IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCH " A "

BEFORE SHRI A.K. GARODIA, ACCOUNTANT MEMBER AND
SHRI VIJAY PAL RAO, JUDICIAL MEMBER

I.T.(T.P) A. No.288/Bang/2015 (Assessment Year : 2010-11)		
Income Tax Officer, Ward 6(1)(2), Bangalore.	Vs.	M/s. Solidcore Techsoft Systems (India) Pvt. Ltd., (now merged with McAFee Software India Pvt. Ltd.) Embassy Golf Links, Business Park Pine Valley, 2nd Floor, Intermediate, Bangalore-560 066 PAN AAHCS 7694C
Appellant		Respondent.

I.T.(T.P) A. No.609/Bang/2015
(Assessment Year : 2010-11)
(By Assessee)

Assessee By : Shri Ujjwal Tiwari,Advocate.
Revenue By : Shri G.R. Reddy, CIT (DR) (ITAT)-1, Bengaluru.

Date of Hearing : 06.03.2017.
Date of Pronouncement : 28.04.2017.

O R D E R

Per Shri Vijay Pal Rao, J.M. :

These cross appeals are directed against the assessment order dt.30.01.2015 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.16.12.2014 for the Assessment Year 2010-11.

2. First we take up the revenue's appeal wherein the revenue has raised the following grounds :

1. The directions of the Dispute Resolution Panel are opposed to law and facts of the case.
2. On the facts and in the circumstances of the case the Dispute Resolution Panel erred in law in holding that the size, turnover and brand of the company are the deciding factors for treating a company as a comparable and accordingly erred in excluding M/s. Tata Elxsi Limited, Sasken Communication Technologies Ltd., Persistent Systems Ltd., Mindtree Ltd., L & T Infotech and Infosys Technologies Ltd. as comparables.
3. On the facts and in the circumstances of the case, the Disputes Resolution Panel erred in excluding uncontrolled comparables having turnover more than Rs. 200 crores in the absence of Turnover criterion prescribed in Rule 10B of Income Tax Rules and also there being no correlation between turnover and profit margin.
4. On the facts and in the circumstances of the case the Dispute Resolution Panel erred in stating that there is no reliable method to make adjustment on account of risk level and has erred in directing to give 1% risk adjustment to the average margin.
5. On the facts and in the circumstances of the case, the Dispute Resolution Panel erred in directing the AO to reduce the expenditure incurred towards telecommunication, insurance and travel expenses incurred in foreign currency both from the Export Turnover and as well from Total Turnover for the purpose of computation of deduction u/s 10A of the Income tax Act without appreciating the fact that the statute allows exclusion of such expenditure only from the Export Turnover by way of specific definition of export turnover as envisaged by sub clause (4) of explanation 2 below sub section 8 of Section 10A by placing reliance on the decision of Hon'ble High Court of Karnataka in the case of M/s Tata Elxsi Ltd., which has not become final since the same has not been accepted by the Department and SLPs are pending before the Hon'ble Supreme Court.

6. For these and other grounds that may be urged at the time of hearing, it is prayed that the directions of the Dispute Resolution Panel in so far as it relates to the above grounds may be reversed.

7. The appellant craves leave to add, alter, amend and / or delete any of the grounds mentioned above.

3. Ground No.1 is general in nature and do not require any specific adjudication.

4. Ground No.2 & 3 are regarding exclusion of companies from the set of comparables by applying the turnover filter of more than Rs.200 Crores.

5. We have heard the learned Authorised Representative as well as learned Departmental Representative and considered the relevant material on record. The assessee is a software development services provider. The assessee has reported its international transactions which have been reproduced by the TPO/A.O. in para 3.1 as under **:**

3.1 International transactions (as mentioned in the 92CE Report)

Sl. No.	Type of transaction	Amount (Rs)
1	Provision of Software Development services	16,78,89,904
2	Reimbursement of expenses	8,08,584
3	Receipt of assets on loan basis	20,37,876
	Total	**17,07,36,364**

Thus the turnover of the assessee from international transactions is Rs.17.07 Crores. Since the Dispute Resolution Panel ('DRP') has excluded six companies

by applying the turnover filter of more than Rs.200 Crores, the revenue has challenged the directions of the DRP and consequent assessment order. Though the filter of Rs.200 Crores may not be appropriate filter however even if we apply the turnover filter of 10 times of the assessee's turnover on both sides, the companies which are having more than Rs.171 Crores of turnover are required to be excluded. In view of the fact that the DRP has excluded the companies which are having more than Rs.200 Crores turnover which is more than the filter to be applied at 10 times of the assessee's turnover which comes to Rs.171 Crores, we do not find any reason to interfere with the impugned order and directions of the DRP as by applying the filter of 10 multiples all these six companies are required to be excluded from the set of comparables.

