

IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH : I-2 : NEW DELHI

BEFORE SHRI R.K. PANDA, ACCOUNTANT MEMBER
AND
SHRI SUCHITRA KAMBLE, JUDICIAL MEMBER

ITA No.1333/Del/2015
Assessment Year: 2010-11

Knowledge Platform India Pvt. Ltd.,
C/o Ravi Gupta, Advocate,
E-6A, Kailash Colony,
New Delhi.

Vs. DCIT,
Circle-14(2),
New Delhi.

PAN: AACCK1186E

(Appellant)

(Respondent)

Assessee by	:	Shri P.C. Yadav, Advocate
Revenue by	:	Shri Rakesh Kumar, Sr. DR
Date of Hearing	:	10.01.2019
Date of Pronouncement	:	29.01.2019

ORDER

PER R.K. PANDA, AM:

This appeal filed by the assessee is directed against the order dated 21.11.2014 passed by the DRP-14, New Delhi, relating to assessment year 2010-11.

2. Ground Nos.1,4 and 5 being general in nature are dismissed.
3. Ground of appeal No.3 by the assessee reads as under:-

“3. That the Ld.A.O/DRP has erred on facts and in law in making the addition of Rs.10,470 by invoking the provisions of section 14A of the Income Tax Act, 1961.”

4. The ld. counsel for the assessee, at the time of hearing, did not press this ground due to smallness of the amount for which the ld. DR has no objection. Accordingly, ground of appeal No.3 is dismissed as not pressed.

5. Ground of appeal Nos.2.1 to 2.5 by the assessee read as under:-

“2.1 That the Hon'ble Members of the DRP have erred on facts and in law in holding that the TPO was correct in the selection of comparables and in upholding the adjustments of Rs.88,04,775 u/s 92CA of the Income Tax Act, 1961.

2.2 That the Hon'ble Members of the DRP have erred on facts and in law in holding that the comparables used by the TPO are correct.

2.3 That the Ld. Assessing Officer has erred on facts and in law in making an addition of Rs.88,04,775/- on the basis of the order passed by TPO.

2.4. That the Ld. Assessing Officer/TPO/DRP has erred on facts and in law in not appreciating that the appellant is “non-risk bearing entity which does the facilitating functions” and in categorizing the appellant as software developer.

2.5 That the Ld. TPO has erred on facts and in law in observing that the appellant has used comparable data for more than previous two years and has arrived at the ALP on the basis of irrelevant considerations.”

6. Facts of the case, in brief, are that the assessee is a company engaged in providing customized e-learning modules and IT enabled services to its parent company at Singapore. The assessee filed its return of income on 24th September, 2010 declaring income of Rs.30,86,800/-. Since the assessee had undertaken international transactions with its AE, a reference u/s 92CA(1) was made by the Assessing Officer to the TPO for determination of the ALP of the international

transaction. The TPO, during the course of TP assessment proceedings noted that the assessee is a wholly owned subsidiary of Pacific Knowledge Platform Pte Ltd. providing e-module learning software services to Knowledge Platform Singapore. He observed that the assessee during the impugned assessment year has undertaken the following international transactions:-

1.	Developing E-Learning modules and related work	6,69,27,856
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7. He observed that the main international transaction of the assessee is the provision of software development services. The assessee has applied TNMM as the most appropriate method and the OP/TC ratio is taken as the profit level indicator in the TNMM analysis. The PLI of the company is arrived at 10.1% on cost whereas the average PLI of the six comparables as per fresh search executed by the assessee was at 8.5%. It was accordingly stated that the price charged in its international transaction being more than the arithmetical mean of the comparables, the price charged is at arm's length.

