

**IN THE INCOME TAX APPELLATE TRIBUNAL
'A' BENCH, BENGALURU**

**BEFORE SHRI B.R. BASKARAN, ACCOUNTANT MEMBER
and
SHRI PAVAN KUMAR GADALE, JUDICIAL MEMBER**

IT(TP)A No.685/Bang/2015
(Assessment year: 2010-11)

M/s. Force 10 Networks India Pvt. Ltd.
(merged with Dell International Services
India Pvt. Ltd.,)
'Divyashree Greens III Floor, Survey
No.12/1, 12/2A, Challaghatta Village,
Varthur Hobli,
Bengaluru-560 071. ... Appellant
PAN:AAACF 8609 B

Vs.

Deputy Commissioner of Income-tax,
Circle 3(1)(1),
Bengaluru. ... Respondent

Appellant by : Shri K.R.Vasudevan, Advocate.
Respondent by : Shri C.H.Sundar Rao, CIT(DR)

Date of hearing: 23/04/2019
Date of pronouncement: 15/05/2019

O R D E R

Per PAVAN KUMAR GADALE, JM :

The assessee has filed the appeal against the assessment order u/s 143(3) r.w.s. 144C dated 20/02/2015 passed in pursuance to the directions of the Dispute Resolution Panel (DRP) dated 18/12/2014.

2. The assessee has raised the following grounds of appeal:

1. Transfer Pricing

1. The learned Deputy Commissioner of Income Tax (Transfer Pricing-IV), Bangalore ("Transfer Pricing Officer" or "learned TPO") grossly erred in determining an adjustment u/s 92CA of the Income-tax Act, 1961 to the Arm's Length Price ('ALP') of the international transaction entered into by the Appellant with its Associated Enterprises ("AEs") with respect to the Information Technology enabled Services ("ITeS").
2. The Appellant aggrieved by the learned TPO Order further appealed before the Dispute Resolution Panel ("DRP") against the TPO order and subsequently, the learned Assessing Officer ("learned AO") issued the final assessment order with a Transfer Pricing ("TP") adjustment of INR 2,18,00,000/-.
3. The learned AO/learned TPO erred in rejecting the TP documentation maintained by the Appellant by invoking provisions of sub-section (3) of 92C of the Act contending that the information or data used in the computation of the ALP is not reliable or correct. The learned AO/ learned TPO has grossly erred therefore in
 - 3.a rejecting comparability analysis carried in the TP documentation and in conducting a fresh comparability analysis by introducing various filters in determining the ALP.
 - 3.b rejecting companies that are functionally comparable to the Appellant while performing the comparability analysis. Specifically, the following companies ought to have been included as comparable:
 - Crazy Infotech Limited
 - 3.c including companies that do not satisfy the test of comparability. Specifically, the following companies selected as functionally comparable by the learned AO / learned TPO ought to have been rejected:
 - Kals Information Systems Limited
 - ICRA Techno Analytics Limited
 - Taksheel Solutions Limited
 - FCS Software Solutions Limited
 - SPRY Resources India Private Limited
4. The learned AO / learned TPO erred in not considering the multiple year / prior year financial data of comparable companies while determining the ALP.
5. The learned AO / learned TPO erred in application of different financial year ending filter.
6. The learned AO / learned TPO erred in using data as at the time of assessment proceedings, instead of that available as on the date of preparing the TP documentation for comparable

companies while determining ALP.

7. The learned AO / learned TPO erred in application of employee cost filter of 25%.
8. The learned AO / learned TPO, while giving working capital adjustment, erred in computing the same adjustment.
9. The learned AO / learned TPO erred in not considering the provision for bad and doubtful debts as operating in nature.
10. The learned AO / learned TPO erred in ignoring the limited risk nature of the contractual services provided by the Appellant and in not providing an appropriate adjustment towards the risk differential. even when the full-fledged entrepreneurial companies are selected as comparable companies.

