

IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCH 'A', BANGALORE

BEFORE SHRI. SUNIL KUMAR YADAV, JUDICIAL MEMBER
AND
SHRI. ABRAHAM P. GEORGE, ACCOUNTANT MEMBER

I.T(TP).A No.1604/Bang/2014
(Assessment Year : 2009-10)

Deputy Commissioner of Income-tax,
Circle – 6(1)(2), Bangalore .. Appellant

v.

M/s. Sunquest Information Systems (India) P. Ltd,
1st floor, Eagle Ridge, Embassy Gold Links Business Park,
Off Intermediate Ring Road,
Bangalore 560 071 .. Respondent
PAN : AAEC2754E

I.T(TP).A No.1666/Bang/2014
(Assessment Year : 2009-10)
(By the Assessee)

Assessee by : Shri. K.R. Vasudevan, Advocate
Revenue by : Dr. P. K. Srihari, Addl. CIT

Heard on : 05.05.2016
Pronounced on : 27 .05.2016

ORDER

PER ABRAHAM P. GEORGE, ACCOUNTANT MEMBER :

These are appeals filed by the Department and the assessee respectively, directed against an order dt.27.10.2014 of CIT (A) –IV, Bengaluru.

02. Facts apropos are that assessee engaged in providing software development services, design and support, had filed a return declaring income of Rs.9,18,153/-. Since assessee had international transactions with its Associated Enterprise (AE) exceeding the limits laid down, pricing of such international transactions was referred to the TPO by the AO. Profile of the assessee mentioned by the TPO in para 2 of his order, is as a contract software development service provider. Assessee was a wholly owned subsidiary of one M/s. Sunquest, US, and was primarily developing software and providing support to its principal. Sunquest, US, was providing solutions in healthcare services which helped physicians, hospitals and medical practitioners to effectively manage the complexities in healthcare services. For the support services rendered by the assessee, Sunquest, US, was remunerating on cost plus basis. Assessee's financial results for relevant previous year read as under :

Operating Revenues *	19,88,17,946
Forex gain **	2,83,48,688
Total operating revenues	22,71,66,634
Operating Expenses ***	20,34,92,094
Operating (Profit)/Loss	2,36,74,540
Op Profit on cost %	11.63%

03. Whole of the revenue of the assessee came from the software development services rendered to its principal. Though it had also received certain cost reimbursements and expenses from the principal, such reimbursements were considered by the TPO to be at arms length and the adjustments made by him were confined to the software development services.

04. In order to justify its profit on cost of 11.63% assessee had selected 21 comparables. These 21 comparables and their average of operating profit on operating cost as derived by the assessee, read as under :

Sl. No.	Name of the company	Weighted average of operating profits on operating costs (%)
1	Akshay Software Technologies Limited	6.79%
2	Ancent Software International Limited	7.41%
3	Aztecsoft Limited	12.13%
4	CG-VAK Software & Exports Limited	-1.41%
5	Goldstone Technologies Limited	24.01%
6	Helios & Matheson Information Technology Limited	38.09%
7	Indium Software (India) Limited	1.25%
8	Infosys Technologies Limited	40.83%
9	K P I T Cummins Infosystems Limited	12.36%
10	Larsen & Toubro Infotech Limited	16.46%
11	LGS Global Limited (Lanco Global Systems Limited)	24.60%
12	Maars Software International Limited	7.14%
13	Mindtree Limited	12.01%
14	Persistent Systems Private Limited	24.10%
15	Quintegra Solutions Limited	18.95%
16	R S Software (India) Limited	9.80%
17	Sasken Communication Technologies Limited	19.55%
18	S I P Technologies and Exports Limited	-10.97%
19	Softsol India Limited	14.95%
20	V M F Softech Limited	2.08%
21	Zvlog Systems Limited	16.63%
	Arithmetic mean	14.13%

05. As per the assessee, arithmetic mean of 14.13% on the above 21 comparables fell within + / - 5% of its own profit rate of 11.63% and therefore there was no requirement of any adjustments for the pricing of the international transactions with the AE. Assessee had selected TNMM as the most appropriate one for the TP study. TPO while accepting TNMM, was of the opinion that except for Akshay Software Technologies Ltd, Infosys Technologies Ltd, L & T Infotech Ltd, Mindtree Ltd, Persistent Systems P. Ltd, R. S. Software (India) Ltd, Sasken Communications Technologies Ltd, and Zylog Systems Ltd, none of the other comparables selected by the assessee were appropriate. As per the TPO in the case of some of the companies selected by the assessee, employee-cost was less than 25%, in some others export sales were less than 25%, some were functionally different, some failed the RPT filter and some had very negligible turnover. Thereafter, TPO made his own analysis on the capitaline plus and prowess data bases. Final list selected by the TPO for the comparative study read as under :