8. However, the TPO did not accept the contention of the assessee. The TPO made fresh search of the comparables by applying new filters such as (1) companies whose data is not available for the financial year 2009-10 (2) companies whose software development income is less than Rs.5 crores; (3) companies whose revenue from services is less than 75% of the total operating revenues; (4) companies who have export sales less than 75% of the sales from software development services; (5) companies having more than 25% RPT; (6) companies who have persistent loss for the

last three years upto and including financial year 2009-10; (7) companies whose employee cost is less than 25% of the Operating cost; (8) companies having different financial years i.e., not March 31, 2010; (9) companies that are functionally different from the tax payer; and (10) companies that are having peculiar economic circumstances. He also proposed to use only the current year data i.e., data pertaining to F.Y. 2009-10. Based on the above filters, the TPO finally selected 22 comparables whose average was 22.08% and proposed an upward adjustment of Rs.72,70,603/- u/s 92CA(2) of the IT Act. The TPO accordingly confronted the assessee as to why the above addition should not be made.

9. The assessee filed reply challenging the selection of the comparables selected by the TPO. The request of the assessee to add certain comparables having turn over of less than Rs.5 crores was rejected by the TPO on the ground that these are very small companies and the margin earned by these companies fluctuate to extremes because of the narrow base. Further, according to him, the reliability of the data in respect of the small companies is also not always very high. Their contribution towards overall turnover of the industry is negligible and, therefore, more often they escape from the eyes of the regulators. Further, the small companies lack competitive strength, lack operational efficiencies and also lack human resources. According to the TPO, the reliability of the financial data for companies with low levels of sales/operating income can be significantly reduced because the same persons are often both major shareholders and also the key employees, thereby obliterating the

economic distinction between profits and salaries. Relying on various decisions, the TPO rejected the argument of the assessee to add certain companies whose turnover was less than Rs.5 crore. Similarly, he also rejected the argument of the assessee challenging the selection of certain companies with abnormal margins/super normal profits. After considering the various arguments of the assessee challenging the various filters adopted by the TPO, the TPO finally selected the following 23 companies whose average margin is 21.97%:-

Sl.No.	Name of the Company	OP/OC Without Forex
1.	Accelya Kale Solutions Ltd.	13.65%
2.	Akshay Software Technologies Ltd.	-1.07%
3.	Allgo Embedded	9.67%
4.	CTIL Ltd.	18.11%
5.	E-Infochips Bangalore Ltd.	71.38%
6.	Evoke Tech	18.56%
7.	E-Zest Solutions	18.66%
8.	Infinite Data System Private Limited	88.25%
9.	Kuliza Technologies Private Limited	15.50%
10.	Larsen & Toubro Infotech Ltd.	19.06%
11.	Mindtree Ltd. (Segment)	13.92%
12.	Persistent Systems Limited	29.02%
13.	Persistent Systems & Solutions Limited	11.37%
14.	Quintegra Solutions Ltd.	-8.20%
15.	R S Software (India) Ltd.	10.18%
16.	Sankhya Infotech	18.11%
17.	Sasken Communication Technologies Ltd.	17.54%
18.	Sonata Software	35.87%
19.	Tata Elxsi (Segment)	20.29%
20.	Thinksoft Global Services Ltd.	17.35%
21.	Thirdware Solutions Limited	33.43%
22.	Zylog Systems Limited	25.07%
23.	Logix Microsys	9.52%
	Average	21.97%

10. The TPO accordingly proposed an upward adjustment of Rs.88,04,775/- towards arm's length price of the international transaction undertaken by the assessee. The Assessing Officer in the proposed order made the above addition. The assessee approached the DRP, but, without any success. Aggrieved with such order of the DRP, the assessee is in appeal before the Tribunal.

11. The ld. counsel for the assessee has also filed an additional ground which reads as under:-

“On the facts and circumstances of the case the Draft assessment order as affirmed by the DRP, is bad in law and *void ab initio*, as the impugned year of assessment has been selected by the A.O. in utter disregard of the guidelines of the CBDT, which guidelines clearly provides that cases where international value of international transaction exceeds Rs.15 Crore, would only be selected via manual instructions.”

12. The ld. counsel for the assessee submitted that the additional ground filed by the assessee is purely a legal ground and does not require any fresh facts to be investigated. Relying on various decisions including the decision of Hon'ble Supreme Court in the case of *CIT vs. Varas International reported in 284 ITR 80 (SC)*; *National Thermal Power Corporation Ltd. vs. CIT reported in 229 ITR 383 (SC)*; and the decision of the Special Bench of the Tribunal in the case of *DHL Operators reported in 108 TTJ 152 (SB)*, he submitted that the additional ground raised by the assessee should be admitted.

