

**IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCH " B "**

**BEFORE SHRI ARUN KUMAR GARODIA, ACCOUNTANT MEMBER AND
SHRI VIJAY PAL RAO, JUDICIAL MEMBER**

I.T.(T.P)A. No.1294/Bang/2010 (Assessment Year : 2006-07)		
M/s. Altimetrik India Pvt. Ltd., Sy.No.7(P) and 93(P), Electronic City, Phase II, Indl. Area, Begur Hobli Taluk, Bengaluru-560 100	Vs.	Asst. Commissioner of Income Tax, Circle 1(1)(1), Bangalore.
Appellant		Respondent.

Appellant By : Shri Sharath Rao, C.A. Respondent By : Ms. Neera Malhotra, CIT (DR) (ITAT)-2, Bengaluru.
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Date of Hearing : 06.09.2017.

Date of Pronouncement : 25.10.2017.

O R D E R

Per Shri Vijay Pal Rao, J.M. :

This appeal by the assessee is directed against the assessment order dt.22.09.2010 passed under Section 143(3) r.w.s. 144C of the Income Tax Act, 1961 (in short 'the Act') in pursuant to the directions of the Dispute Resolution Panel (in short 'DRP') dt.30.08.2010 for the Assessment Year 2006-07.

2. The assessee has filed revised concise grounds as under :

1. “ The assessment order dated September 22, 2010 passed by the learned Assessing Officer ("Ld.AO") pursuant to the directions passed by the Honourable Dispute Resolution Panel ("DRP") is not in accordance with the law and is contrary to the facts and circumstances of the present case and in any case in violation of the principle of equity and natural justice.

TRANSFER PRICING

2. The Honourable DRP has erred in upholding the adjustment made by the learned Transfer Pricing Officer ("Ld. TPO") to the Arm's Length Price ("ALP") of the international transactions of the Appellant;
3. The Honorable DRP and the Ld. AO have erred in upholding the action of the Ld. TPO in rejecting the Transfer Pricing ("TP") study of the Appellant and holding it to be "unreliable or incorrect";
4. The Honourable DRP has erred in facts and in law in upholding the action of the Ld. TPO in making ALP adjustment on offshore services which does not have any transactions with associated enterprises and were not 'international transactions';
5. The Honourable DRP has erred in facts and in law in upholding the action of the Ld. TPO in considering transactions of the Appellant which were not 'international transactions' while determining 'onsite revenues to export revenues' filter of 55 percent;
6. The Honourable DRP has erred in facts and in law in, upholding the margins of the following comparables determined by the Ld. TPO by not considering the submissions of the Appellant that there were certain errors in the computation of the margins:
 - ***Orient Information Technologies Limited***
 - ***Synfosys Business Solutions Limited***
7. The learned TPO has, in his fresh study, erred in finalizing the transfer pricing order with the following companies as comparable to the Appellant despite these companies

failing to meet the legally acceptable criteria for comparability. The Honorable DRP has also erred in confirming the order of the TPO in this regard.

- **Zylog Systems Ltd**
- **Visualsoft Technologies Ltd**

8. The Honourable DRP has erred in facts and in law in upholding the action of the Ld. TPO in excluding foreign exchange gain while computing the operating margins of the Appellant;
9. The Honourable DRP has erred in facts and in law in upholding the action of the Ld. TPO in not allowing the benefit of 5 percent range as provided in the proviso to section 92C(2) of the Income-tax Act, 1961 ("Act"), as applicable for the subject assessment year;
10. The Honourable DRP and the learned AO/ TPO have erred in not providing working capital adjustment from the arithmetic mean margin computed by the TPO;