6. Ground No.4 is regarding risk adjustment allowed by the DRP.

7. The learned Departmental Representative has submitted that the assessee has not furnished any computation or details as to how the risk adjustment has to be calculated therefore the directions of the DRP are not sustainable. In support of his contention, he has relied upon the decision of co-ordinate bench of this Tribunal dt.22.1.2016 in the case of **Zyme Solutions Pvt. Ltd. Vs. ITO** in IT(TP)A No.465/Bang/2015.

8. On the other hand, the learned Authorised Representative has not disputed this fact that the assessee did not furnish any detail in respect of risk adjustment claim.

9. Having considered the rival submissions and relevant material on record, when the assessee has not given any details and computation for risk adjustment then the claim of the assessee is purely hypothetical in nature. The co-ordinate bench of this Tribunal in the case of **Zyme Solutions Pvt. Ltd. Vs. ITO** (supra) has considered an identical issue in para 23 as under :

> " 23. We have perused the orders and heard the rival contentions. No doubt, DRP had followed a coordinate bench decision in the case of Inellinet Technologies India P. Ltd v. ITO [ITA No.1237/Bang/2007], in taking a view that single customer risk borne by a tax payer as a competing service provider was equivalent to the market and technical risk borne by the comparables. Nevertheless assessee itself had never made any attempt in its TP study to quantify the risk. On the other hand, assessee itself had mentioned the difficulties of attempting a risk adjustment. We are of the opinion that the DRP was putting the onus on TPO to give a risk adjustment on the PLI, when assessee had never discharged its onus in its TP study. Perceived single party risk is purely hypothetical and since assessee's AE is its holding company, it is in its best interest that work is given to the assessee. It is not that assessee could not have had other client, but it chose to service only its principal. Thus the perceived risk even if any, has been voluntarily taken by the assessee. An adjustment for such a perceived or hypothetical risk can never be factored while working out the Profit Level Indicator. In the circumstances, we are of the opinion that DRP ought not have directed the TPO to consider the risk adjustment at 1%. We find merit in this ground taken by the Revenue. Ground 5 of the Revenue is allowed."

In view of the facts and circumstances when the assessee has not made any attempt to quantify the risk or furnish the details for computation of risk adjustment then by following the decision of the co-ordinate bench, we decide this issue in favour of the revenue and set aside the directions of the DRP.

10. Ground No.5 is regarding exclusion of expenditure incurred towards telecommunications, insurance and travel in foreign currency both from export turnover and total turnover.

10.1 We have heard both sides and perused and carefully considered the material on record and the judicial decision cited. On perusal thereof we find that the issue before us for adjudication i.e. if expenditure incurred towards telecommunications, insurance and travel in foreign currency attributable to the delivery of computer software abroad 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 Tata Elxsi Ltd. (supra). In this order, the Hon'ble Court held –

> *" The Bombay High Court had an occasion to consider the earning of the word 'total turnover' in the context of section 10A, in the case of CIT Vs. Gem Plus Jewellery India Ltd. (2011) [330 ITR P. 175 (Bom)] (2010-TIOL-456-HC-MUM-IT). Interpreting sub-section (4) of section 10A, it is held as under :*
>
> *"Under sub-section (4) the proportion between the export turnover in respect of the articles or things, or as the case may be, computer software exported, to the total turnover of the business carried over by the undertaking is applied to the profits of the business of the undertaking in computing the profits of the business of the undertaking in computing the profits derived from export. In other words the profits of the business of the undertaking are multiplied by the export*

turnover in respect of the articles, things or, as the case may be, computer software and divided by the total turnover of the business carried on by the undertaking. The formula which is prescribed by sub-section (4) of section 10A is as follows :

<table>
<tr><td rowspan="2">Profits derived from export of articles or things or computer software.</td><td>Profits of the business of the undertaking.</td><td>Export turnover in respect of the articles or things or computer software.</td></tr>
<tr><td colspan="2">Total turnover of the business carried on by the undertaking</td></tr>
</table>

