

IN THE INCOME TAX APPELLATE TRIBUNAL

“C” BENCH : BANGALORE

BEFORE SHRI ARUN KUMAR GARODIA, ACCOUNTANT MEMBER AND
SHRI PAVAN KUMAR GADALE, JUDICIAL MEMBER

Appeal No.	Appellant	Respondent	Assessment Year
ITA No. 2026/Bang/2017	M/s. CSG Systems International (India) Private Limited, [Formerly known as Independent Technology Systems (India) Pvt. Ltd.], Divyasree Towers, 4 th Floor, No. 55, Guruppanna Palya, Madivala Range, Bangalore – 560 029. PAN: AABCI2954B	The Deputy Commissioner of Income Tax, Circle 11 (3), Bangalore.	2010-11
IT(TP)A Nos. 2642/Bang/2017	The Deputy Commissioner of Income Tax, Circle – 2 (1) (1), Bangalore.	M/s. CSG Systems International (India) Private Limited, [Formerly known as Independent Technology Systems (India) Pvt. Ltd.], Divyasree Towers, 4 th Floor, No. 55, Guruppanna Palya, Madivala Range, Bangalore – 560 029. PAN: AABCI2954B	2010-11
IT(TP)A Nos. 2643/Bang/2017			2011-12
Assessee by	:	Shri K.R. Vasudevan, Advocate	
Revenue by	:	Shri Pradeep Kumar, CIT (DR) & Dr. P.V. Pradeep Kumar, Addl. CIT (DR)	
Date of hearing	:	09.07.2019	
Date of Pronouncement	:	31.07.2019	

ORDER

Per Shri A.K. Garodia, Accountant Member

This bunch of three appeals is including two cross appeals of assessee and revenue for Assessment Year 2010-11 and one appeal of revenue only for Assessment Year 2011-12. All these three appeals were heard together and are being disposed of by way of this common order for the sake of convenience.

2. The grounds raised by the assessee in ITA No. 2026/Bang/2017 for Assessment Year 2010-11 are as under.

“Based on the facts and circumstances of the case and in law, CSG

Systems International (India) Private Limited ("CSG India" or the "Company" or the "Appellant") respectfully craves leave to prefer an appeal under section 253 of the Income-tax Act, 1961 ("the Act") against the order dated 21 August 2017 passed by the Commissioner of Income-tax (Appeals), Circle - 3 ["CIT(A)"], Bangalore under section 250 of the Act on the following grounds:

That on facts and circumstances of the case and in law:

1. The learned CIT(A) has erred in law and facts, by upholding adjustment made by the learned Assessing Officer ("AO") / Transfer Pricing Officer ("TPO") to the arm's length price of the international transactions of software development services rendered by the Appellant to its Associated Enterprise ("AE");

2. The learned CIT(A) has erred in law and facts by not accepting the Appellant's plea in entirety and upholding the action of the learned AO/TPO of rejection of Transfer Pricing Documentation ['TP Documentation'] including economic analysis undertaken by the Appellant in accordance with the provisions of the Act read with the Income-tax Rules, 1962 ("the Rules") by erroneously invoking provision of section 92C(3)(a) and (c) of the Act without providing cogent reasons;

3. The learned CIT(A) has erred in law and facts, by upholding the action of learned AP/TPO of disregarding certain comparable companies selected by the appellant in the TP Documentation and instead conducted fresh search and thereby erroneously selected additional comparable companies for determination of the arm's length price in connection with the impugned international transaction and holding that the international transaction entered into by the Appellant is not at arm's length;

4. The learned CIT (A) has erred in law and facts, by upholding action of the learned AO/TPO of rejecting the use of multiple year data adopted by the Appellant for determining the arm's length price of the international transaction;

5. The learned CIT (A) has erred in law and facts, by upholding action of the learned AO/TPO of using only FY 2009-10 data for determining the arm's length margin/price of the international transaction, which was not available to the Appellant at the time' of complying with the transfer pricing documentation requirements:

6. The learned CIT(A) has erred in law and facts by upholding the action of learned AO/TPO of accepting/rejecting companies which are comparable to the Appellant's operations by applying the following quantitative and qualitative filters:

a) The learned CIT(A) has erred, in law and in facts, by not accepting

the Appellant's plea that companies should not be rejected using software development services less than 75% of the total operating revenue as a comparability criterion;

b) The learned CIT (A) has erred, in law and in facts, by not accepting the Appellant's plea that companies should not be rejected using employee cost greater than 25% of the turnover as a comparability criterion;

c) The learned CIT (A) has erred, in law and in facts, by not accepting the Appellant's plea that companies should not be rejected using export sales less than 75% of the sales as a comparability criterion;

d) The learned CIT (A) has erred, in law and in facts, by not accepting the Appellant's plea that companies should not be rejected using related party transactions greater than 25% of the sales as a comparability criterion;

e) The learned CIT (A) has erred, in law and in facts, by not accepting the Appellant's plea that companies having different financial year ending or data of the company which do not fall within 12 month period (i.e. April 1, 2009 to March 31, 2010) should not be rejected.

f) The learned CIT (A) has erred, in law and in facts, by upholding the action of the learned AO/TPO of not applying upper limit to the turnover filter.

7. The learned CIT(A) has erred, in law and in facts, by upholding the action of the learned AO/TPO of rejection of advertisement, marketing and distribution expenses less than or equal to 3 percent of sales as a comparability criterion for the purpose of selection of comparable companies;

8. The learned CIT(A) has erred, in law and facts, by upholding the action of the learned AO/TPO of selecting companies such as Infosys Limited, Persistent Systems Limited and retaining companies such as Larsen & Toubro Infotech Limited and Sasken Communications Limited as comparables which are functionally dissimilar;

9. The learned CIT(A) has erred, in law and facts, by upholding the action of the learned AO/TPO of rejecting Akshay Software Technologies Limited as a comparable company on the ground that the company is earning 90 per cent of revenue by conducting operations from Dubai instead of from India which is factually incorrect;

10. The learned CIT(A) has erred, in law and facts, by upholding the action of the learned AO/TPO of rejecting Teledata Marine solutions limited as a comparable company on the ground of failing the RPT filter of 25 percent, which is factually incorrect;

11. The learned CIT(A) has erred, in law and facts, by upholding the action of learned AO/TPO of not considering foreign exchange fluctuations (gain/loss) as operating in nature for the purpose of computation of margin of the Appellant as well as the comparable companies;

12. The learned CIT(A) has erred, in law and facts, by upholding the action of learned AO/TPO of not considering provision for doubtful debts as operating in nature for the purpose of computation of margin of the comparable companies;

13. The learned CIT(A) has erred, in law and facts, by not providing working capital adjustment to account for difference in the working capital of the Appellant and the comparable companies

14. The learned CIT(A) has erred, in law and facts, by not providing risk adjustment to account for difference in the risk profile of the Appellant and the comparable companies;

15. The learned CIT(A) has erred, in law and facts, by upholding the action of learned AO of levying interest under section 234B, 234C & 234D of the Act;

16. The learned CIT(A) has erred, in law and facts, by upholding the action of learned AO of initiating penalty proceedings under section 271(1) (c) of the Act

The Appellant submits that each of the above grounds is independent and without prejudice to one another.

The Appellant craves leave to add, alter, amend, vary, omit or substitute any of the aforesaid grounds of appeal at any time before or at the time of hearing of the appeal, so as to enable the Hon'ble Tribunal to decide on the appeal in accordance with the law."

3. The grounds raised by the revenue for Assessment Year 2010-11 in IT(TP)A No. 2642/Bang/2017 are as under.

“Corporate issue: "Whether CIT(A) was correct in directing the AO to reduce the impugned expenses from both the export turnover as well as the total turnover while calculating deduction U/s 10A".