II. Corporate Tax

- 1. Re-computation of deduction under section 10A of the Act.**
The learned AO has erred in re-computing the deduction under Section 10A by reducing travelling expenditure in foreign currency from both export turnover and total turnover of the undertaking without appreciating that the same is not specifically incurred for providing technical services outside India.
- 2. Short credit of Tax Deducted at Source**
The learned AO has erred in granting credit for TDS of Rs.1,140 instead of Rs.16,691 claimed by the Company.
- 3. Interest under section 234A of the Act**
The learned AO has erred in levying interest under section 234A of the Act amounting to Rs.43,957 without considering the fact that the Appellant had filed its return within the extended due date.
- 4. Interest under section 234B of the Act**
The levy of interest under section 234B of the Act is consequential in nature.

The appellant craves leave to add, alter, rescind and modify the grounds provided herein above or produce further documents, facts and evidence before or during the course of hearing of this appeal.

For the above and any other grounds which may be raised at the time of hearing, it is prayed that necessary relief may be provided."1

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3. The grounds of appeal No.1, 2 and 3(a) are general in nature and do not require adjudication. Ground No.3(b) and (c) is the prayer for inclusion and exclusion of comparables and ground Nos.4 to 10 are general and consequential. In the corporate grounds, the learned AR has not pressed the ground Nos.1 and 2 and whereas ground Nos.3 and 4 in regard to levy of interest u/s 234A and 234B are consequential.

4. Brief facts of the case are that the assessee is a company engaged in the business of providing support services like software testing, software enhancements, Bug fixing, Bug testing, debugging and other internet-based applications for networking equipments like switches and routers for high performance cluster computing the projects. The assessee has filed the Return of income electronically on 11/10/2010 with total income of Rs.8,22,500/- under normal provisions of the of the Income-tax Act,1961 ['the Act' for short] and book profits of Rs.1,70,28,286/- under the provisions of section 115JB of the Act. The Return of income was processed u/s 143(1) of the Income-tax Act,1961 ['the Act' for short]. The assessee has international transactions with its Associated Enterprises (AE) as under:

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Sl. No.	Description of the transaction	Amount (in Rs.)
1	Provision of software development services	19,15,66,438
2	Provision of marketing support services	67,78,145
3	Reimbursement of directors remuneration received	2,00,000
4	Reimbursement of expenses paid	30,64,849
	Total	20,16,09,432

5. On reference to the Transfer Pricing Officer (TPO), the TPO dealt on the profile of the company and functions performed by the assessee. The assessee has entered into international transactions with its AE and has adopted TNMM as the Most Appropriate Method (MAM) for its IT enabled services and the assessee-company adopted operating profit to operating cost (OP/OC) as profit level indicator for the transferring pricing study. The assessee-company earned margin of 9.47% for software development services and has selected 16 comparables with specific criteria and filter referred at page 7.2 of the TPO's order. The TPO has analyzed the comparables selected by the assessee-company at para.7.4 and applied the filters. The TPO rejected the assessee's transfer pricing study and applied filters referred at para.8 of the order as under:

1	All Industries - Services - IT
2	Financials not available
3	Sales above 1 crore to 200 crore
4	(Trading+rental)/Sales)*100<30% selected
5	Consecutive losses were rejected
6	RPT is more than 25% were rejected

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7	Export turnover above 75% are selected
8	Functionally dissimilar

The TPO has considered 20 comparable companies and the arithmetic average of operating profit margin is computed at 25.46%. The TPO made analysis and gave reasons for rejecting the transfer pricing documents:

