

**THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCH "B", HYDERABAD**

**BEFORE SMT P. MADHAVI DEVI, JUDICIAL MEMBER
AND SHRI B. RAMAKOTIAH, ACCOUNTANT MEMBER**

**ITA No.232/Hyd/2016
Assessment Year: 2011-12**

Open Text Corporation vs. Dy. CIT, Circle-1(2),
India Pvt Ltd., (Cordys Hyderabad.
Software India Pvt Ltd is
now merged with Open Tex
Corporation India Pvt Ltd.,)
Hyderabad.
PAN- AAACB8264E

(Appellant)

(Respondent)

Assessee by : Shri Ravi Bharadwaj
Revenue by : Shri R. Laxman

Date of hearing : 07-02-2018
Date of pronouncement : 28-03-2018

ORDER

PER P. MADHAVI DEVI, J.M.:

This is assessee's appeal for the A.Y 2011-12. The assessee was originally known as M/s Cordys Software India Pvt Ltd., and the assessment was completed in the said name. The appeal was also disposed of by the CIT(A) in the same name. Thereafter, there has been a merger with M/s. Open Text Corporation India Pvt. Ltd., and the revised Form No. 36 incorporating the name of assessee as M/s Open Text Corporation India Pvt. Ltd., is filed on

27.10.2017 and therefore this appeal is disposed in the name of the merged company.

2. In this appeal, the assessee is aggrieved by the transfer pricing adjustment made by the TPO by imputing interest on outstanding receivables relating to provision of software services rendered by the assessee to its AEs as on 31.03.2011. The assessee has raised the following grounds of appeal:

1.a) Making TP adjustment by imputing interest at 5% on outstanding receivables relating to provision of software services to Associated Enterprise's (AE's) as on March 31st 2011:

(i) Not appreciating that the instant transaction is not covered in the definition of international transaction as defined u/s 92B of the Act in the facts and circumstances of the case.

(ii) Not appreciating the fact that the receivables are consequential closely linked to the principle transaction of provision of software services and hence have been aggregated for determination of ALP under TNMM.

(iii) Not appreciating the facts and circumstances surrounding the receivables and re-characterizing the outstanding receivables as unsecured loans advanced to AEs.

(iv) Not appreciating the fact that under TNMM, the impact of outstanding receivables on the working capital adjustments have already been taken into account while determining the arm's length margin for the international transactions and hence there is no need of imputing interest on outstanding receivables again.

l.b) Without prejudice to the above, not undertaking an objective economic analysis to determine the arm's length price of the outstanding receivables by

(i) Not appreciating that the receivables due from overseas AE's are in foreign currency and hence interest, if any, is

to be benchmarked with the rates prevalent in the international market for foreign currency loans. (i.e. at USD "LIBOR plus").

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2. Imposition interest u/s section 234B and 234D of the Act on the Transfer Pricing adjustment.

3. Imposing penalty u/ s 271(1)(C) of the Act

3. Brief facts of the case are that the assessee company, which is engaged in the business of providing software development services, consultancy and reselling services, filed its e-return for the A.Y 2011-12 on 29.09.2011 admitting a total income of Rs. 9,90,00,709/- under the normal provisions of the Act and Rs. 10,40,34,469/- under the provisions of sec 115JB of the Act. During the assessment proceedings u/s 143(3), the A.O observed that the assessee has entered into an international transaction with its AEs and therefore he made a reference to the TPO u/s 92CA of the Act for determining the Arm's Length Price.

4. The TPO during the proceedings u/s 92CA of the Act, called for various details and observed that after allowing the working capital adjustment, the transactions of software development services and also the distribution activity are at Arm's Length. However, he observed that a sum of Rs. 45,38,74,268/- was receivable by the assessee

at the end of the year and that a sum of Rs. 45.12 crores has been received after considerable delay and the balance has been received within time. He, therefore, issued a show cause notice proposing to charge interest @ 12% on the delayed receipts after allowing credit period of one month.

5. The assessee submitted its detailed explanation, but the TPO was not convinced with the contentions of the assessee. The TPO observed that any independent party would like to receive its funds within the credit period allowed and if not, would normally charge interest. After coming to this conclusion, the TPO relied upon the decision of the Tribunal at Bengaluru in the case of Logix Micro Systems Ltd., in ITA No. 524/Bang/2009 (42 SOT 525), for charging interest @ 12% p.a and proposed an adjustment under Sec. 92CA of the Act.

6. The A.O, consequently proposed the draft assessment order, against which, the assessee preferred its objections before the DRP. The DRP, vide its orders dated 02.11.2015, confirmed the order of the A.O, but restricted the interest to 5% as against 12% applied by the TPO.

Thereafter, the A.O passed the final assessment order, against which the assessee is in appeal before us.