TP issues: Hon'ble CIT(A) has rejected the following comparables for TP issues. The grounds of appeal against the rejection are as follows:

1. KALS information systems Ltd:

i) Whether the Hon'ble CIT(A) erred in fact and law in holding the company M/s Kals information Systems Ltd as a software product company when there is no revenue reported from sale of products in

the annual report of the company and rejecting the company as a comparable.

ii) Whether the Hon'ble CIT(A) erred in fact and law in holding the company M/s Kals Information Systems Ltd as a software product company when there is no inventory as either part of the stock in trade or work in progress accounted in the profit & loss account.

iii) Whether the Hon'ble CIT(A) erred in fact and law in holding the company M/s Kals Information Systems Ltd as a software product company without appreciation the fact that the company in its annual report in point no 06 page no 22 disclosed that the revenue earned is from the business of development of computer software and other related services. The production and sale of such software is not capable of being expressed in any generic unit.

iv) Whether the Hon'ble CIT(A) was right in fact and in law seeking exact comparability, which searching for comparable companies of the assessee under TNMM whereas the requirement of law and international jurisprudence require seeking similar comparable companies?

v) Whether while seeking the exact comparability as mentioned above the Hon'ble CIT(A) was right in fact and in law in imposing condition beyond law whereas the requirement of law is to acknowledge only those differences that are likely to materially affect the margin.

vi) Whether the Hon'ble CIT(A) is correct in fact and law in disregarding the position of law that there could be differences between the enterprise compared under the TNMM method that are not likely to materially affect the price or cost charged or the profits accruing to such enterprise?

vii) Whether Hon'ble CIT(A) erred in fact in rejecting the company as a comparable on the grounds that it is functionally different when the primary source of income of the comparable is from provision of software development services.

2) *Tata Elxsi Ltd:*

i) Whether the Hon'ble CIT(A) was right in fact in law in seeking exact comparability, which searching for comparable companies of the assessee under TNMM whereas the requirement of law and international jurisprudence require seeking similar comparable companies?

ii) Whether while seeking the exact comparable as mentioned above the Hon'ble CIT(A) was right in fact and in law in imposing condition beyond law whereas the requirement of law is to

acknowledge only those differences that are likely to materially affect the margin.

iii) Whether the Hon'ble CIT(A) is correct in fact and law in disregarding the posting of law that there could be differences between the enterprise compared under the TNMM method that are not likely to materially affect the price or cost charged or the profits accruing to such enterprise?"

4. Similarly, the grounds raised by the revenue for Assessment Year 2011-12 in IT(TP)A No. 2643/Bang/2017 are as under.

“Grounds of appeal in case of M/s. CSG System International Pvt. Ltd for A.Y. 2011-12

Corporate issue: "Whether CIT(A) was correct in directing the AO to reduce the impugned expenses from both the export turnover as well as the total turnover while calculating deduction U/s 10A".

TP issues: Hon'ble CIT(A) has rejected the following comparables for TP issues. The grounds of appeal against the rejection are as follows:

- 1) Tata Elxsi Ltd*
- 2) ICRA Techno Analytics Ltd:*

Grounds of Appeal:

i) On the fact & circumstances of the case and in law Ld. CIT(A) erred in seeking exact comparability, while searching for comparable companies of the assessee under TNMM whereas the requirement of law and international jurisprudence require seeking similar comparable companies?

ii) Further, while seeking the exact comparability as mentioned above whether the Ld. CIT (A) was right in fact and in law in imposing condition beyond law whereas the requirement of law is to acknowledge only those differences that are likely to materially affect the margin.

iii) Further, whether the Ld.CIT(A) is correct in fact and law in disregarding the position of law that there could be differences between the enterprise compared under TNMM method that are not likely to materially affect the price or cost charged or the profits accruing to such enterprises?"

5. Regarding assessee's appeal for Assessment Year 2010-11, it was submitted that ground nos. 1 to 14 are in respect of TP issues and the same can be decided on the basis of chart submitted by Id. AR of assessee which contains the assessee's submissions regarding these issues. Regarding ground no. 15, it was submitted that the issue involved in this ground is regarding interest