12.1 After hearing both the sides and considering the fact that the additional ground raised by the assessee is purely a legal one, the same is admitted for adjudication.

13. Before adjudicating the additional ground, we would first like to decide the appeal on merit. The Id. counsel for the assessee submitted that the assessee is basically challenging the addition of Rs.88,04,775/- on the ground that the TPO has erred in holding that the assessee is providing software development services and by holding so, the TPO has erred in selecting six comparables whose functions are different from that of the assessee. Further, the selection of comparables on the basis of their turnover, risk and export sales is not correct since these cannot be compared with that of the assessee and, therefore, by applying these filters, they should have been excluded by the TPO from the list of comparables. The Id. counsel for the assessee, referring to the order of the TPO submitted that the TPO has made an allegation that the assessee himself has contended not to apply the turnover filter. However, this is factually incorrect and wrong since the assessee has never contended to the applicability of this filter. It was pointed out to the TPO that the assessee being a small company, therefore, companies having turnover of Rs.5 crore or less than Rs.5 crores should also be included in the list of comparables. For the above proposition, the Id. counsel for the assessee drew the attention of the Bench to page 160 of the paper book where vide clause No.c, the assessee has made objection to the turnover filter adopted by the TPO. The Id. counsel for the assessee submitted that the following nine companies which are engaged in software development cannot be considered as comparable whose turnover is more than Rs.100 crore as against the turnover of the assessee at Rs.6.69 crore:-

Sl.No.	Name of the company
1.	Accelya Kale Solu.
2.	L& T Infotech
3.	Mindtree
4.	Persistent Systems
5.	R.S. Software
6.	Sasken Software
7.	Sonata Software
8.	Tata Eleksi
9.	Zylog Systems Ltd.

14. Relying on the following decisions, he submitted that the companies having huge turnover cannot be taken as comparables:-

- a. CIT vs. New River Software Solutions, 85 Taxman.com 302 (Del);
- b. Witness System Software India Pvt. Ltd. vs. DCIT, 34 Taxman.com 183 (Bangalore Trib.); and
- c. CIT vs. Aginity India Technologies Pvt. Ltd. 36 taxmann.com 289 (Del).

15. He further submitted that the international transaction of the assessee is a low risk selling as the assessee has only made sales to its AE and not to any outsider. Therefore, the companies having high risk selling cannot be compared with the assessee and, therefore, the TPO has erred in excluding the companies having export sales below 75%.

16. He submitted that out of the 23 comparables chosen by the TPO, 21 companies are engaged in the software development segment which line is completely

different from e-learning. Relying on various decisions, he submitted that e-learning is IT enabled services and cannot be held as software development service. The ld. counsel for the assessee submitted that the following six comparables are also not comparables because of the criteria laid down by the TPO himself:-

- a. Infinite data- Abnormally huge sales and Profit before Tax in comparison to 2009 (137 of PB). A perusal of the submissions vis-a-vis distinction made by the assessee would prove beyond doubt that this Company is full fledge risk bearing whereas assessee is captive service provider dealing only with its AE and hence both cannot be compared.
- b. E-Zest Solutions - No export sales during the year- Detailed submission as per page No-136 of PB.
- c. Thirdware solutions. It has diversified income sources and high risk bearing company (Page No-155).
- d. CTIL- Technical Education sector and not e-learning services. Further it is high risk bearing company and hence not comparable with assessee (Page132 of PB).
- e. E-info chips-Extraordinary profits (page134 of PB) Huge fixed assets whereas assessee has no fixed asset, further high risk bearing company-
- f. Sankhaya Infotech- less than 25% related party transactions (Page-146 of PB)

17. He accordingly submitted that these comparables should also be excluded. He submitted that once the above 15 companies (i.e., nine companies on account of turnover and six comparables on account of distinctive features) are excluded, then, the PLI of the remaining seven comparables comes to 10.06% whereas the PLI of the assessee is at 10.1% which is within the +/- 5% ratio. Therefore, no addition is called for. He, accordingly submitted that the order of the DRP sustaining the adjustment made by the TPO/Assessing Officer should be deleted.

