

IN THE INCOME TAX APPELLATE TRIBUNAL

“B” BENCH : BANGALORE

BEFORE SHRI ARUN KUMAR GARODIA, ACCOUNTANT MEMBER AND

SHRI PAVAN KUMAR GADALE, JUDICIAL MEMBER

ITA No. 1554/Bang/2017
Assessment Year : 2011-12

M/s. ARM Embedded Technologies Private Limited, Bagmane World Technology Pvt. Ltd., SEZ Citrine Block, 5 th Floor, Marathahalli Outer Ring Road, Doddanakundi Village, Mahadevapura, Bangalore – 560 048. PAN: AAECA1582E	Vs.	The Deputy Commissioner of Income Tax, Circle – 1 (1) (1), Bangalore.
APPELLANT		RESPONDENT
Assessee by	:	Shri T. Suryanarayana, Advocate
Revenue by	:	Ms. Neera Malhotra, CIT (DR)
Date of hearing	:	04.06.2019
Date of Pronouncement	:	07.06.2019

ORDER

Per Shri A.K. Garodia, Accountant Member

This appeal is filed by the assessee and the same is directed against the order of Id. CIT(A)-1, Bangalore dated 20.03.2016 for Assessment Year 2011-12.

2. The grounds raised by the assessee are as under.

“The grounds mentioned herein taken by the Appellant are without prejudice to one another.

1. That the orders passed by the Deputy Commissioner of Income Tax, Circle -1(1)(1), Bangalore (learned Assessing Officer' or 'learned AO') and the Learned Commissioner of Income-tax (Appeals) - I, Bangalore ('CIT(A)'), to the extent prejudicial to the Appellant, are bad in law and liable to be set aside.

2. That the learned AO / learned TPO and the learned CIT(A) erred in not appreciating that the Appellant had prepared the Transfer Pricing documentation bona fide and in good faith in compliance with the provisions of Section 92D of the Income Tax Act, 1961 (the 'Act') read with Rule 10D of the Income-tax Rules, 1962 ("the Rules") and that the Appellant had selected uncontrolled comparable companies based on a detailed Functional, Asset and Risk ("FAR") analysis, following a methodical and consistent benchmarking process in respect of the international transactions of provision of software development services and marketing and sales support services.

3. That the learned CIT(A) erred both in facts and law in confirming the action of the learned AO/TPO by making an adjustment to the price charged by the Appellant in respect of software development services provided to its associated enterprises by INR 82,844,691 and in respect to the marketing and sales support services provided to its associated enterprises by INR 1,670,645, holding that the international transactions do not satisfy the arm's length principle envisaged under the Act and in doing so, the CIT(A) grossly erred in;

(a) Upholding the rejection of comparability analysis of the Appellant in the TP documentation and accepting the comparability analysis performed by the learned TPO in the TP Order.

(b) Upholding the learned TPO's action in disregarding application of multiple year/prior year data as used by the Appellant in the TP documentation and in holding that current year (i.e. Financial Year 2010-11) data alone should be used for comparability.

(c) Upholding the learned TPO's approach of 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 the arm's length price.

(d) Upholding the set of companies selected by the learned TPO as comparables for the services rendered by the Appellant and thus upholding his action in rejecting/not considering companies that are functionally comparable to the Appellant and in including companies that fail the test of comparability.

(e) Upholding the learned TPO's action in arbitrarily arriving at a set of companies as comparables for the software development services and marketing and sales support activities rendered by the Appellant by rejecting companies that are functionally comparable to the Appellant and by including companies that fail the test of comparability.

(f) Upholding the learned TPO's approach of not providing risk adjustment and in thus ignoring the limited risk nature of the services provided by the Appellant and the fact that full-fledged entrepreneurial companies are selected as comparables.

(g) Upholding the learned TPO's approach in concluding that there is no correlation between the operating mark-up on cost earned and the turnover of a company and in thereby failing to appreciate that the learned TPO erred in failing to reject companies which have a large scale of operations when compared to the Appellant.

(h) Upholding the learned TPO's approach in not considering certain expenses/income while computing the operating mark-up on cost of the comparable companies on the premise that these are not routine operating costs without providing any cogent reason to substantiate the findings.