The total turnover of the business carried on by the undertaking would consist of the turnover from export and the turnover from local sales. The export turnover constitutes the numerator in the formula prescribed by sub-section (4). Export turnover also forms a constituent element of the denominator in as much as the export turnover is a part of the total turnover. The export turnover, in the numerator must have the same meaning as the export turnover which is constituent element of the total turnover in the denominator. The legislature has provided a definition of the expression "export turnover" in Expln.2 to s.10A which the expression is defined to mean the consideration in respect of export by the undertaking of articles, things or computer software received in or brought into India by the assessee in convertible foreign exchange but so as not to include inter alia freight, telecommunication charges or insurance attributable to the delivery of the articles, things or software outside India. Therefore in computing the export turnover the legislature has made a specific exclusion of freight and insurance charges. The submission which has been urged on behalf of the revenue is that while freight and insurance charges are liable to be excluded in computing export turnover, a similar exclusion has not been provided in regard to total turnover. The submission of the revenue, however, misses the point that the expression "total turnover" has not been

defined at all by Parliament for the purposes of s.10A. However, the expression "export turnover" has been defined. The definition of "export turnover" excludes freight and insurance. Since export turnover has been defined by Parliament and there is a specific exclusion of freight and insurance, the expression "export turnover" cannot have a different meaning when it forms a constituent part of the total turnover for the purposes of the application of the formula. Undoubtedly, it was open to Parliament to make a provision which has been enunciated earlier must prevail as a matter of correct statutory interpretation. Any other interpretation would lead to an absurdity. If the contention of the Revenue were to be accepted, the same expression viz. 'export turnover' would have a different connotation in the application of the same formula. The submission of the Revenue would lead to a situation where freight and insurance, though these have been specifically excluded from 'export turnover' for the purposes of the numerator would be brought in as part of the 'export turnover' when it forms an element of the total turnover as a denominator in the formula. A construction of a statutory provision which would lead to an absurdity must be avoided."

The Special Bench of the Tribunal, in the case of ITO Vs. Sak Soft Ltd. (2009) 313 ITR (AT) 353 (Chennai) (SB) (2009-TIOL-187-ITAT-MAD-SB) also had an occasion to consider the meaning of the word 'total turnover'. After referring to the various judgments of the High Court as well as the Supreme Court held as under :

"53. For the above reasons, we hold that for the purpose of applying the formula under sub-section (4) of section 10-B, the freight, telecom charges or insurance attributable to the delivery of articles or things or computer software outside India or the expenses, if any, incurred in foreign exchange in providing the technical services outside India are to be excluded, both from the export turnover and from the total turnover, which are the numerator and the denominator respectively in the formula….."

The formula for computation of the deduction under section 10A would be as under :

Profits of the business x export turnover / Total turnover

From the aforesaid judgments, what emerges is that, there should be uniformity in the ingredients of both the numerator and the denominator of the formula, since otherwise it would produce anomalies or absurd results. Section 10A is a beneficial section. It is intended to provide incentives to promote exports. The incentive is to exempt profits relatable to exports. In the case of combined business of an assessee, having export business and domestic business, the legislature intended to have a formula to ascertain the profits from export business and domestic business, the legislature intended to have a formula to ascertain the profits from export business by apportioning the total profits of the business on the basis of turnovers. Apportionment of profits on the basis of turnover was accepted as a method of arriving at export profits. In the case of section 80HHC, the export profit is to be derived from the total business income of the assessee, whereas in section 10A, the export profit is to be derived form the total business of the undertaking. Even in the case of business of an undertaking, it may include export business and domestic business, in other words, export turnover and domestic turnover. The export turnover would be a component or part of a denominator, the other component being the domestic turnover. In other words, to the extent of export turnover, there would be a commonality between the numerator and the denominator of the formula. In view of the commonality, the understanding should also be the same. In other words, if the export turnover in the numerator is to be arrived at after excluding certain expenses, the same should also be excluded in computing the export turnover as a component of total turnover in the denominator. The reason being the total turnover includes export turnover cannot be different. Therefore, though there is no definition of the term 'total turnover' in section 10A, there is nothing in the said section to mandate that, what is excluded from the numerator that is