Sl.no	Name of the comp company	Margin (%)
1	Manipal Digital Systems Pvt. Ltd.	22.05
2	KALS Information system Ltd	36.25
3	Spry Resources India Pvt Ltd	33.01
4	ICRA Techno Analytics Ltd	28.89
5	CTIL(Comp-U-LearnTech India Ltd)	16.94
6	Taksheel Solutions Ltd	41.92
7	Thinksoft Global Services Ltd	17.27
8	Nucleus Software Exports Ltd	20.59
9	R.S.Software (India) Ltd	10.59
10	FCS Software solutions Ltd	49.12
11	Accelya Kale Consultants Ltd	21.11
12	Tecnotree Convergence Ltd	33.39
13	Virinchi Tech Ltd	21.13
14	Persistent Systems Ltd.	15.40
15	Exensis Software Solutions Ltd	31.99
16	Penta Media Graphics Ltd	39.72
17	First Object Technologies Ltd.	21.91
18	Tanla Solutions Ltd.	14.05
19	Aftek Limited	30.26
20	Teledata Marine Solutions Ltd.	18.79
	Average	25.46

and after test checking selected 9 comparables and the average arithmetic mean being at 25.90% as under:

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Sl.no	Name of the comp company	Margin(%)
1	Akshay Software Tech Ltd	(-)0.91
2	KALS Information system Ltd	36.25
3	Spry Resources India Pvt Ltd	33.01
4	ICRA Techno Analytics Ltd	28.89
5	CTIL(Comp-U-Learn Tech India Ltd)	16.94
6	Taksheel Solutions Ltd	41.92
7	Thinksoft Global Services Ltd	17.27
8	R.S.Software (India) Ltd	10.59
9	FCS Software solutions Ltd	49.12
	Average	25.90

The TPO dealt on the usage of multiple year data and computed the average profit margin of the comparables in respect of software development services and gave the working capital adjustment and determined the arm's length price (ALP) with adjustment of Rs.2.18 crores which is as under:

ALP Calculation:

Value of transaction with AE = 19.16 cr.

Margin of the assessee company = 13.04%

Margin of the comparable companies = 25.90%

If

Cost	Markup (%)	Sale
100	13.04	113.04
100	25.90	125.90

ALP of the Transaction = $19.16 \times 125.90 / 113.04 = 21.34$ Cr.

+ 5% range = Rs.22.40 cr. come to Rs.20.27 cr.

Adjustment required = Rs.2.18 crore

The TPO passed the order u/s 92CA(3) dated 7/1/2014. The AO passed the draft assessment order with transfer pricing adjustments and other additions u/s 10A and assessed the

income at Rs.2,27,91,617/- vide order u/s 143(3) r.w.s. 92CA and 144C dated 23/1/2014.

6. Aggrieved by the draft assessment order, the assessee filed objections before the Dispute Redressal Panel (DRP) the DRP upheld the validity and reference to the TPO and passed order on 18/12/2014. The AO passed the final assessment order u/s 143(3) r.w.s. 144C dated 20/02/2015.

7. Aggrieved by the order, the assessee has filed an appeal before the Tribunal. At the time of hearing, learned AR submitted that the comparable M/s.Crazy Infotech Ltd., selected by the assessee but was excluded by the TPO as it is engaged in hardware and training. Whereas the learned AR relied on the Annual Report at page 255 of the paper book where segmental information is provided with computer hardware and software development and IT training and segmental results are available. Whereas the learned DR emphasized that the TPO has excluded for valid reasons and there is a negative segmental results and engaged in software development and the learned AR prayed for inclusion of this company.

8. The learned AR further submitted for exclusion of KALS Information Systems Ltd. because it is functionally different predominantly a product company and segmental information

is not available. The learned AR supported his stand relying on the Tribunal decision in the case of *Sella Synergy India Pvt. Ltd.* vs. DCIT(2016) 75 taxmann.com 286 (Chennai – Trib).

8.1 Similarly, the learned AR also prayed for exclusion of ICRA Techno Analytics Ltd., as it is functionally different and provides diversified services and segmental data break-up is not available and relied on the Tribunal decision in *Sella Synergy India Pvt. Ltd.*(supra).

8.2 The learned AR argued for exclusion of comparable company M/s.Taksheel Solutions Ltd., The company provides diversified services without segmental break-up and fails employee cost filter and relied on ITAT decision in *DCIT vs. Wabco TVS Ltd.* in ITA No.883/Mds/2015 & CO No.51/Mds/2015.