u/s. 234B, 234C and 234D and hence, this issue is consequential. Regarding ground no. 16, he submitted that the issue involved in this ground is about initiation of penalty proceedings u/s. 271(1)(c) of IT Act and he submitted that this ground is premature. The Id. DR of revenue supported the orders of Id. CIT(A). Regarding ground no. 11 of assessee's appeal in respect of this aspect that foreign exchange fluctuation gain / loss should be considered as operating in nature for the purpose of computation of the margin of the assessee company as well as of the comparable companies, it was submitted by Id. DR of revenue that for deciding this issue, the assessee has to bring on record the details as to whether such foreign exchange fluctuation gain / loss of assessee or of the comparable companies is in respect of turnover of the present year or an earlier year and if such gain/loss is in relation to the turnover of the present year, then only the same can be considered for TP analysis. Since such details are not brought on record by the assessee, this issue should be decided against the assessee. Regarding revenue's appeal for Assessment Year 2010-11, it was agreed by both sides that the corporate tax issue involved in this appeal of revenue is squarely covered in favour of the assessee by the judgment of Hon'ble Karnataka High Court rendered in the case of CIT Vs. Tata Elxsi Ltd. as reported in 349 ITR 98. Regarding the TP issue involved in the appeal of the revenue in respect of objection to the exclusion of two comparables i.e. KALS information systems Ltd. and Tata Elxsi Ltd., it was agreed by both sides that this TP issue involved in revenue's appeal may be also be decided on the basis of chart submitted by Id. AR of assessee.

6. We have considered the rival submissions. We find that in the appeal of the revenue, one ground involved is regarding computation of deduction allowable to the assessee u/s. 10A of the IT Act for which the AO has reduced the expenditure incurred in foreign currency of Rs. 1,68,00,443/- from export turnover whereas this was the claim of the assessee that even if it is reduced from export turnover, the same expenditure should be reduced from total turnover also. Ld. CIT(A) held that such expenditure should be reduced from export turnover as well as total turnover while calculating deduction u/s. 10A. Now this issue is squarely covered in favour of the assessee by the judgment

of Hon'ble Karnataka High Court rendered in the case of CIT Vs. Tata Elxsi Ltd. (supra) in which it is held that total turnover is sum total of export turnover and domestic turnover and if an amount is reduced from export turnover then the total turnover also goes down by the same amount automatically. Since the direction of Id. CIT(A) is in line with this judgment of Hon'ble Karnataka High Court, we find no reason to interfere in the order of Id. CIT(A) on this issue. Accordingly, this ground of the revenue's appeal is rejected.

7. On TP issues, the revenue has two grievances i.e. regarding direction of Id. CIT(A) to exclude two comparables i.e. KALS information systems Ltd. and Tata Elxsi Ltd. As per the chart submitted by Id. AR of assessee, this is the submission of Id. AR of assessee that the issue regarding exclusion of KALS information systems Ltd. (seg) is covered in favour of the assessee by the Tribunal order rendered in the case of Cerner Healthcare Solutions P. Ltd. Vs. ITO in IT(TP)A Nos. 44 & 69/Bang/2015, copy available on pages 1 to 12 of case law paper book and our attention was drawn to para nos. 12 to 14 of this Tribunal order and it was pointed out that as per these paras, this comparable i.e. KALS information systems Ltd. was excluded by the Tribunal. He submitted that regarding exclusion of KALS information systems Ltd., the Tribunal has considered another Tribunal order rendered in the case of DCIT vs. Electronics for Imaging India (P.) Ltd., [2016] 70 taxmann.com 299 (Bang-Trib.) and relevant portion of this Tribunal order is noted in which it is noted by Tribunal in that case that this company is engaged in the development of software and software products. Therefore, this is not a comparable company for software development service providing company.
8. Regarding exclusion of Tata Elxsi Ltd., reliance was placed on the Tribunal order rendered in the case of AMD India P. Ltd. vs. ACIT in IT(TP)A Nos. 1487 & 1496/Bang/2015 dated 06.04.2017, copy submitted and our attention was drawn to page nos. 25 and 32 of this Tribunal order as per which it was held by the Tribunal in that case that Tata Elxsi Ltd. is not a good comparable for a software development company. The Id. DR of revenue supported the order of TPO regarding exclusion of these two companies.

