

**IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCH "A", HYDERABAD**

**BEFORE SMT P. MADHAVI DEVI, JUDICIAL MEMBER
AND SHRI S. RIFAUR RAHMAN, ACCOUNTANT MEMBER**

**ITA No. 584/Hyd/2016
Assessment Year: 2011-12**

Income Tax Officer,
Ward – 2(1), Hyderabad.

vs. Knoah Solutions Pvt. Ltd.,
Hyderabad.

(Assessee)

PAN – AABCK 6861 B
(Respondent)

Revenue by : Smt. Alka Rajvanshi Jain
Assessee by : Shri A.V. Raghuram

Date of hearing : 25-09-2018
Date of pronouncement : 09-11-2018

ORDER

PER S. RIFAUR RAHMAN, A.M.:

This appeal filed by the revenue is directed against the order passed u/s 143(3) r.w.s. 92CA(3) of the Income Tax Act, 1961 (in short 'Act') dated 26/02/2016 relating to AY 2011-12.

2. Brief facts of the case are, the assessee company, which is engaged in the business of software development, filed its return of income for AY 2011-12 on 25/11/2011 declaring income of Rs. 17,30,364/- after claiming deduction u/s 10A of Rs. 2,50,56,792/-. The AO referred the case under section 92CA(1) of the IT Act for determination of arm's length price in respect of the international transactions reported by the taxpayer company for the FY relevant to the AY 2011-12. The AO passed a draft order dated 25/03/2015 u/s 143(3) read with section 92CA(3) of the IT Act for arriving at a total income of Rs. 2,18,66,705/-. The AO made adjustment as proposed

by the TPO of Rs. 2,01,36,335/- towards adjustment of arm's length price. The AO also held that as per the proviso to sub-section (4) of section 92C, no deduction is allowable u/s 10A on the enhanced arms length price adjustment.

3. When the assessee filed objections before the DRP, the DRP vide its order dated 28/12/2015 has directed to exclude 7 comparable companies and to include one company for determining the Arms Length Price. The TPO accordingly recomputed the ALP and intimated that the adjusted mean margin is 23.22% and the same is within the (+/-) 5% of the comparables and hence stated that no adjustment is warranted in ALP. Accordingly, the adjustment of Rs. 2,01,36,335/- made in the draft assessment order is deleted.

4. Aggrieved by the order of DRP, the revenue is in appeal before us raising the following grounds of appeal:

"1. Whether on the facts and circumstances of the case, the Hon'ble DRP was justified in excluding Infosys BPO Ltd., on the grounds of high turnover which is contrary to Rule 10B(2), which prescribes compatibility of international transactions with uncontrolled transactions with reference to functions performed, asset employed and risk assumed.

2. Whether on the facts and circumstances of the case, the order of the Hon'ble DRP was correct in excluding companies on the ground of turnover and profit without appreciating the fact that (i) there is no linkage between the profits and turnover in service industry, (ii) no economic rationale backed with any statistical analysis was brought on record, (iii) in the business of ITES sector the operational size has no impact on profit margin when TNMM is the MAM and (iv) high or low turnover does no influence the margins of the comparables.

3. Whether on the facts and circumstances of the case, the Hon'ble DRP was correct to exclude Jeevan Scientific Technology Ltd. when both segments BPO and RPT fall under ITES.

4. Whether on the facts and circumstances of the case, the Hon'ble DRP was justified in including ICRA Online Limited only for the reason that TPO, Bengaluru has selected this company as comparable without appreciating the fact that the company fails RPT filter applied by the TPO.

5. Whether on the facts and circumstances of the case, the Hon'ble DRP was correct in directing the AO to exclude reimbursement of expenses for the computation of RPT, ignoring the fact that reimbursement is a recognized RPT transaction."

4.1 Basically, Revenue is in appeal objecting to exclusion Infosys BPO and Jeevan Scientific Technology Ltd. Also inclusion of ICRA Online Ltd. Ground No. 5 is general in nature.

5. Considered the rival submissions and perused the material on record. Ground Nos. 1 & 2 are squarely covered by the decision of the coordinate bench of this Tribunal in assessee's own case for AY 2010-11 in ITA No. 180/Hyd/2015 and 326/Hyd/2015 vide order dated 24/08/2016 wherein the coordinate bench held as under:

"5. As regards ground No. 1 regarding exclusion of comparables of three companies, the same are to be decided as under:

5.2 Infosys BPO Ltd., and TCS Eservice Ltd.,

i) The TPO added these companies as comparable which are functionally different besides being super turnover company, which is above Rs. 200 crores.

ii) The objections of the assessee are that the comparable company under TNMM should be similar to the tested company in functionally, size, employees skill sets, brand value and intangibles. As these three companies are different from the assessee company in terms of the turnover, brand value, intangibles and other assets employed, employee skill sets, and also the customers that it caters all over the world, these cannot be comparables for assessee company which renders low end BPO services as captive service provider to its AE company located in US on a cost plus model.