18. The Id. DR, on the other hand, heavily relied on the order of the Assessing Officer/TPO/DRP.

19. We have considered the rival argument made by both the sides and perused the orders of the authorities below. We have also considered the various decisions cited before us. We find the assessee, in the instant case, is engaged in providing customized e-learning modules and IT enabled service to its parent company at Singapore. The assessee during the year under consideration has entered into an international transaction amounting to Rs.6,69,27,856/- the details of which have already been given in the preceding paragraphs. We find the TPO, after considering the various arguments advanced by the assessee selected 23 comparables whose average margin was calculated at 29.97%. Based on the average margin of the comparables, the TPO had proposed an upward adjustment of Rs.88,04,775/- which was adopted by the Assessing Officer in the proposed order and upheld by the DRP. Accordingly, the addition of Rs.88,04,775/- has been made being the ALP of the international transaction entered into by the assessee. It is the submission of the Id. counsel for the assessee that out of 23 comparables selected by the Assessing Officer/TPO, nine comparables the details of which are given at para 13 should be excluded because of their turnover exceeding more than Rs.100 crores. It is his argument that when the TPO has excluded the companies having turnover of Rs.5 crores or less, then, the TPO should not have selected comparables whose turnover is more than Rs.100 crores. Similarly, it is also the argument of the Id. counsel for the

assessee that the six comparables (the details of which are given at para 16) are also to be excluded on the basis of their distinctive features and FAR Analysis. Thus, according to him, if the 15 companies are excluded, then, the margin of the remaining eight comparables will be 10.06% as against 10.1% declared by the assessee and will fall within +/- 5% ratio and, therefore, no adjustment is required.

20. We find some force in the argument of the Id. counsel for the assessee. It is an admitted fact that the assessee, during the TP assessment proceedings, has requested the TPO to select certain comparables whose turnover is Rs.5 crore or less. However, we find from the order of the TPO that he rejected the argument of the assessee on the ground that companies having turnover of less than Rs.5 crores have to be excluded because the margin earned by these companies fluctuate to extremes because of narrow base and reliability of the data in respect of these companies is also not always very high. According to him, the contribution of such companies towards overall turnover of the industry is negligible for which they escaped the eyes of the regulator. Further, they lack competitive strength, lack operational efficiencies and also lack human resources. It is also his opinion that the reliability of the financial data for companies with low levels of sales/operating income can be significantly reduced because the same persons are often major shareholders and also key employees thereby obliterating the economic distinction between profits and salaries. We do not find any merit in the approach of the TPO rejecting the claim of the assessee to select certain comparables with turnover of less than Rs.5 crores when the turnover of the

assessee is only 6.68 crores during the year. In our opinion, if the TPO has rejected certain companies from the list of comparables on the basis of low turnover, then by adopting the same criteria he should have excluded at least the companies whose turnover is more than Rs.100 crores. We find from the list that even certain companies are having turnover of more than Rs.1000 crores. Further, the assessee in the instant case is a captive service provider and working exclusively for the AE and its entire export sale is to the AE. However, in the instant case, the above nine companies whose details have been given in the preceding paragraphs are not captive service providers and they are not working exclusively for the AE and their entire sales is not to the AE. Even otherwise also these companies cannot be considered as comparable with that of the assessee company due to the following FAR analysis:-

1) Accelya Kale Solutions Ltd. is engaged in software package and service as available in public domain whereas assessee is in e-learning modules and content writing. It has incurred huge R&D expenditure whereas assessee has not incurred any such expenditure. Further, the above comparable is a full risk bearing company whereas assessee is a captive service provider to its AE with zero risk. Therefore, this company cannot be considered as comparable.