Sl No.	Name of the Comparable	Sales (in Rs.)	Cost In Rs.)	Margin
1	Kals Information Systems Ltd.	2,14,04,686	1,87,93,813	13.89%
2	Akshay Software Technologies Ltd	12,23,21,483	11,31,49,350	8.11%
3	Bodhtree Consulting Ltd	16,05,75,212	9,89,56,821	62.27%
4	R S Software (India) Ltd.	1,49,57,12,634	1,36,01,02,589	9.97%
5	Tata Elxsi Ltd (segmental)	3,78,43,03,000	3,14,63,15,000	20.28%
6	Sasken Communication Technologies Ltd(seg)	4,05,31,20,000	3,18,69,97,000	27.91%
7	Persistent Systems Ltd	5,19,69,10,000	3,67,52,70,000	41.40%
8	Zylog Systems Limited	7,34,93,51,475		7.81%
	Bodhtree Ltd (seg)	7,93,22,79,326	5,74,06,73,058	5.52%

10	Larsen and Toubro infotech	19,50,83,81,374	15,64,12,76,626	24.72%
11	Infosys Ltd	2,02,64,00,00,000	1,39,17,00,00,000	45.61%
Average mean				24.32%

06. Thereafter the AO made a work out of the working capital adjustment as per the formula prescribed in OECD guidelines, 2009. Average working capital adjustment worked out by the TPO came to (-) 5.12 %. However, as per the TPO, average cost of capital for the uncontrolled comparables came to only 1.71%. He therefore restricted the working capital adjustment to 1.71%. Though the assessee requested the TPO to give an adjustment for risk this was not accepted by the TPO for a reason that an accurate adjustment for risk could not be quantified and

therefore by virtue of Section 10 B of the Act, no such adjustment could be made. He thereafter worked out the adjustment required u/s.92 CA as under :

Arm's Length Mean Margin on cost	24.32%
Less: Working Capital Adjustment (Annex.C)	-5.12%
Adjusted margin	29.44%
Operating Cost	20,34,92,094
Arms Length Price (ALP) 129.44% of Operating cost	26,34,00,166
Price Received	22,71,66,634
Shortfall being adjustment u/s 92CA:	3,62,33,532

Based on the recommendation of the TPO assessment was completed by making an addition of Rs.3,62,33,532/-.

07. Assessee there upon chose to move the CIT(A) in appeal. Before the CIT (A), argument of the assessee was that its comparables were unjustly rejected citing software development revenue being less than 75% of total income. Assessee also assailed application of RPT filter by the TPO. Though the assessee pleaded for application of turnover filter, it seems the said ground was not pressed by the assessee before the CIT (A). Assessee also sought exclusion of eleven number of companies falling in the list of comparables citing functional dissimilarity. However, CIT (A) did not accept these contentions, but on the other hand confirmed the addition

made by the AO. However, CIT (A) accepted assessee's request for granting it risk adjustment. CIT (A) was of the opinion that such a risk adjustment had to be given to the assessee based on prevailing norms.

08. Now before us, Ld. AR submitted that though application of turnover filter was a ground before the CIT (A), assessee had by mistake not pressed such ground. Hence, according to him, he had filed an additional ground for applying upper level of sales turnover for selection of comparables. As per the Ld. AR, by virtue of decision of the Special Bench of the Tribunal in the case of DCIT v Quark Systems P.Ltd, [42 DTR 414], such additional ground had to be admitted.

09. Ld. AR pointed out that Tata Elxsi Ltd (seg), Sasken Communication Technologies Ltd (seg), Persistent Systems Ltd, Zylog Systems Ltd, Mindtree Ltd (seg), L & T Infotech and Infosys Technologies Ltd, had turnover well in excess of Rs.200 crores. Relying on a decision of coordinate bench in the case of Lam Research (India) P. Ltd, v. DCIT [ITA Nos.1437 & 1385/Bang/2014, dt.30.04.2015], Ld. AR submitted that the comparability of these companies had come up before the coordinate bench in this case where the assessee concerned was into software development segment. As per the Ld. AR, of M/s. Lam Research (India) P. Ltd, (supra)

had two segments, namely, software development segment and ITES segment. With regard to the software development segment, this Tribunal had held that the above mentioned companies were to be excluded.

10. Continuing his arguments, Ld. AR submitted that M/s. Bodhtree Consulting Ltd, was also one among the comparables which were disputed in the case of Lam Research India (P) Ltd (supra). According to him, at para 10 of the said order, it was held by this Tribunal that Bodhtree Consulting Ltd, was not a proper comparable in the software development services segment.

