub-section (1)..... has the effect of reducing the income chargeable to tax or increasing the loss, as the case may be, computed on the basis of entries made in the books of account in respect of the previous year in which the international transaction



was entered into". Section 92(1), in turn, states that "(a)ny income arising from an International transaction shall be computed having regard to the arm's length price". What follows is thus that when, as a result of computation of income on the basis of arm's length price, the income of the assessee is lowered or the loss is increased, the provisions of computation of income on the basis of arm's length price do not come into play. Viewed in this perspective, when we examine the facts of the present case, we find that the determination of ALP of the intra group service at NIL value does lower the profits of the assessee inasmuch as the revenue of the assessee from the IT enabled services will reduce correspondingly, and infact 20% more than the adjustment- as a result of loss of mark up as well. The ALP adjustment of Rs 8,40,95,610 by the revenue authorities is, therefore, essentially required to be coupled with reduction of 10,09,14,732. That would erode our tax base, rather than augmenting it. The computation of income from International transactions on the basis of arm's length price, in the given situation, would result in lowering the income of the assessee vis-a-vis the income "computed on the basis of entries made in the books of accounts in respect of the previous year in which the transactions were entered into". In the light of this factual position coupled with the relief granted by the DRP on the ALP adjustment in the mark-up rate of the cost plus basis billing to the AE in respect of revenues for the IT enabled services, and in the light of the provisions of section 92(3), the transfer pricing provisions cannot be invoked in respect of intra group services, which admittedly form part of the cost base of the assessee availed by the assessee. This is a case in which transfer pricing provisions cannot be applied because the application of ALP adjustment will indeed result in erosion of Indian tax base- as visualized by the scheme of Section 92(3) inasmuch for every rupee of ALP adjustment in intra group service, the revenue of the assessee on the basis of application of arm's length price will stand reduced by one and one fifth times of the ALP adjustment Section 92(3) does not permit computation of income on the basis of arm's length price in such a situation; as a matter of fact, it prohibits application of arm's length principle in such a situation. The plea of the assessee, as specifically taken up in ground no. 5 (g), is thus indeed well taken and merits our acceptance."

3. The fact that if the challenge as raised by the appellant were to be accepted, it would result in a reduction of the income chargeable to tax is not questioned or disputed before us.
4. In view of the aforesaid, we find that no exception can possibly be taken to the view as expressed by the ITAT. No substantial



question of law arises. The appeal is thoroughly misconceived and shall consequently stand dismissed.

YASHWANT VARMA, J.

PURUSHAINDRA KUMAR KAURAV, J.
MARCH 14, 2024/MJ