NON TRANSFER PRICING ADJUSTMENT

11. The Ld. AO / Honourable DRP have erred in facts and in law in setting-off the losses of the domestic unit with the profits of the eligible units while computing the relief under section 10A of the Act;
12. The Ld. AO / Honourable DRP have erred in not giving due relief to the brought forward losses as shown by the Appellant in its return of income;
13. The Ld. AO / Honourable DRP has erred in facts and in law in holding that foreign currency expenses of Rs 2,354,254 (break-up provided below) should be excluded from the 'export turnover' while computing the relief under section 10A of the Act:

	Particulars
Insurance expenses	133,540
Foreign travel expenses	23,450
Telecommunication expenses	2,197,264

14. Without prejudice to the above, the Ld. AO / Honourable DRP have erred in facts and in law in reducing the foreign currency expenses only from the 'export turnover' without reducing the same from the 'total turnover' while computing the relief under section 10A of the Act;

OTHERS

- 15. The Appellant craves leave to add, alter, vary, omit, substitute or amend the above grounds, at any time before or at the time of hearing of the appeal. Each of the above objections is independent and without prejudice to the other grounds preferred by the Appellant."**

3. Ground Nos. 1, 2 & 3 are general in nature and do not require any specific adjudication.

4. Ground Nos.4 & 5 are regarding incorrect Transfer Pricing Adjustment by considering the off shore services transactions with non-Associated Enterprise.

5. The assessee company is engaged in the business of computer software development services and IT Enabled Services. The TPO while determining the Arm's Length Price (ALP) in respect of on site services received by the assessee from its AE for providing the services to the clients of the assessee. The assessee retained 5% of the receipt and balance amount is paid to the AE in respect of on site services provided by the AE. The TPO while computing the arm's length cost has taken the total operating cost consist of AE transactions as well as non-AE transactions. The assessee challenged the action of the TPO before the DRP and contended that the adjustment has been made on the off shore segment including uncontrolled transaction that constitute 45% of the

turnover. Thus the assessee contended that the adjustment made by the TPO is based on the wrong details considered by the TPO instead of taking the cost of RPT the TPO took the entire cost. The DRP did not accept the objection and confirmed the action of the TPO.

6. We have considered the rival submissions as well as the relevant material on record. There is no dispute that non-AE transactions constitute 45% of the total turnover. The TPO while computing the arm's length cost of the international transactions has first computed arm's length operating cost of the total transaction which includes AE and non-AE transactions and thereafter the TPO has made the adjustment only in respect of cost of the international transactions. In this process the multiplying factor got changed and therefore the assessee has contended that the TPO has made an excessive adjustment of about Rs.60 lakhs. The assessee has further submitted that if the TPO would have considered only cost of international transactions then the adjustment as per the ALP determined by the TPO would have been Rs.81,37,245 instead of Rs.1,41,90,963 made by the TPO. Thus the learned Authorised Representative has submitted that there is an excess addition of Rs.60,53,718 due to the method adopted by the TPO.

7. On the other hand, the learned Departmental Representative has relied upon the orders of the authorities below and submitted that this particular fact has not been brought to the notice of the authorities below.

8. Having considered the rival submissions as well as the relevant material on record, we note that the TPO while computing the arm's length cost has first determined the total arm's length cost of the entire revenue of the assessee and then it was divided in proportionate to the transaction with the related party and non-related party. The contention of the assessee is that instead of computing the total arm's length cost, the TPO has to compute arm's length cost of the international transactions only and then adjustment if any could have been made. The assessee has also furnished the details to show that in this methodology of the TPO there is excess adjustment. Since these details were not furnished before the authorities below to show how the computation of the arm's length cost and consequential adjustment is giving incorrect results therefore, in the facts and circumstances of the case and in the interest of justice we set aside this issue to the record of the TPO for considering the relevant details and facts of the international transactions as well as non-

related party transactions and then decide this issue after giving an opportunity of hearing to the assessee.