11. Vis-a-vis, Tata Elxsi Ltd, Sasken Communication Technologies Ltd, Persistent Systems P. Ltd, Mindtree Ltd (seg) and Infosys Technologies Ltd, Ld. AR submitted that in the same decision, these were directed to be excluded since the turnover of the said companies exceeded Rs.200 crores. As per the Ld. AR, assessee's turnover was negligible and came to only Rs.22.71 crores. As per the Ld. AR, turnover of the above companies was more than ten times of that of the assessee and hence could not be considered as good comparable.

12. Vis-a-vis, Zylog Systems Ltd, Ld. AR submitted that this company also had a turnover of Rs.734.93 crores. According to him, this was evident from para 6 of the order of the Tribunal in of Lam Research (India) P. Ltd, (supra). Similarly, according to him, the turnover of L & T Infotech Ltd, came to Rs.1950 crores and had to go out of the list of comparables on application of turnover filter.

13. Continuing his argument, Ld. AR submitted that CG-VAK (seg) was rejected as a comparable though it formed a part of assessee's list of comparables. As per the Ld. AR it was rejected for a reason that employee cost was less than 25% of turnover. Once again relying on the decision of the Tribunal in Lam Research India P. Ltd, (supra), Ld. AR submitted that comparability of CG-VAK had come up there. In the said case at para 21 of the order, it was held that CG- VAK could be considered as a proper comparable.

14. With regard to the adjustment for foreign currency fluctuation, Ld. AR submitted that this was rightly considered by the CIT (A) to be operational in nature. However according to him, while working out the margins of the comparables also, foreign exchange gains and losses

considered as operational revenue had to be reckoned. As per the Ld. AR, directions in this regard were required to be given by the Tribunal.

15. Per contra, Ld. DR submitted that assessee himself has not pressed the application of turnover filter before the CIT (A) and therefore could not now turn back and require its application. As per the Ld. DR the said aspect was never considered by the CIT (A) and hence required a fresh look by him. Further as per the Ld. DR, if assessee's contentions were accepted what would be left were only four comparables and this would not be sufficient enough to make a meaningful arms length pricing study.

16. We have perused the orders and heard the rival contentions. Assessee's first submission is for application of turnover filter as applied by this Tribunal in the case of M/s Genisys Pvt Ltd Vs DCIT(2011)64 DTR 225. Reliance has also been placed on the case of Yodlee Infotech Pvt. Ltd., vs. ITO (IT(TP)A.108/Bang/2014, dt.12.12.2014). No doubt before the CIT (A) though assessee had raised a ground for applying the turnover filter, it was not pressed. Nevertheless, assessee has raised an additional ground before us for application of turnover filter of Rs.200 crores. By virtue of the Special Bench decision in the case of Quark Systems P. Ltd, (supra), an assessee cannot be deprived of the right to raise

such a pleading as additional ground, since the Transfer Pricing is an evolving area. As per the Ld. DR if the turnover filter is to be applied, matter has to be sent to the CIT (A) for consideration since he had not adjudicated the issue. Assessee is seeking application of turnover filter in the case of Tata Elxsi Ltd, Sasken Communication Technologies Ltd, Persistent Systems Ltd, Zylog Systems Ltd, Mindtree Consulting Ltd (seg), L & T Infotech Ltd, and Infosys Ltd. Reliance has been placed by the assessee on the decision of coordinate bench in the case of Lam Research (India) P. Ltd, (supra). Profile of the assessee, as we have already captured in para 02 of this order is one of providing software development services to its principal abroad. Lam Research (India) P. Ltd, (supra) had two segments, namely, software development services and ITES. With regard to software development services, it was providing software development services to its principal called Novelleus Systems International Inc. USA. Thus vis-a-vis software development services, adjudication done by the Tribunal in the case of Lam Research (India) P. Ltd, (supra) can be applied here also, since the said case was also for the very same assessment year. Turnover of various companies considered in the comparables of the said case appears at para 6 of the order and this is reproduced hereunder :

06. The list of comparables considered by the assessee for its software development segment included 19 companies and for ITES segment included six companies. With respect to the software development segment, TPO when the matter was referred to him by the AO, accepted only five of the companies from the list of assessee, which were Akshay Software Technologies Ltd., Bodhtree Consulting Ltd., Tata Elxsi Ltd., (segmental), Sasken Communication Technologies Ltd., and Mindtree Ltd., (seg). TPO after considering the data bases of prowess and capitaline, arrived at the following list as the appropriate comparables, for the software development segment :