Software Development Services:

4. That the learned CIT(A) erred in confirming the action of the learned TPO of selecting Acropetal Technologies Ltd. (seg) although it is functionally incomparable to the Appellant and fails the employee costs and export sales filters, besides otherwise failing the test of comparability, and is thus not comparable to the Appellant.

5. That the learned CIT(A) erred in confirming the action of the learned TPO of selecting E- infochips Ltd. although it is functionally incomparable to the Appellant, there is non-availability of segmental data, performs research and development functions, holds intellectual property rights, there is a presence of inventory, and fails the service revenue filter, besides otherwise failing the test of comparability, and is thus not comparable to the Appellant.

6. That the learned CIT(A) erred in confirming the action of the learned TPO of selecting I C R A Techno Analytics Ltd. (seg) although it has diversified operations but no segmental data and has RPT in excess of 15%, besides otherwise failing the test of comparability, and is thus not comparable to the Appellant.

7. That the learned CIT(A) erred in confirming the action of the learned TPO of selecting Infosys Ltd. although it is a market leader, has diversified operations, non-availability of segmental data, holds intellectual property rights, has significant brand value, has presence of intangibles, and has high scale of operations, besides otherwise failing the test of comparability, and is thus not comparable to the Appellant.

8. That the learned CIT(A) erred in confirming the action of the learned TPO of selecting Persistent Systems Ltd. although is not functionally comparable to the Appellant, is engaged in providing outsourced product development services, develops software products and earns income from sale thereof, earns revenue from licensing of royalty, and has RPT in excess of 15%, besides otherwise failing the test of comparability, and is thus not comparable to the Appellant.

9. That the learned CIT(A) erred in confirming the action of the learned TPO of selecting Sasken Communication Technologies Ltd. although it is not functionally comparable to the Appellant, develops products and earns income from sale thereof, and has high R&D activities, besides otherwise failing the test of comparability, and is thus not comparable to the Appellant.

10. That the learned CIT(A) erred in confirming the action of the learned TPO of selecting Tata Elxsi Ltd. (seg) although it is functionally incomparable to the Appellant as it has diversified operations but no segmental data, fails the exports sales filter, and has high R&D expenses, besides otherwise failing the test of comparability, and is thus not comparable to the Appellant.

11. That, without prejudice, the learned CIT(A) erred in upholding the erroneous computation of mark-up of Tata Elxsi Ltd.

12. That Larsen and Toubro Infotech Ltd. ought to stand rejected as it is a market leader, has diversified operations, non-availability of segmental data, holds intellectual property rights, has significant brand value, has presence of intangibles, and has high scale of operations, besides otherwise failing the test of comparability, and is thus not comparable to the Appellant.

13. That Persistent System & Solutions Ltd. ought to stand rejected as it is not functionally comparable to the Appellant, is engaged in providing outsourced product development services, develops software products, and earns revenue from licensing of royalty, besides otherwise failing the test of comparability, and is thus not comparable to the Appellant.

14. That E-zest Solutions Ltd. ought to stand rejected as it is not functionally comparable to the Appellant since it is engaged in providing KPO services, provides end to end product development services, and has presence of inventory, besides otherwise failing the test of comparability, and is thus not comparable to the Appellant

15. That the learned CIT(A) erred in upholding the erroneous computation of mark-up of R S Software (India) Ltd.

16. That the learned CIT(A) erred in confirming the action of the learned TPO of rejecting companies that are functionally comparable to the Appellant such as Spry Resources India Pvt. Ltd., Akshay Software Technologies Ltd., LGS Global Ltd., and Thinksoft Global Services Ltd.

17. That the learned CIT(A) erred in confirming the learned TPO's action in rejecting FCS Software Solutions Ltd. on wholly baseless and erroneous grounds despite him having accepted that it is functionally similar to the Appellant and otherwise passing all the filters applied by him.

18. That the learned CIT(A) erred in upholding the action of the learned TPO in erroneously computing the working capital adjustment.

Marketing and sales support services:

19. That the learned CIT(A) erred in confirming the action of the learned TPO of selecting Asian Business Exhibition & Conferences Ltd. although it is functionally dissimilar to the Appellant on numerous counts, and also because it has no export earnings and is thus not comparable to the Appellant.

20. That the learned CIT(A) erred in confirming the action of the learned TPO of selecting ICC Industrial Agencies Ltd. although it is functionally dissimilar to the Appellant and thus fails the test of

comparability.