2) L&T Infotech: This company is functionally different being in ITES, software development and engineering whereas assessee is in e-learning modules. It has a huge asset base of Rs.1028 crores whereas assessee has assets of Rs.2.29 crore only. It has incurred huge advertisement expenditure of Rs.2.24 crore as

against nil by the assessee. Apart from this it is a full risk bearing company whereas assessee is a zero risk bearing company being captive service provider to its AE. Therefore, this company cannot be considered as comparable.

3) Mindtree Ltd.: This company is again functionally different being in ITES and has diversified business activity. Although the TPO has taken segmental revenue, however, allocation of assets has not been considered. Further, it has huge asset base of Rs.649 crores as against Rs.2.29 crores in case of the assessee. It has huge geographical market such as USA, Europe and India and few other countries whereas assessee has only Singapore. Further, it has acquired a big company namely Aztec Soft Ltd., a listed company which has contributed to its revenue. Thus, extraordinary event has taken place. Therefore, this company in our opinion cannot be considered as a comparable.

4) Persistent Systems Ltd.: This company is functionally different being in product engineering, technology consulting and IP-led business. It has incurred Rs.52 crores in R&D expenses and has assets of Rs.642.36 crores. Therefore, this cannot be compared with that of the assessee company.

5) R.S. Software (India) Ltd.: This company being in e-payments software company which is high end futuristic business is functionally different from the assessee. Further, it has asset of Rs.32 crores as against Rs.2.29 crores in case of the assessee. Therefore, this company cannot be retained as comparable.

6) Sasken Communication Technologies Ltd.: This company again is a high end company making satellite phones and is functionally unrelated with the assessee. It has many subsidiaries. It has huge assets of Rs.483 crores including 36 patents and 31 are under grant. Its geographical area covers UK, USA and other big countries. Therefore, this company in our opinion cannot be compared with that of the assessee.

7) Sonata Software: This company has three large subsidiaries including one in Germany and is one of the top ten players in R&D. It has asset base of Rs.292 crores and is one of the top 20 IT firms in India. Therefore, this company in our opinion cannot be compared.

8) Tata Eleksi (Segment): This company is a specialized embedded software development company and is in complex segment which cannot be compared with that of the assessee company. It has incurred huge R & D expenditure which is 3% of its total turnover. It has assets of Rs.208 crores and has incurred advertisement expenses of about Rs.3 crores. Therefore, this in our opinion cannot be considered as a comparable with that of the assessee company.

9) Zylog Systems Ltd.: This company again is a high end full risk bearing company and has eight subsidiaries. It has acquired a number of companies during the year as per report of the directors and has a huge asset base of Rs.785.60 crores. It has spent Rs.13.91 crores on marketing and selling expenses and Rs.46 crores towards sales commission. Its geographical market consists of

80 countries. Therefore, this company in our opinion cannot be considered as a comparable.

20.1 In view of the above discussion, we find merit in the argument of the Id. counsel for the assessee that the above nine comparables should be excluded. We, accordingly direct the A.O./TPO to exclude the above nine comparables.

21. Now, coming to the six comparables as argued by the assessee is concerned, we find from page 137 of the paper book that the assessee pointed out the differences between Infinite Data System Pvt. Ltd. and the assessee. In the case of Infinite Data System, the company earns its revenue from technical support. A perusal of the details filed shows this company has revenue from infrastructure management services. The company has entered into with customers on time and material basis. Further, it is a full-fledged risk bearing company earning from non-AEs, thus, enjoys more revenue and is in a position to dominate the terms of services. It is also seen from the submission before the TPO that in 2009, the company had turnover of around Rs.4 crores and it ran into loss before that. However, due to some super activities, the turnover jumped to more than 900% in the relevant year. Further Infinite Data Systems Pvt. Ltd. is located in Japan whereas Knowledge India is based at Singapore. We, therefore, find merit in the argument of the Id. counsel for the assessee that this company should not be treated as a comparable and has to be excluded from the list of comparables. We find the Hon'ble Delhi High Court in the case of *CIT vs. Agnity India Technologies (P) Ltd.*, 36 taxmann.com 289 (Del) under similar circumstances

has rejected this company as a comparable. Therefore, this company is directed to be excluded from the list of comparables.