Sl. No.	Name of the comparable	Sales (in Rs.)	Cost (in Rs.)	Margin
1.	Kals Information Systems Ltd	2,14,04,686	1,87,93,813	13.89%
2.	Akshay Software Technologies Ltd	12,23,21,483	11,31,49,350	8.11%
3.	Bodhtree Consulting Ltd	16,05,75,212	9,89,56,821	62.27%
4.	R. S. Software (India) Ltd	1,49,57,12,634	1,36,01,02,589	9.97%
5.	Tata Elxsi Ltd(segmental)	3,78,43,03,000	3,14,63,15,000	20.28%
6.	Sasken Communication Technologies Ltd	4,05,31,20,000	3,18,69,97,000	27.91%
7.	Persistent Systems Ltd	5,19,69,10,000	3,67,52,70,000	41.40%
8.	Zylog Systems Ltd	7,34,93,51,475	6,81,69,98,160	7.81%
9.	Mindtree Ltd (seg)	7,93,22,79,326	5,74,06,73,058	5.52%
10.	Larsen and Toubro Infotech (L & T Infotech)	19,50,83,81,374	15,65,12,76,626	24.72%
11.	Infosys Ltd	2,02,64,00,00,000	1,39,17,00,00,000	45.61%
Average				24.32%

17. It is clear from the above, that turnover of Tata Elxsi Ltd was Rs.378.43 crores, that of Sasken Communication Technologies Ltd, came to Rs.405.31 crores, that of Persistent Systems Ltd, was Rs.519.69 crores, that of Zylog Systems Ltd was Rs.734.9 crores, that of Mindtree Ltd (seg) was Rs.793.22 crores, that of L & T Infotech Ltd, was Rs.1,950.83 crores and that of Infosys Ltd, was Rs.20,264 crores. Turnover of the assessee was only Rs. 22.72 crores. Obviously the volume of activity of the above mentioned companies were much higher to that of the assessee. It was more than ten times that of the assessee. In the case of Lam Research (India) P. Ltd, (supra) with regard to application of turnover filter, it was held as under at para 13 of the order dt.30.04.2015 :

13. We have heard the rival contentions and perused the material on record. In the case of Yodlee Infotech Pvt. Ltd., (supra), it was held as under :

“20. We have to hold that assessee can seek exclusion of comparables which were a part of its own list, at a later stage, and therefore, we are constrained to reject the line of argument of the learned DR. Coming to the arguments of the learned AR that M/s Tata Elxsi Ltd., M/s Sasken Communication Ltd., M/s Persistent Systems Ltd., M/s L&T Infotech and M/s Infosys Ltd., had turnover in excess of Rs.200 Crores and were to be excluded, we are of the opinion that turnover filter can be applied for selection of comparables. This has been the view consistently taken by the Co-ordinate Benches of this Tribunal in a number of cases. In the case of M/s Genisys Pvt Ltd Vs DCIT(2011)64 DTR 225 it was held by this Tribunal as under at paras-8 to 09 of its order;

8. According to learned counsel for the assessee size is an important facet of an enterprise level difference. He submitted that comparables should have something similar or equivalent and should possess same or almost the same characteristics. To use a simile, he submitted that a Maruti 800 car cannot be compared to Benz car, even though both are cars only. He submitted that unusual pattern, stray cases, wide disparities have to be eliminated as they do not satisfy the test of comparability. Companies operating on large scale benefit from economies of scale, higher risk taking capabilities, robust delivery and business models as opposed to the smaller or medium sized companies and therefore, size matters. Two companies of dissimilar size therefore, cannot be assumed to earn comparable margins and this impact of difference in size could be removed by a quantitative adjustment to the margins or price being compared if it is possible to do so reasonably accurately. He submitted that size as one of the selection criteria has also been approved by various Benches of the Tribunal, in the following cases :

1. Dy. CIT vs. Quark Systems (P) Ltd. (2010) 132 TTJ (Chd)(SB) 1 : (2010) 42 DTR (Chd)(SB)(Trib) 414 : (2010) 38 SOT 307 (Chd)(SB), wherein it was held that even the filter of lower turnover of Rs. 1 crore is without any reasonable basis and there is no filter for higher turnover also. The application of turnover filter also leaves much to be desired and has to no rationale basis. In our considered view, it is improper to proceed on the basis that the turnover of Rs. 1 crore to infinite is a reasonable classification as turnover base.

2. E-Gain Communication (P) Ltd. vs. ITO (2008) 118 TTJ (Pune) 354 : (2008) 13 DTR (Pune)(Trib) 65;

3. Sony India (P) Ltd. vs. Dy. CIT (2008) 118 TTJ (Del) 865 : (2008) 14 DTR (Del)(Trib) 228 : (2008) 114 ITD 448 (Del);

4. Dy. CIT vs. Indo American Jewellery Ltd., ITA No. 6194/Mum/2008 [reported at (2010) 131 TTJ (Mumbai) 163 : (2010) 40 DTR (Mumbai)(Trib) 386—Ed.];

5. *Philips Software Centre (P) Ltd. vs. Asstt. CIT (2008) 119 TTJ (Bang) 721 : (2008) 15 DTR (Bang)(Trib) 505 : (2008) 26 SOT 226 (Bang);*

6. *Asstt. CIT vs. NIT (2011) 57 DTR (Del)(Trib) 334*

8.1 He further submitted that size as a criteria for selection of comparables is also recommended by OCED in its TP guidelines. The observation of OCED in para 3.43 of the chapter on guidelines reads as follows :

"Size criteria in terms of sales, assets or number of employees : The size of the transaction in absolute value or in proportion to the activities of the parties might affect the relative competitive positions of the buyer and seller and therefore comparability."