8.3 The learned AR prayed that FCS Software Solutions Ltd., is functionally different and diversified without segmental break-up and referred to Annual Report and relied on the decision of *Tibco Software India Pvt. Ltd.* vs. DCIT in iT(TP)A No.276 & 334/Pune/2015 where segmental details are available.

8.4 Finally, learned AR prayed that Spry Resources India Pvt.Ltd., is functionally different and is engaged in diversified

services and segmental data is not available as against low-end services of the assessee and relied on *Sella Synergy India Pvt. Ltd.* (supra) for exclusion.

9. Contra, the learned DR argued that Crazy Infotech Ltd., cannot be included and referred to Annual Report placed at page 251 of the paper book where export turn over is nil whereas 75% of the revenue is from other operations and prayed for not including this company. In respect of inclusion of comparables KALS Information Systems Ltd., the learned DR referred to page 251 and it is functionally different. Similarly, ICRA Techno Analytics Ltd., has web business and it tallies with assessee's functional profile and has to be included. In respect of Taksheel Solutions, the operating expenses are on higher side and it has to be examined in comparison with assessee's product. Similarly, learned DR vehemently argued that TPO has correctly excluded FCS Software (India) Ltd., and Spry Resources India Ltd., from the list of comparables and prayed for dismissing of the assessee's appeal.

10. We heard the rival submissions and perused material on record. Prima facie, in respect of inclusion of M/s.Crazy Infotech Ltd., after considering the TPO's observation and the DRP finding, M/s.Crazy Infotech Ltd., is in different line of business as the current business operations are of sale of

computer hardware and ERP software development, IT education and training and in Job Portal for placement and retirement and cannot be included and accordingly we confirm the action of TPO in excluding the comparable.

10.1 Whereas in respect of exclusion of M/s.KALS Information Systems Ltd., and M/s.Spry Resources India Pvt. Ltd., we found these companies are functionally different and no segmental data break-up and primarily a software product company and evident from the Annual Reports and holds nearly 26% of its revenue in the form of inventory and TPO has ignored the fact reported in the Audited statement and the company is full-fledged software product development company and provides implementation and maintenance of software products. We support our view relying on the decision of the Chennai bench of Tribunal in the case of *Sella Synergy India Pvt. Ltd.* (supra):

“7.3 We heard the rival submissions, perused the material on record and judicial decisions cited. In Kals information systems Ltd, the margin worked out by the Id. TPO being 36.25. The contention that this company is creating and providing 3D animation software content as a captive service provider to its Associated Enterprise. The company is providing software development activities and quality assurances services to its Associated Enterprise on an exclusive basis and also provides software maintenance support functions like documentation of the programmed code, IT integration and configuration management to its Associated Enterprise and it is a produce development company and relied on the judicial decisions *Ikanos Communication India (P.) Ltd.* (supra), *CNO IT Services (India) (P.) Ltd.* (supra), *Lionbridge Technologies (P.) Ltd.* (supra), *Obopay Mobile Technology India (P.) Ltd.* (supra), *Parexel International (India) (P.)*

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Ltd. (supra), pegasystems Worldwide India (P.) Ltd. (supra)
- *Lexreported and Prana Studios (P.) Ltd. (supra)*.

7.4 The company is not functionally comparable to the assessee company as the company is in providing 3D animation as captive service provider and also provide software development activities and segmental information is not available. Hence, we accept the contention of the Id. Authorised Representative and this company is excluded from the comparables and we direct the Id. TPO to exclude this company from comparables.”

In view of the above facts and details and ratio of judgment, we direct the TPO to exclude the comparable.

10.2 In respect of comparable company M/s.Spry Resources, India Pvt. Ltd., which is in software consultancy, product sale and has provision of software services and also impart computer training entrepreneur resources, planning and provision of ERP solution to its customers and no clarity on Revenue Recognition from the Annual Report and we found the Chennai bench of Tribunal in the case of *Sella Synergy India Pvt. Ltd. (supra)* has observed as under:

“6.6 In Spry Resources India Pvt. Ltd the Id. TPO worked out margin at 22.37. The company would undertake maintenance projects for the development projects concluded in the previous year. Company to focus on e-governance. However, profit and loss account does not show any revenue from maintenance projects. As per revenue recognition policy, the company has revenue from sale of software. However, no further segmental is available to show sale of software. Hence, the financial statements are not reliable.