9. We have considered the rival submissions. First of all, we examine the applicability of the Tribunal order rendered in the case of Cerner Healthcare Solutions P. Ltd. Vs. ITO (supra), copy available on pages 1 to 12 of the paper book of case laws for Assessment Year 2010-11. In the chart submitted by ld. AR of assessee, it has been pointed out that pages 9 to 11 of this Tribunal order are relevant. On page no. 9 of this Tribunal order, there is discussion about exclusion of Tata Elxsi Ltd. and decision is in para no. 14 but we first reproduce the relevant portion of that para no. 12 from page no. 9 of the Tribunal order.

“(6) Tata Elxsi Ltd.

15. The assessee has raised objections against this company on the ground that the company is functionally different from the assessee. Though the TPO has considered the software development and services segment of this company as comparable to that of assessee, however, the assessee contended that even within the software segment, this company is engaged in diverse activities. The assessee placed reliance on the information in the annual report under the Directors Report and submitted before the DRP that even under the software development services segment, this company is engaged in various diversified activities including product design service, innovation design, engineering service, visual computing labs, etc. The assessee also placed reliance on the decision of Mumbai Bench of the Tribunal in the case of Telcordia Technologies Pvt. Ltd. v. ACIT, 137 ITD 1 (Mum).

16. The DRP found that this company is not functionally comparable with assessee company as it is engaged in diversified activities even in the software development services. The DRP has followed the decision of the Mumbai Bench of the Tribunal in the case of Telcordia Technologies Pvt. Ltd. (supra).

17. We have heard the ld. DR as well as ld. AR and considered the relevant material on record. We find that this company even in the software development segment is engaged in diversified activities of product design services, innovation design, engineering services, visual computing labs, etc. We further note that in the case of Telcordia Technologies Pvt. Ltd. (supra), the Mumbai Bench of the Tribunal vide its order dated 11.5.2012 in para 9.7 has held as under:-

“7.7 From the facts and material on record and submissions made by the learned AR, it is seen that the Tata Elxsi is engaged in development of niche product and development services which is entirely different from the assessee company. We agree with the contention of the learned AR that the nature of product developed and services provided by this company are different from the

assessee as have been narrated in para 6.6 above. Even the segmental details for revenue sales have not been provided by the TPO so as to consider it as a comparable party for comparing the profit ratio from product and services. Thus, on these facts, we are unable to treat this company as fit for comparability analysis for determining the arm's length price for the assessee, hence, should be excluded from the list of comparable parties."

18. No contrary view has been brought to our notice regarding comparability of this company with that of a pure software development service provider. Accordingly, in view of the decision of the Mumbai Bench of the Tribunal in the case of Telcordia Technologies Pvt. Ltd. (supra), we do not find any reason to interfere with the finding of the DRP."

10. Thereafter the issue regarding exclusion of Tata Elxsi Ltd. was decided by the Tribunal as per para no. 14 of this Tribunal order and hence, for ready reference, we reproduce para 14 of this Tribunal order from page no. 11 of this judgment rendered in the case of Cerner Healthcare Solutions P. Ltd. Vs. ITO (supra). This para reads as under.

"14. We find that the CIT (A) accepted the assessee's plea by following the decisions of this Tribunal in Genisys Integrating System v DCIT 15 ITR Trib 475, Kodiak Networks v ACIT 15 ITR Trib 610, Trilogy e-Business Software India v DCIT 23 ITR Trib 464 and held that those companies which are within the turnover range of Rs one crore to Rs two hundred crore only should be taken into consideration for the TP study and hence directed the TPO to exclude Infosys Ltd, Larsen & Toubro Infotech Ltd, Mindtree Ltd (seg) , Persistent System Ltd, Sasken communication Technologies and Tata Elxsi Ltd(seg) against which the Revenue filed appeals. However, from the decisions extracted, supra, the assessee has made out a case for the exclusion of ICRA Techno Analytics Ltd. (seg), Infosys Technologies Ltd., KALS Information Systems Ltd, Persistent Systems Ltd, Sasken Communication Technologies Ltd, Tata Elxsi Ltd and L&T Infotech Ltd. Following them, we direct the TPO to exclude them from the list of comparables. To that extent, the assessee's appeal grounds are allowed and the Revenue's appeal grounds are dismissed. With regard to the comparable Mindtree Ltd (seg), since the assessee has not opposed the Revenue's appeal, the Revenue's appeal on that comparable is treated as allowed."