8.2 The learned counsel for the assessee submitted that similar observations were also made by ICAI in para 15.4 of TP guidance note. He submitted that TPO's range of Rs. 1 crore to infinity has resulted in selection of companies like M/s Infosys which is having a turnover of Rs. 9,028 crores which is 1,1007 times bigger than the assessee company which has a turnover of Rs. 8.15 crores. He further submitted that NASSCOM has also categorized the companies based on the turnover as follows :

- 1. Greater than USD 1 billion (approx. Rs. 50,000 crores)*
- 2. Between USD 100 million to USD 1 billion (Rs. 500 crores to Rs. 5,000 crores) and*
- 3. Others having less than USD 100 million (Rs. 500 crores).*

Thus, the learned counsel for the assessee submitted that an appropriate turnover range should be applied in selecting a comparable of uncontrolled companies and the assessee has accordingly, applied the turnover range of Rs. 1 crore to Rs. 200 crores based on Dun and Bradstreet's analysis. He submitted that in the alternative, the categories recognized by NASSCOM may also be applied in selecting comparables.

8.3 The learned Departmental Representative rebutted this argument and submitted that the Act or Rules does not provide for the turnover filter. He submitted that as rightly pointed out by the TPO in the case of service sector, the size of the company does not matter because, the infrastructure layout is very less and it will not affect the profit ratio in any way. He drew our attention to the particular portion of TPO's order wherein the TPO has the reasoning given for rejecting the turnover filter.

9. Having heard both the parties and having considered the rival contentions and also the judicial precedents on the issue, we find that the TPO himself has rejected the companies which are making losses as comparables. This shows that there is a limit for the lower end for identifying the comparables. In such a situation, we are unable to understand as to why there should not be an upper limit also. What should be upper limit is another factor to be considered. We agree with the contention of the learned counsel for the assessee that the size matters in business. A big company would be in a position to bargain the price and also attract more customers. It would also have a broad base of skilled employees who are able to give better output. A small company may not have these benefits and therefore, the turnover also would come down reducing profit margin. Thus, as held by the various Benches of the Tribunal, when companies which are loss making are excluded from comparables, then the super profit making companies should also be excluded. For the purpose of classification of companies on the basis of net sales or turnover, we find that a reasonable classification has to be made. Dun & Bradstreet and NASSCOM have given different ranges. Taking the Indian scenario into consideration, we feel that the classification made by Dun & Bradstreet is more suitable and reasonable. In view of the same, we hold that the turnover filter is very important and the companies having a turnover of Rs. 1 crore to Rs. 200 crores have to be taken as a particular range and the assessee being in that range having turnover of Rs. 8.15 crores, the companies which also have turnover of Rs. 1 to Rs. 200 crores only should be taken into consideration for the purpose of making TP study.

The above view was followed by the Co-ordinate Bench of this Tribunal in the case of M/s Bearing Point Business Consulting Pvt. Ltd.,(supra) At paras-5.1 of its order dated 21-12-2012 it was held as under;

“5.1 We have heard the rival submissions and perused the materials on record. The TPO had, while selecting the above 26 comparables, applied a lower turnover filter of Rs.1 Crore but preferred not to apply any upper turnover limit. The size of the comparable is an important factor in comparability. The ICAI TP guidelines note has observed that the transaction entered into by a Rs.1000 Crores company cannot be compared with the transaction entered into by a Rs.10 Crores company and the two most obvious reasons are the size of the two companies and related economies of scale under which they operate. The TPO’s range had resulted in selection of companies as comparable such as Infosys which was 277 times bigger than that of the assessee. The Bangalore Bench of the Tribunal in the case of M/s Genisys Integrating Systems (Ind.) Pvt.Ltd., Vs DCIT ITA No.1231/Bang/2010 relying on Dun and Bradstreet’s analysis had held that turnover range of Rs.1 Crore to 200 Crore is appropriate. The said proposition has followed by the earlier Benches of this Tribunal in the following cases:

(i) M/s Kodiak Networks (I) Pvt. Ltd., Vs ACIT – ITA No.1413/Bang/2010

(ii) M/s Genisys Microchip(I) Pvt. Ltd., Vs DCIT ITA No.1245/Bang/2010

(iii) Electronic for Imaging Indi Pvt.Ltd., -ITA No.1171/Bang/2010 &

(iv) M/s Trilogy E-Business Software India Pvt.Ltd., Vs DCIT – ITA No.1054/Bang/2011 ated 23.11.2012.