9. Ground No.6 is regarding error in computation of margin of certain companies.

10. At the time of hearing, the learned Authorised Representative of the assessee has stated at Bar that the assessee does not press Ground No. 6 and the same may be dismissed as not pressed. The learned Departmental Representative has raised no objection if the Ground No. 6 is dismissed as not pressed. Accordingly, Ground No. 6 is dismissed being not pressed.

11. Ground No.7 is regarding functional comparability of two companies namely **Zylog Systems Limited** and **Vishal Soft Technology Limited**.

12. We have heard the learned Authorised Representative as well as learned Departmental Representative and considered the relevant material on record. At the outset, we note that the assessee raised objection regarding the functional dissimilarity of these two companies namely **Zylog Systems Limited** and **Vishal Soft Technology Limited** as it is apparent from the objections filed by the assessee before the DRP placed at page Nos.1291 & 1292 of the paper book. However the DRP has not adjudicated this issue of functional

comparability or dissimilarity of these two companies. Accordingly in the facts and circumstances of the case when the DRP has not adjudicated this issue of functional comparability of these two companies, the same is set aside to the record of the DRP for adjudication after affording an opportunity of hearing to the assessee.

13. Ground No.8 is regarding forex gain/loss as operating in nature.

14. We have considered the learned Authorised Representative as well as learned Departmental Representative and perused the material on record. There is no quarrel on the point that the foreign exchange loss or gain arising on account of realization of sales/exports is operating in nature however it requires verification whether such gain or loss pertains to the sales made during the year under consideration or earlier year. Therefore for limited purpose of verification of the forex gain on realization of sale for the year under consideration this issue is set aside to the record of the TPO/A.O.

15. Ground No.9 is regarding the benefit under proviso to Section 92C(2) of the Act.

16. At the time of hearing, the learned Authorised Representative of the assessee has stated at Bar that the assessee does not press Ground No. 9 and

the same may be dismissed as not pressed. The learned Departmental Representative has raised no objection if the Ground No. 9 is dismissed as not pressed. Accordingly, Ground No. 9 is dismissed being not pressed.

17. Ground No.10 is regarding denial of working capital adjustment. The TPO has denied the working capital adjustment to the assessee. The assessee raised this objection before the DRP but could not succeed.

18. We have heard the learned Authorised Representative as well as learned Departmental Representative and considered the relevant material on record. The DRP has rejected the objection of the assessee on the ground that no specific submissions have been made by the assessee in this regard. The learned Authorised Representative has pointed out that the assessee has given all the details in the objections filed before the DRP. In view of the facts and circumstances of the case when the DRP has not adjudicated this issue on merits we set aside the same to the record of the DRP for consideration and adjudication of the same after affording an opportunity of hearing to the assessee.

19. Ground Nos.11 & 12 are regarding restricting the deduction under Section 10A being setting off of the losses of non-STPI unit against the profits of STPI unit.

20. We have heard the learned A.R. as well as learned D.R. and considered the relevant material on record. At the outset, we note that this issue is covered in favour of the assessee and against the revenue by the decision of the Hon'ble jurisdictional High Court in the case of **CIT Vs. Yokogawa India Ltd.** 341 ITR 385 which has been upheld by the Hon'ble Supreme Court vide decision reported in 391 ITR 274 wherein the Hon'ble Supreme Court has held in paras 15 to 17 as under :

“ 15. Sub-section 4 of Section 10A which provides for pro rata exemption, necessarily involving deduction of the profits arising out of domestic sales, is one instance of deduction provided by the amendment. Profits of an eligible unit pertaining to domestic sales would have to enter into the computation under the head "profits and gains from business" in Chapter IV and denied the benefit of deduction. The provisions of Sub-section 6 of Section 10A, as amended by the Finance Act of 2003, granting the benefit of adjustment of losses and unabsorbed depreciation etc. commencing from the year 2001-02 on completion of the period of tax holiday also virtually works as a deduction which has to be worked out at a future point of time, namely, after the expiry of period of tax holiday. The absence of any reference to deduction under Section 10A in Chapter VI of the Act can be understood by acknowledging that any such reference or mention would have been a repetition of what has already been provided in Section 10A. The provisions of Sections 80HHC and 80HHE of the Act providing for somewhat similar deductions would be wholly irrelevant and redundant if deductions under Section 10A were to be made at the stage of operation of Chapter VI of the Act. The retention of the said provisions of the Act i.e. Section 80HHC and 80HHE, despite the amendment of Section 10A, in our view, indicates that some additional benefits to eligible Section 10A units, not contemplated by Sections 80HHC and 80HHE, was intended by the legislature. Such a benefit can only be understood by a legislative mandate to understand that