11. Respectfully following this Tribunal order rendered in the case of Cerner Healthcare Solutions P. Ltd. Vs. ITO (supra) which is for the same Assessment Year i.e. Assessment Year 2010-11 and we have noted that in para 2 of this Tribunal order, this is noted by the Tribunal in this case that

Cerner Healthcare Solutions P. Ltd. Vs. ITO (supra) that Cerner Healthcare Solutions Pvt. Ltd. is a captive service provider engaged in the business of rendering software development services to its AE. Hence the functional profile of the present assessee and Cerner Healthcare Solutions Pvt. Ltd. is same and therefore, in our considered opinion, this Tribunal order is applicable in the present case. Respectfully following this Tribunal order, we hold that no interference is called for in the order of CIT (A) regarding exclusion of Tata Elxsi Ltd. We decline to interfere in the order of Id. CIT(A) on this issue.

12. Now we examine the issue in respect of KALS information systems Ltd. (seg). Reliance has been placed before us on the Tribunal order rendered in the case of Cerner Healthcare Solutions P. Ltd. Vs. ITO (supra). In the chart it has been submitted that page nos. 7, 8 and 11 of this Tribunal order are relevant regarding exclusion of this comparable i.e. KALS information systems Ltd. (seg). The Id. DR of revenue has placed reliance on the order of TPO in this regard.
13. We have considered the rival submissions. We first examine the applicability of this Tribunal order rendered in the case of Cerner Healthcare Solutions P. Ltd. Vs. ITO (supra). We find that this Tribunal order is also for same Assessment Year i.e. 2010-11 and as per para 10 of this Tribunal order, the assessee is also involved in providing software development services to its AE and hence, it is seen that the functional profile is also same and therefore, in our considered opinion, this Tribunal order is applicable in the present case. Now we find that issue regarding exclusion of KALS information systems Ltd. (seg) has been discussed by the Tribunal on pages 7 and 8 of this Tribunal order which is part of para no. 12 of this Tribunal order and hence, we reproduce the relevant portion of this para no. 12 of this Tribunal order for ready reference.

“(3) KALS Information Systems Ltd.

6. The assessee raised objections against this company on the ground that this company is engaged in the development of software and software products. Further, this company consists of STPI unit and also having a training centre engaged in training of software professionals on online products. Thus, when this company is having revenue from software services as well as software product, the same

cannot be considered as comparable with software development service providing company.

7. The DRP has directed the AO to exclude this company from the list of comparables by taking note of the fact that there were inventories in the books of accounts of this company which shows that this company is in the software product business. Further, by following the decision of this Tribunal in the case of Trilogy e-business Software India Ltd. v. DCIT, ITA No.1054/Bang/2011 dated 23.11.2012, this company was found to be not comparable with that of the assessee.

8. We have heard the ld. DR as well as ld. AR and considered the relevant material on record. The ld. DR has not disputed the fact that comparability of this company has been examined by this Tribunal in a series of decisions including in the case of Trilogy e-business Software India Ltd. (supra). We further note that in the balance sheet of this company as on 31.3.2010, there are inventories of Rs.60,47,977. Therefore, when this company is in the business of software products, the same cannot be compared with a pure software development services provider. Accordingly, we do not find any error or illegality in the impugned findings of the DRP.”

14. The issue regarding exclusion of KALS information systems Ltd. (seg) was ultimately decided by the Tribunal as per para no. 14. This is also reproduced hereinbelow for ready reference.