5.1.1 In the case of M/s Genisys Integrating Systems (Ind.) Pvt.Ltd., Vs DCIT (supra) relying o Dun and Bradstreet’ has observed as under;

“9.....we find that the TPO himself has rejected the companies which are making losses as comparables. This shows that there is a limit for the lower end for identifying the

comparables. In such a situation, we are unable to understand as to why there should not be an upper limit also. What should be upper limit is another factor to be considered. We agree with the contention of the learned counsel for the assessee that the size matters in business. A big company would be in a position to bargain the price and also attract more customers. It would also have a broad base of skilled employees who are able to give better output. A small company may not have these benefits and therefore, the turnover also would come down reducing profit margin. Thus, a held by the various benches of the Tribunal, when companies which are loss making are excluded from comparables, then the super profit making companies should also be excluded. For the purpose of classification of companies on the basis of net sales or turnover, we find that a reasonable classification has to be made. Dun and Bradstreet is more suitable and reasonable. In view of the same we hold that the turnover filter is very important and the companies having a turnover of Rs.1 Crore to 200 Crores have to be taken as a particular range and the assessee being in that range having turnover of 8.15 Crores, the companies which also have turnover of 1.00 to 200 Crores only should be taken into consideration for the purpose of making TP study”.

5.12 The above view has been followed in the recent order of the Tribunal in the case of Trilogy E - Business(supra). The relevant findings of the Tribunal are extracted as under;

“20. In this regard we find that the provisions of law pointed out by the learned counsel for the assessee as well as the directions referred to by the learned counsel for the assessee clearly lay down the principle that the turnover filter is an important criteria in choosing the comparables. The assessee’s turnover is Rs.47,46,66,638/-. It would therefore, fall within the category of companies in the range of turnover between 1 Crore and 200 Crores (as laid down in the case of Genesis Integrating Systems (Ind.) Pvt. Ltd., Vs DCIT ITA NO.1231(Bang)/2010) Thus, companies having turnover of more than 200 Crores have to be eliminated from the list of comparables as laid down in several decisions referred to by the learned counsel for the assessee. Applying those tests, the following companies will

have to be excluded from the list of 26 comparables drawn by the TPO viz.,

<u>Turnover Rs.</u>	
1) Flextronics Software Systems Ltd.,	848.66 Crores
2) iGate Global Solutions Ltd.,	747.27 Crores
3) Mindtree Ltd.,	590.39 Crores
4) Persistent Systems Ltd.,	293.74 Crores
5) Sasken Communication Tech.Ltd.,	343.57 Crores
6) Tata Elxsi Ltd.,	262.58 Crores
7) Wipro Ltd.,	961.09 Crores
8) Infosys Tech.Ltd.,	13149 Crores

Accordingly, we have no qualms in directing the TPO to exclude M/s Tata Elxsi Ltd., M/s Sasken Communication Pvt. Ltd., M/s Persistent System Ltd., M/s L&T Infotech Ltd. and M/s Infosys Tech.Ltd., from the selected comparables. This Tribunal in the case of 3DPLM Software Solutions Ltd Vs DCIT (IT(TP) A.1303/Bang/2012 dated 28-11-2013) had also held that Persistent Software Systems Pvt.Ltd., was in product designing services and into software product development. In the same decision it was also held that M/s Infosys Technologies Ltd, had considerable intangibles like IPR, and was into software product development. It was also held that M/s Tata Elxsi Ltd., was developing niche products and into product designing services. Hence, these companies would in any case have to be excluded from the comparables being functionally different.”

18. Even if we say that applying turnover limit of Rs.200 crores may not be a wise and prudent one, the turnover of the comparables mentioned above would clearly show that these were much beyond that of the assessee taking them out of the reasonable realm of comparability. Just because the

matter was not adjudicated by the CIT (A) may not be a reason for sending it back to him when the facts are clearly on record. There can be no dispute on the position of facts as mentioned above. In such a situation it would be fruitless exercise to remit the issue of application of turnover filter back to the CIT (A). We therefore direct exclusion of Tata Elxsi Ltd, Sasken Communication Technologies Ltd (seg), Persistent Systems Ltd, Zylog Systems Ltd, Mindtree Ltd (seg), L & T Infotech Ltd, and Infosys Ltd, from the list of comparables.