6. The DRP held as follows:

11.2 The taxpayer vehemently argued that the four companies should not be included in view of their brand value and high turnover as well as relying on the decision of the ITAT to exclude M/s. Infosys Technologies Ltd also argued that M/s Eclerx is KPO not comparable. The panel feels that only M/s Infosys SPO and TCS E serve Ltd should not be included as comparable in view of their advantageous brand value along with high turnover of 1000 crores and above. Similarly, M/s. Eclerx Services that also

to be excluded as it renders high end services and considered as KPO. However, the argument of the taxpayer with regard to the comparable company M/s. TCS Eserve International Ltd. is not acceptable, as the said company has passed all the filters and it is true comparable to the taxpayer company. Hence, the taxpayer's objection for exclusion of TCS Eserve international Ltd. is rejected and direct the TPO/AO to exclude the following comparables from the final set of comparables and recompute the Arm's length price.

- (i) eclerx Services Ltd.*
- (ii) TCS Eserve Ltd.*
- (iii) Infosys BPO Ltd.*

Accordingly the TPO/AO is directed to rework the ALP by excluding the above three companies from the ALP Adjustment.

7. Considered the submissions of both the parties and perused the material facts on record. The issue in dispute is squarely covered by the decisions of the ITAT including the decision in assessee's own case for AY 2007-08 vide order dated 25/04/2014 in ITA No. 1407/Hyd/2013 and for AY 2009-10 vide order dated 31/10/2014 in ITA No. 392/Hyd/2014 wherein the coordinate bench directed to exclude the said companies from the list of comparables and recompute the ALP accordingly. Therefore, we do not find any infirmity in the order of the DRP in directing the AO/TPO to exclude the said companies from the list of comparables considering their advantageous brand value along with high turnover. Accordingly, this ground of appeal of revenue is dismissed."

Following the said decision, we dismiss the ground Nos. 1 & 2 raised by the revenue.

8. As regards ground No. 3 regarding exclusion of Jeevan Scientific Technology Ltd. by the DRP, the submissions of the Assessee before the DRP was that the TPO ought to have computed the operating profits of this company based on the segment results exclusively available for BPO segment in the annual report, but, the TPO has taken both income from BPO and ERP segment which is software segment and being functionally different with that of assessee company. The DRP directed the AO to exclude the above company from the comparables by observing as under:

Having considered the submissions, it is noticed by us from the perusal of annual report that the foreign exchange earnings of Rs. 79.21 lakhs is only from BPO operations and there is no foreign exchange earning in respect of ERP segment. Therefore, the ERP segments cannot be considered as it does not have any revenue from the export. It is also noticed by us that the ERP segment is not otherwise comparable to the functions of the assessee company. The BPO segment, alone cannot be considered as comparable as the revenue to the total revenue ratio is only 32.28%. It is also noticed by us that there is a huge fluctuation in the margin of the company from F.Y. 2008-09 to 2012-13 viz., in BPO segment 15.66%, 18.22%, 6.24%, 14.42% and (-)56.89%, which indicate that certain peculiar circumstances influencing the profit margin of the company and the company fails the revenue earning filter of 75% applied by the TPO, in view of the above differences, we direct the A.O. to exclude the above company from the comparables.”

9. Considered the rival submissions and perused the material on record. We noticed that Jeeven Scientific Technology Ltd. has two segments and they have published their segmental results also. From the segmental results, it clearly shows that only BPO has foreign exchange earnings and there is no foreign exchange in ERP segment. Therefore, this segment cannot be considered for comparison with the assessee company. Moreover, the DRP also observed that there is huge fluctuations in the results of this company over the years. In our view, there is no infirmity in the findings of DRP. Therefore, we are inclined to dismiss the ground raised by the revenue.

10. With regard to ground Nos. 4 & 5, revenue objected for inclusion of the company ICRA Online Ltd. as comparable company. We noticed that the assessee has incurred related party transaction including reimbursement expenses/income which is to the extent of 28.04% as determined by TPO. The same was objected before DRP. The DRP excluded the reimbursement of expenses/income from the related party transactions by observing that such transactions do not have any influence on the margin of the company. By excluding the reimbursement expenses, the % age of related party transaction came down below 25% filter. Accordingly, they directed the TPO to include

the company ICRA Online Ltd. as one of the comparables. Revenue has raised ground Nos. 4 & 5 objecting to above directions of DRP.

11. Considered the rival submissions and perused the material on record. We noticed that assessee has incurred related party transaction with its AE and it is in the nature of international transaction. Even though it has no impact on the margin of the company, but, it is international transaction and to determine the quantum of transaction with its Associates, we have to accumulate all the transactions with the related party transaction and not confined to the transactions which will have impact on the margin. We are not dealing with the ALP but we are determining the extent of related party transaction with its Associates and this information is used to apply filter. At this stage, we have to consider all the transactions with its Associates, which may include reimbursement of expenses/income. Therefore, in our considered view, we cannot exclude reimbursement of expenses to apply the filters. Hence, we are not in agreement with the findings of DRP and we direct the TPO to exclude the company ICRA Online Ltd. as comparables as it failed the RPT filter. Accordingly, we allow the ground nos. 4 & 5 by revenue.

12. In the result, appeal of the revenue is partly allowed.

Pronounced in the open court on 9th November, 2018.

Sd/-
(P. MADHAVI DEVI)
JUDICIAL MEMBER

Sd/-
(S. RIFAUH RAHMAN)
ACCOUNTANT MEMBER

Hyderabad, Dated: 9th November, 2018

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Copy to:-

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- 3) *DRP, Hyderabad*
4. *CIT, (International Taxation & TP), Income Tax Towers, 10-2-3, AC Guards, Hyderabad – 500 004.*
- 5) *The Departmental Representative, I.T.A.T., Hyderabad.*