export turnover would nevertheless form part of the denominator. Though when a particular word is not defined by the legislature and an ordinary meaning is to be attributed to the same, the said ordinary meaning to be attributed to such word is to be in conformity with the context in which it is used. When the statute prescribes a formula and in the said formula, 'export turnover' is defined, and when the 'total turnover' includes export turnover, the very same meaning given to the export turnover by the legislature is to be adopted while understanding the meaning of the total turnover, when the total turnover includes export turnover. If what is excluded in computing the export turnover is included while arriving at the total turnover, when the export turnover is a component of total turnover, such an interpretation would run counter to the legislative intent and impermissible. If that were the intention of the legislature, they would have expressly stated so. If they have not chosen to expressly define what the total turnover means, then, when the total turnover includes export turnover, themeaning assigned by the legislature to the export turnover is to be respected and given effect to, while interpreting the total turnover which is inclusive of the export turnover. Therefore the formula for computation of the deduction under section 10A, would be as under :

$$\frac{\text{Profits of the business of the undertaking} \times \text{Export turn over}}{\text{(Export turnover + domestic turn over)}}$$

Total Turnover

11. In that view of the matter, we do not see any error committed by the Tribunal in following the judgments rendered in the context of section 80HHC in interpreting section 10A when the principle underlying both these provisions is one and the same. Therefore, we do not see any merit in these appeals. The substantial question of law framed is answered in favour of the assessee and against the revenue."

Respectfully following the aforementioned decision of the Hon'ble High Court of Karnataka in the case of Tata Elxsi Ltd. (supra), we uphold the directions of DRP in directing the Assessing Officer to reduce the expenditure incurred towards telecommunications, insurance and travel in foreign currency from both export turnover and total turnover for the purpose of computing the deduction under section 10A of the Act in the case on hand. Consequently this ground raised by revenue is dismissed.

11. The assessee has raised the following grounds :

Corporate Tax

1. Re-computation of deduction under section 10A of the Act claimed by the Appellant in its Return of Income.

1.1 The learned Assessing Officer ("AO") has erred in facts and in law in reducing the foreign exchange loss from export turnover without giving any reasons for making such adjustments and has also erred in not providing an opportunity to make any submission against the impugned adjustment.

1.2 Without prejudice to the above objections (raised in ground no 1.1) the learned AO has further erred in considering an incorrect figure for foreign exchange losses in order to compute the deduction under section 10A of the Act.

2. Incorrect computation of demand to be payable by the Appellant.

2.1 The learned AO has erred in facts and in law in not correctly determining the tax demand payable by the Appellant.

2.2 Consequently, the learned AO has erred in levying interest u/s. 234D of on the purported excess refund been granted to the Appellant.

The appellant craves leave to add, alter and modify the above grounds during the course of the appeal.

12. Ground No.1 is regarding restricting the deduction under Section 10A by reducing the foreign exchange loss from the export turnover.

13. The assessee has contended that the Assessing Officer has not given appropriate opportunity to make the submissions against the said rejection of export turnover. Further the figure taken by the Assessing Officer is not a correct amount in respect of foreign exchange loses while computing the deduction under Section 10A. Thus the learned Authorised Representative has submitted that this issue requires a proper verification and fresh adjudication at the level of the Assessing Officer.

14. On the other hand, the learned Departmental Representative has relied upon the orders of the authorities below.

15. Having considered the rival submissions and perused the relevant material on record, we note that the foreign exchange loss has to be considered only arising from the sale proceeds and pertaining to the period relevant to the assessment year under consideration. Since the assessee has contended that it was not given an appropriate opportunity to make submissions 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 Assessing Officer for proper verification and adjudication of this issue as per law. We make it clear that foreign exchange loss is reduced from the export turnover, the same

has to be also reduced from the total turnover for the purpose of computing the deduction under Section 10A of the Act.

16. Ground No.2 is regarding levy of interest under Section 234D which is consequential in nature.

17. In the result, the appeals of the assessee and revenue are partly allowed for statistical purpose.

Order pronounced in the open court on 28th April, 2017.

Sd/-	Sd/-
(A.K. GARODIA)	**(VIJAY PAL RAO)**
Accountant Member	Judicial Member

Bangalore,
Dt. 28.04.2017.

*Reddy gp

Copy to :

1. Appellant
2. Respondent
3. C.I.T.
4. CIT(A)
5. DR, ITAT, Bangalore.
6. Guard File.

Assistant Registrar
Income Tax Appellate Tribunal
Bangalore.