19. No doubt we are alive to the fact that Sasken Communication Technologies Ltd, Persistent Systems Ltd, Zylog Systems Ltd, Mindtree Ltd (seg), L & T Infotech Ltd, Infosys Ltd, were a part of assessee's own comparables. However as mentioned by us, assessee had taken a ground before the CIT (A) seeking exclusion based on turnover, though it has not pressed it. At least in the case of Persistent Systems Ltd, CIT (A) specifically mentioned this plea of the assessee though he had not directed its exclusion, for a reason that assessee was not pressing application of turnover filter. In such circumstances, we are of the opinion that assessee can very well plead for exclusion of these companies from the list of comparables.

20. Coming to Bodhtree Consulting Ltd, argument of the assessee is that it is functionally dissimilar. In the case of Lam Research India P. Ltd, (supra), comparability of Bodhtree Consulting Ltd, was an issue. In the software development services segment, it was held as under by this Tribunal at para 18 of its order :

Bodhtree Consulting Ltd.:- As far as this company is concerned, it is not in dispute that in the list of comparables chosen by the assessee, this company was also included by the assessee. The assessee, however, submits before us that later on it came to the assessee's notice that this company is not being considered as a comparable company in the case of companies rendering software development services. In this regard, the ld. counsel for the assessee has brought to our notice the decision of the Mumbai Bench of the Tribunal in the case of Nethawk Networks Pvt. Ltd. v. ITO, ITA No.7633/Mum/2012, order dated 6.11.2013. In this case, the Tribunal followed the decision rendered by the Mumbai Bench of the Tribunal in the case of Wills Processing Services (I) P. Ltd., ITA No.4547/Mum/2012. In the aforesaid decisions, the Tribunal has taken the view that Bodhtree Consulting Ltd. is in the business of software products and was engaged in providing open & end to end web solutions software consultancy and design & development of software using latest technology. The decision rendered by the Mumbai Bench of the Tribunal in the case of Nethawk Networks Pvt. Ltd. (supra) is in relation to A.Y. 2008-09. It was affirmed by the learned counsel for the Assessee that the facts and circumstances in the present year also remains identical to the facts and circumstances as it prevailed in AY 08-09 as far as this comparable company is concerned. Following the aforesaid decision of the Mumbai Bench of the Tribunal, we hold that Bodhtree Consulting Ltd. cannot be regarded as a comparable. In this regards, the fact that the assessee had itself proposed this company as comparable, in our opinion, should not be the basis on which the

said company should be retained as a comparable, when factually it is shown that the said company is a software product company and not a software development services company

Accordingly we have no hesitation in directing the exclusion of Bodhtree Consulting Ltd also.

21. Now taking the pleading of the assessee that CG-VAK was unjustly rejected from the list of comparables, we find that the said company was also one of the comparables , which had come up before this Tribunal in the case of Lam Research (India) P. Ltd, (supra). This Tribunal had held as under at para 21 of the order, as under :

CG-VAK Software & Exports Ltd.

(D) (i) As far as this company is concerned, the TPO rejected the same by applying the 25% employee cost filter. According to the TPO, usually software development services are high-end services performed by skilled and professional employees and hence the cost of rendering such high-end services is also high as they comprise of high salaries and better welfare facilities, compared to low-end services. Therefore, the filter of employee cost of more than 25% of turnover was considered by the TPO while choosing the comparable.

(ii) The submission of the ld. counsel for the assessee was that in the case of assessee, this test is satisfied. In this regard, our attention was drawn to page 818 to 824 of the assessee's paperbook wherein annual report of this company has been provided. Attention was drawn to the fact that in the profit & loss account of the audited accounts, the cost of services has been shown as an expenditure and in Schedule 15 to the Notes to Accounts, it has been elaborated as follows:-

Cost of services:

Cost of Services	- Overseas	2,77,32,337
Cost of Services	- Domestic	2,58,40,435
Transcription charges		3,97,389
Web Designing Charges		1,64,602
Staff Welfare		11,43,144
Staff Training		3,63,496
Contribution to PF & ESI		15,47,906
Gratuity		13,04,894
Ex Gratia		0
HRD Expenses		<u>3,10,871</u>
		<u>5,88,05,074</u>

(iii) It was submitted by the ld. counsel for the assessee that the TPO ignored the contribution to PF & ESI, Gratuity and Ex Gratia payments and arrived at the employee cost. According to the ld. counsel for the assessee, doing so was not proper. If all the employee costs are properly considered, then this company can pass the filter applied by the TPO for excluding it.

(iv) We have considered the submission of the ld. counsel for the assessee and are of the view that prima facie the submissions of the ld. counsel are acceptable. We, however, feel that it would be just and appropriate to direct the TPO to consider including this company as a comparable afresh in the light of the facts brought to our notice by the ld. counsel for the assessee. We hold and direct accordingly.