6.7 We heard the rival submissions, perused the material on record. As per the Annual report of the company, the company has earned Revenue from Software consultancy and sale of software products and there is no breakup of Revenue segment

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wise between software products and software services. The operating income @16% from work in progress and the software consultancy and products functions differ from software development activities carried out by the assessee. Since there is no segmental income and company is not functionally in comparables, we are inclined to accept the contention of the Id. Authorised Representative and company should be excluded from the comparables. Accordingly, we direct the Id. TPO to exclude the company from comparables.”

Considering the circumstances and the information and the decision, we direct the TPO/AO to exclude the comparable from the list of comparables for determination of ALP.

10.3 Whereas in the matter of comparable company M/s. ICRA Techno Analytics Ltd., where the company is engaged in provision of variety of services being software products, consultancy, engineering services, web services and diversified into domain of business analytics and business process outsourcing and no segmental data available and also in KPO services and the Chennai bench of Tribunal held in the case of *Sella Synergy India Pvt. Ltd.* (supra) as under:

“7.8 We on perusal found that the said comparable company ICRA is in the business of software development & consultancy, engineering and diversified into domain of business analytics and business processing outsourcing and earned its Revenue from software development, consultancy, licensing, sub-licensing and others. As per the Annual report, the Revenue recognition from sale is recognized as and when delivery of branded software is made booked at net trade discount and in respect of development and consultancy, licensing and sub-licensing fee. The Revenue is recognized to the extent of services are performed. However, there is no breakup of Revenue development software development services and other services. The assessee company has not disclosed separate segments for ascertaining profitability and also cannot be regarded for the

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purpose of TNM analysis. We are of the opinion that the said company should be excluded from the list of comparables and we direct the ld. TPO to exclude.”

Accordingly, we direct the TPO to exclude this comparable.

10.4 Whereas in the case of M/s Taksheel Solutions, as pointed out by the learned DR the matter has to be re-looked and examined as it is mainly engaged in software development, community services, software products and provision of intangible assets in the books and segmental information is not available and employee cost to total sales is 2.53% and fails employee cost filter. Accordingly, we set aside this comparable company to the file of the TPO/AO to verify and examine the operations of the company.

10.5 Lastly, we find that the learned AR's contention that M/s.FCS Solutions which is functionally different and mainly into E-learning solutions and manages strategic business unit of IT community, education and information management and further allocated more than 20% of time of senior and skilled professional to research and development and support our view relying on the decision of the Pune Bench of Tribunal in the case of *TIBCO Software India (P) Ltd., vs. Dy.CIT* [2017] 78 taxmann.com 261 (Pune-Trib.) at para.39 which is as under:

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“39. The Revenue is in appeal before us not only against exclusion of Infosys Ltd., but also against exclusion of FCS Software Ltd., We find no merit in the said plea of the Revenue as the product companies are functionally not comparable to the concerns engaged in providing software services to its associate enterprises. Accordingly, we uphold the order of DRP for excluding FCS Software Ltd., and Infosys Ltd.”

and direct the TPO to exclude the comparable company. We order accordingly.

11. Ground Nos.3 and 4 are in regard to charging of interest u/s 234A and 234B which is consequential and the learned AR has not argued any other grounds of appeal and partly allow the grounds of appeal for statistical purposes.

12. In the result, the assessee's appeal is partly allowed for statistical purposes.

Order pronounced in the open court on 15th May, 2019.

Sd/-

(B.R. BASKARAN)
ACCOUNTANT MEMBER

Place : Bengaluru
Date : 31/05/2019
srinivasulu, sps

Sd/-

(PAVAN KUMAR GADALE)
JUDICIAL MEMBER

Copy to :

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By order

Assistant Registrar
Income-tax Appellate Tribunal
Bangalore