21. That, without prejudice, the learned CIT(A) erred in upholding the erroneous computation of mark-up of Asian Business Exhibition & Conferences Ltd. and ICC Industrial Agencies Ltd.

22. That the mark-up of Cyber Media Research Ltd. has been erroneously computed.

23. That the learned CIT(A) erred in confirming the action of the learned TPO by rejecting companies that are functionally comparable to the Appellant such as PAE Ltd., Empire Industries Ltd. (Trading and Indenting Segment), Salora International Ltd. (Infocom Division), Kores (India) Ltd., and Killick Agencies & Marketing Ltd.

24. That the learned CIT(A) erred in upholding the action of the learned TPO of arbitrarily not granting working capital adjustment for the marketing and sales support services segment of the Appellant.

That the Appellant craves leave to add to and/or to alter, amend, rescind, modify the grounds herein below or produce further documents before or at the time of hearing of this Appeal.”

3. At the very outset, it was submitted by Id. AR of assessee that the order of CIT(A) is very cryptic and in this regard, he pointed out that the order of CIT(A) is of 14 pages and upto page no. 10 of the order of CIT(A), he has reproduced the statement of facts and grounds of appeal filed by the assessee before CIT(A). Thereafter he submitted that on page nos. 11 to 13 of the order of CIT(A), he has noted the arguments advanced by the Id. AR of assessee before him. Thereafter he pointed out that finally on page no. 14 of his order in para 7.3, he has decided the issue in one line by saying that the TPO has made correct determination of arm's length price and has made total adjustment of Rs. 8,45,15,336/-. He submitted that since the order of CIT(A) is not a speaking and reasoned order, the matter may be restored back to his file for passing a speaking and reasoned order. The Id. DR of revenue supported the order of CIT(A).
4. We have considered the rival submissions. We find force in the submission of Id. AR of assessee. We find that the whole issue was decided by CIT(A) in one line. For this purpose, we reproduce para 7.3 from the order of CIT(A). This para reads as under.

“7.3 The TPO is also of the view that in the case of taxpayer TNMM is the most appropriate method of determining the ALP of the international transactions of the taxpayer in the market support

services segment. Therefore, the TPO searched the public database Prowess and selected a set of 7 uncontrolled comparables considering financial data for financial year 2010-11 only. The Arm's length price of the international transaction of the taxpayer relating to market support services is determined by applying TNMM as and using the set of 3 uncontrolled comparables selected by the TPO, with average PLI (OP/Cost) of 18.25%. The tax payer's PLI (OP/Cost) in the segment is 8%. Based on the detailed discussion held in various parts of this order the arm's length price of the international transactions entered into by the taxpayer is computed. UNMM is used as the most appropriate method both by the tax payer as well as the TPO. The arithmetic mean of the profit level indicators is taken as the arm's length margin. Based on this, the arm's length price of the services rendered by the taxpayer to its AE(s) is computed. The shortfall of Rs.16,70,645/- is treated as transfer pricing adjustment u/s 92CA in respect of SALES AND MARKETING SEGMENT of the taxpayer's international transactions. The TPO has made correct determination of arm's length price, and has made total adjustment of Rs.8,45,15,336/-. Accordingly the adjustment made by the TPO is hereby upheld."

5. From the above para reproduced from the order of CIT(A), it is seen that the order of CIT(A) is not a speaking and reasoned order and therefore, we feel it proper to set aside the order of CIT(A) and restore the matter back to his file for fresh decision by way of a speaking and reasoned order after providing adequate opportunity of being heard to both sides. We order accordingly. In view of this decision, we do not make any comment on the merit of the case.
6. In the result, the appeal filed by the assessee is allowed for statistical purposes.
Order pronounced in the open court on the date mentioned on the caption page.

Sd/-
(PAVAN KUMAR GADALE)
Judicial Member

Sd/-
(ARUN KUMAR GARODIA)
Accountant Member

Bangalore,
Dated, the 07th June, 2019.
/MS/

Copy to:

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|---------------|------------------------|
| 1. Appellant | 4. CIT(A) |
| 2. Respondent | 5. DR, ITAT, Bangalore |
| 3. CIT | 6. Guard file |

By order

Assistant Registrar,
Income Tax Appellate Tribunal,
Bangalore.