Following the above, we direct that CG-VAK can be considered as a good comparable.

22. As a result of the above discussion, we direct exclusion of Bodhtree Consulting Ltd, Tata Elxsi Ltd (seg), Sasken Communication Technologies Ltd (seg), Persistent Systems Ltd, Zylog Systems Ltd, Mindtree Ltd (seg),

L & T Infotech Ltd, and Infosys Ltd from the list of comparables and direct inclusion of M/s. CG-VAK as a good comparable. Ordered accordingly.

23. Coming to the pleading of the assessee that foreign exchange adjustment once allowed as operational in nature should also be considered while working out the operating margin of the comparables, we are inclined to agree. This is because comparability should be done based on equal footing and if foreign exchange gains / losses are considered as part of operational income / loss of the assessee, then such items of expenditure , are also to be considered as operational in nature in the case of comparables also. TPO is therefore directed to work out the margin of the comparables that are left in the list after considering foreign exchange gains / losses as operational in nature. Ordered accordingly.

24. Since the Ld. AR had submitted that he was not pressing any grounds other than the grounds relating to application of turnover filter in grounds 5, 6 and 9, other grounds are not considered for adjudication by us.

25. In the result, appeal of the assessee is partly allowed for statistical purpose.

26. Now we take up appeal of the Revenue. Revenue has altogether taken nine grounds of which grounds 1, 8 and 9 are general in nature needing no adjudication. Vide its grounds 2 and 3, grievance raised by Revenue is that CIT (A) directed the AO to exclude from total turnover items which were excluded from export turnover also while working out the deduction available to the assessee u/s.10A of the Act. What we find is that the CIT (A) had followed the judgment of Hon'ble jurisdictional High Court in CIT v. Tata Elxsi Ltd, [349 ITR 98]. Just because of a reason that the Revenue has moved an appeal before the Hon'ble Apex Court against the judgment of Hon'ble jurisdictional High Court, we cannot say that Hon'ble jurisdictional High Court judgment should not be followed. We are of the opinion that CIT (A) was justified in giving directions which were in accordance with the law laid down by the Hon'ble jurisdictional High Court in Tata Elxsi Ltd (supra). Grounds 2 and 3 are dismissed.

27. Vide its ground 4, Revenue is aggrieved on the directions of the CIT (A) to give a risk adjustment to the assessee. CIT (A) had directed the TPO to give risk adjustments at prevailing norms suitable / applicable to the assessee. As per the CIT (A), there was no working capital adjustment actually given by the TPO since the adjustment carried out was negative in

its impact. On this issue what we find is that TPO at para 3.7 of his order had clearly stated that working capital adjustment is restricted to 1.71% considering the uncontrolled comparables selected by him. However, in the actual working of the adjustment u/s.92CA of the Act, reproduced by us at para six above, working capital adjustment has been made at (-) 5,12% . In such a situation, we cannot say that risk adjustment directed by the CIT (A) was incorrect. TPO having not restricted himself to a working capital adjustment of 1.71% as mentioned by him at para 3.7 of his order ought have considered assessee's plea for a risk-adjustment, if found reasonable. In such circumstances, we find that direction given by the CIT (A) was justified and we do not find any reason to interfere. Ground 4 of the Revenue stands dismissed.

28. Vide its grounds 5 and 6, grievance of the Revenue is that loss /gain was considered as operating in nature by the CIT (A). Ld. DR submitted that there was no finding by the CIT (A) that foreign exchange gain / loss was incidental to the operating activity.

29. Per contra, Ld. AR supported the orders of authorities below.

30. We have heard the rival contentions and perused the material on record. Ground 6 of the Revenue clearly admits that forex gain / loss were

incidental to the operating activity of the assessee. Just because it was not critical to the operating activity, we cannot say that these had to be excluded. This Tribunal in the case of Triology E Business Software India P. Ltd v. DCIT [(2013) 147 ITD 540], had held that forex gains / loss are required to be added to the operating revenue relying on another coordinate bench decision in SAP Labs India (P) Ltd, [(2011) 44 SOT 156]. We therefore do not find any error in the directions given by the CIT (A) . Grounds 5 and 6 stand dismissed.

31. To summarise the result, appeal of the assessee is partly allowed whereas appeal of the Revenue is dismissed.

Order pronounced in the open court on 27th day of May, 2016.

Sd/-
(SUNIL KUMAR YADAV)
JUDICIAL MEMBER

Sd/-
(ABRAHAM P GEORGE)
ACCOUNTANT MEMBER

MCN*

Copy to:

1. The assessee
2. The Assessing Officer
3. The Commissioner of Income-tax
4. Commissioner of Income-tax(A)
5. DR
6. GF, ITAT, Bangalore

By Order