7. The Ld. Counsel for the assessee submitted that the interest on outstanding receivables has become an international transaction only by virtue of Finance Act 2012 and therefore is applicable only prospectively and cannot be applied to the assessment year before us. He submitted that similar transaction of corporate guarantee also has become an international transaction only by virtue of the amendment in 2012, and various Benches of the Tribunal including the Benches at Hyderabad have held the amendment to be applicable prospectively. He also placed reliance upon some decisions to contend that notional interest on outstanding receivables cannot be treated as an international transaction and taxed during the relevant assessment year.

8. The Ld. DR, on the other hand, supported the orders of the authorities below.

9. Having regard to the rival contentions and material on record, we find that the issue whether notional interest is chargeable on receivables has been considered by the

Coordinate Bench in the case of Pegasystems Worldwide

India Pvt Ltd (cited Supra) and it was held as under:

“17.3. We have considered the issue and examined the rival contentions. In the case of Evonik Degussa India P. Ltd., in ITA No. 7653/Mum/2011, it was already held the TP adjustment cannot be made on hypothetical and notional basis, until and unless there is some material on record that there has been under charging of real income. Thus on the facts and circumstances of the case, we are of the opinion that addition on account of notional interest relating to alleged delayed payment in collection of receivables from the AEs is uncalled for on the facts of the present case. Even though DRP tried to distinguish the above decision on facts, as seen from the facts in both the cases, we are of the opinion that the above decision will equally apply to Assessee's case. Assessee has outstanding service charges receivables and as seen from the order of TPO, the outstanding is only from 31-07-2009. There seems to be no such delay in earlier months. Assessee has no interest liability at all so notional interest cannot be brought to tax under the provisions of TP. As rightly pointed out by the Ld. Counsel, the outstanding receivables on account of services cannot be equated with capital financing as provided for in the Explanation by the amendment by Finance Act, 2012 retrospectively. Even otherwise, as rightly held by the Logix Micro Systems Ltd v. ACIT [42 SOT 525] (supra), TPO should have allowed some interest free period for receiving the outstanding service charges. While acknowledging the order of the ITAT, TPO did not even bother to exclude the reasonable period and levied interest not only from the date of invoice to the date of realization during the year but also for the period beyond 31-03-2010 in later year. We were informed that no such addition was made in the later year on Assessee's receivables. We are of the opinion that both on the facts of the case and principles of law, there is no need for bringing to tax the notional interest on the outstanding receivables. Accordingly, we allow the grounds 7 & 8 of Assessee and direct AO/ TPO to delete the said addition made.”

10. Respectfully following the above decision, we hold that the notional interest on outstanding receivables is not chargeable and no TP adjustment can be made. Thus, ground of appeal No. 1.a (i) is allowed.

11. As regards the other grounds of appeal, we find that where the working capital adjustment is considered by the A.O, it takes care of the interest on receivables as well. This aspect has been considered by the Tribunal at Delhi in the case of Kusum Healthcare Pvt Ltd., in ITA No. 6814/Del/2014 dated 31.03.2015 which has been confirmed by the Hon'ble High Court of Delhi and at para 14 of its order has held as under:

“14. As mentioned earlier, the differential impact of working capital of the assessee vis-à-vis its comparables has already been factored in the pricing/profitability of the assessee and therefore, any further adjustment to the margins of the assessee on the pretext of outstanding receivables is unwarranted and wholly unjustified.”

12. We find that the Hon'ble High Court of Delhi has confirmed the decision of the ITAT and the SLP filed by the Revenue is pending before the Hon'ble Supreme Court. We find that in the case of EPAM Systems India Pvt Ltd in ITA No. 192/Hyd/2017 dated 24.10.2017, Coordinate Bench of this Tribunal has followed the decision of the Hon'ble Delhi High Court in the case of Kusum Healthcare Pvt Ltd., to

hold that working capital adjustment takes into consideration the interest on the receivables as well. Therefore, on this ground also, no TP adjustment is required. Thus grounds No. 1a(ii) to (iv) are allowed.

13. In view of the above decision, the alternate ground in No. 1(b) is not decided at this stage, as it would be only an academic exercise. Ground No.2 is consequential in nature and AO is directed to give consequential relief, if any, to the assessee.

14 In the result, the appeal filed by the assessee is partly allowed.

Pronounced in the open court on 28th March, 2018.

Sd/-

Sd/-

(B. RAMAKOTAIAH)
ACCOUNTANT MEMBER

(P. MADHAVI DEVI)
JUDICIAL MEMBER

Hyderabad, Dated: 28th March, 2018

KRK/pvv

- 1 M/s Open Text Corporation Ind Pvt Ltd., C/o Building 'D' Plot No. 17, Software Units Layout, Madhupur, Hyderabad – 500 081.
- 2 Dy CIT, Circle-16(2), Hyderabad.
- 3 Dispute Resolution Panel-1, Bengaluru – 560 001.
- 4 Pr.CIT-1, Hyderabad.
- 5 The DR, ITAT Hyderabad