22. So far as E-Zest Solutions is concerned, we find from page 136 of the paper book that this company is in software development and sale of software also. As per the annual report of the company, it has special expertise in emerging technologies such as cloud, SAS and business intelligence, etc. Therefore, this company is functionally different from that of the assessee company. Further, there is existence of stock whereas in the case of the assessee company, there is no such stock. Further, this company is into software development whereas Knowledge India is engaged in preparation of e-learning modules. We, therefore, find merit in the argument of the Id. counsel for the assessee that this company should be excluded from the list of comparables. For the above proposition, we find support from the decision of the Hyderabad Bench of the Tribunal in the case of *Intoto software India (P) Ltd Vs. ACIT* vide ITA Nos.1196 & 1197/Hyd/2010 and batch of other appeals, order dated 24th May, 2013.

23. So far as Thirdware Solutions is concerned, we find this company has diversified income source and high risk bearing company. A perusal of page 155 of the paper book shows that this company is engaged in implementation and customer service which include training, customized development and help desk services for ERP Software and distribution of software products of the company Quad Inc and Hyperion solutions Corporation. Further, it has assets of Rs.66.15 crores whereas the

assessee has assets of only Rs.2.29 crores. Thirdware solutions is a high risk bearing company whereas the assessee is a low risk company since the sales are to the AE only. We, therefore, find merit in the argument of the ld. counsel for the assessee that this company should be excluded from the list of comparables. We accordingly direct the TPO/A.O. to exclude this company from the list of comparables.

24. So far as CTIL Ltd. is concerned, we find this company is into technical/vocational higher education which is normally different from the case of the assessee. Further, as per the notes to accounts of the company, the revenue consisted of software development and from sale, etc. and the company had shown 166% growth in revenue and 126% in net profit due to acquisition of many subsidiaries. Thus, extraordinary events have taken place during the year which is not there in the case of the assessee. Further, this is high risk bearing company whereas the assessee is a low risk bearing company which is limited to the agreement with the parent company. Further, CTIL Ltd. has incurred huge amount towards R&D expenditure and it has large-scale of operations including seven subsidiaries whereas the assessee has not incurred any R&D expenditure and has no subsidiaries at all. We, therefore, find merit in the argument of the ld. counsel for the assessee that this company should be excluded from the list of comparables.

25. So far as e-Infochips is concerned, a perusal of page 134 of the paper book shows that this is a high risk bearing company whereas the assessee is a low risk bearing company. It owns assets such as land, building, etc. and thereby saves rental

cost whereas the assessee has no such assets. Further, the TPO, while calculating the operating profits of e-Infochips Bangalore Ltd., has included the dividend income/interest income and has also considered the expenses incurred to earn such income. However, in the case of the assessee, the Assessing Officer, while computing the profit of Knowledge India removes both these factors. Since e-Infochips is a high risk bearing company, therefore, the same cannot be compared with the profitability of the assessee company which is a low risk bearing company. Further, the geographical market is different from that of the assessee company. We, therefore, direct the Assessing Officer/TPO to exclude this company from the list of comparables.

26. So far as the Sankhya Infotech is concerned, it is also the submission of the ld. counsel for the assessee that Sankhya Infotech has less than 25% of RPT transaction. However, it is not discernible from the details given by the assessee regarding RPT of Sankhya Infotech. In our opinion, in absence of any distinguishable features brought to our notice, this company has to be retained as a comparable. Therefore, we uphold the order of the A.O./TPO/DRP in retaining this company as a comparable. Once the 14 comparables are excluded from the list of comparables taken by the Assessing Officer in the final order, the PLI of the comparables will be within +/- 5% and accordingly no TP adjustment is called for. The grounds raised by the assessee are accordingly disposed of. Since the assessee succeeds on merit, the additional ground is not being adjudicated being academic in nature.

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

The decision was pronounced in the open court on 29.01.2019.

Sd/-

(SUCHITRA KAMBLE)
JUDICIAL MEMBER

Dated: 29th January, 2019

dk

Copy forwarded to

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR

Sd/-

(R.K. PANDA)
ACCOUNTANT MEMFBER

Asstt. Registrar, ITAT, New Delhi