the stages for working out the deductions under Section 10A and 80HHC and 80HHE are substantially different. This is the next aspect of the case which we would now like to turn to.

16. From a reading of the relevant provisions of Section 10A it is more than clear to us that the deductions contemplated therein is qua the eligible undertaking of an assessee standing on its own and without reference to the other eligible or non-eligible units or undertakings of the assessee. The benefit of deduction is given by the Act to the individual undertaking and resultantly flows to the assessee. This is also more than clear from the contemporaneous Circular No. 794 dated 9.8.2000 which states in paragraph 15.6 that,

"The export turnover and the total turnover for the purposes of sections 10A and 10B shall be of the undertaking located in specified zones or 100% Export Oriented Undertakings, as the case may be, and this shall not have any material relationship with the other business of the assessee outside these zones or units for the purposes of this provision."

17. If the specific provisions of the Act provide [first proviso to Sections 10A(1); 10A (1A) and 10A (4)] that the unit that is contemplated for grant of benefit of deduction is the eligible undertaking and that is also how the contemporaneous Circular of the department (No. 794 dated 09.08.2000) understood the situation, it is only logical and natural that the stage of deduction of the profits and gains of the business of an eligible undertaking has to be made independently and, therefore, immediately after the stage of determination of its profits and gains. At that stage the aggregate of the incomes under other heads and the provisions for set off and carry forward contained in Sections 70, 72 and 74 of the Act would be premature for application. The deductions under Section 10A therefore would be prior to the commencement of the exercise to be undertaken under Chapter VI of the Act for arriving at the total income of the assessee from the gross total income. The somewhat discordant use of the expression "total income of the assessee" in Section 10A has already been dealt with earlier and in the overall scenario unfolded by the provisions of Section 10A the aforesaid discord can be reconciled by understanding the expression "total income of the assessee" in Section 10A as 'total income of the undertaking'.

In view of the decision of Hon'ble Supreme Court (supra), we set aside the order of the CIT (Appeals) qua this issue and direct the Assessing Officer to allow deduction under Section 10A before setting off of the losses of non-STPI unit against the profits of STPI unit.

21. Ground Nos.13 & 14 are regarding exclusion of foreign currency expenses from export turnover while computing the deduction under Section 10A of the Act.

22. We have heard the learned A.R. as well as learned D.R. and considered the relevant material on record. We find that the issue of expenditure incurred towards telecommunication charges in foreign currency is reduced from export turnover an equal amount should also be reduced from total turnover while computing the deduction under section 10A of the Act, is covered in favour of the assessee by the decision of the Hon'ble Karnataka High Court in the case of **CIT Vs. Tata Elxsi Ltd.** 349 ITR 98 (Kar). The decision of Hon'ble jurisdictional High Court has been followed in a number of cases in co-ordinate benches of ITAT. Hence, this issue is decided against the revenue and in favour of assessee.

23. Ground No.15 is general in nature and do not require any specific adjudication.

24. In the result, the appeal of the assessee is partly allowed.

Order pronounced in the open court on 25th Oct., 2017.

Sd/-
(ARUN KUMAR GARODIA)
Accountant Member

Sd/-
(VIJAY PAL RAO)
Judicial Member

Bangalore,
Dt. 25.10.2017.

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