“14. We find that the CIT (A) accepted the assessee’s plea by following the decisions of this Tribunal in Genisys Integrating System v DCIT 15 ITR Trib 475, Kodiak Networks v ACIT 15 ITR Trib 610, Trilogy e-Business Software India v DCIT 23 ITR Trib 464 and held that those companies which are within the turnover range of Rs one crore to Rs two hundred crore only should be taken into consideration for the TP study and hence directed the TPO to exclude Infosys Ltd, Larsen & Toubro Infotech Ltd, Mindtree Ltd (seg) , Persistent System Ltd, Sasken communication Technologies and Tata Elxsi Ltd(seg) against which the Revenue filed appeals. However, from the decisions extracted, supra, the assessee has made out a case for the exclusion of ICRA Techno Analytics Ltd. (seg), Infosys Technologies Ltd., KALS Information Systems Ltd, Persistent Systems Ltd, Sasken Communication Technologies Ltd, Tata Elxsi Ltd and L&T Infotech Ltd. Following them, we direct the TPO to exclude them from the list of comparables. To that extent, the assessee’s appeal grounds are allowed and the Revenue’s appeal grounds are dismissed. With regard to the comparable Mindtree Ltd (seg), since the assessee has not opposed the Revenue’s appeal, the Revenue’s appeal on that comparable is treated as allowed.”

15. From the above para as per para 14, it is seen that in that case, the Tribunal held that KALS information systems Ltd. (seg) is not a good comparable. Although in this para, the Tribunal has noted about the turnover filter also being Rs. One crore to Rs. Two hundred crores but considered all the judgments noted before this para and we have already reproduced relevant portion of para 12 of this Tribunal order in which it is noted by the Tribunal regarding KALS information systems Ltd. (seg) that comparability of this company has been examined by the Tribunal in a series of decisions including in the case of Trilogy e-business Software India Ltd. The Tribunal has also noted that in the balance sheet of this company as on 31.03.2010, there are inventories of Rs. 60,47,977/- and on the basis of these facts, this finding is given that this company is in the business of software products and therefore, it is held that the same cannot be compared with a pure software development services provider company. Hence, in the present case, we hold that because of this functional dissimilarity as held by the Tribunal in the case of DCIT vs. Electronics for Imaging India (P.) Ltd. (supra), no interference is called for in the order of Id. CIT(A) regarding this direction to exclude KALS information systems Ltd.
16. In the result, this appeal of the revenue is dismissed in the terms indicated above.
17. Now we take up the assessee's appeal. In assessee's appeal, as per ground no. 8 of assessee's appeal, the assessee is seeking exclusion of four comparable companies i.e. 1) Infosys Ltd. 2) Persistent Systems Ltd. 3) Larsen & Toubro Infotech Ltd. and 4) Sasken Communications Ltd.
18. Regarding the assessee's request for exclusion of these four comparable companies, reliance has been placed on the Tribunal order rendered in the case of Cerner Healthcare Solutions P. Ltd. Vs. ITO (supra), copy available on pages 1 to 12 of the case law paper book. Regarding exclusion of Infosys Ltd., para 12 of this Tribunal order is reproduced hereinbelow.

“12. We have considered the rival submissions and gone through relevant materials. The relevant portion of the order from the case of Electronics for India Imaging India P Ltd ay 2010-11in IT (TP)A no. 212/Bang/2015 & CO No 94/ Bang/2015 dt 24.02.2016 is extracted as under:

“ 2. The assessee challenged the action of the TPO before the DRP and raised objections against some of the comparables selected by the TPO. The DRP in its directions rejected 8 out of 11 comparables selected by the TPO. Thus, the Revenue is aggrieved by the directions of the DRP insofar as the comparables are directed to be excluded from the set of comparables.

3. We shall deal with each comparable which has been disputed by the Revenue one by one as under:-

(1) ICRA Techno Analytics Ltd. (seg)

4. At the outset, we note that apart from having the related party revenue at 20.94% of the total revenue, this company was also found to be functionally not comparable with software development services segment of the assessee. The DRP has given its finding at pages 13 to 14 as under:-

“Having heard the contention, on perusal of the annual report, it is noticed by us that the segmental information is available for two segments i.e., services and sales. However, it is evident from the annual report that the service segment comprises of software development, software consultancy, engineering services, web development, web hosting, etc. for which no segmental information is available and therefore, the objection of the assessee is found acceptable. Accordingly, Assessing Officer is directed to exclude the above company from the comparables.”

5. We find that the facts recorded by the DRP in respect of business activity of this company are not in dispute. Therefore, when this company is engaged in diversified activities of software development and consultancy, engineering services, web development & hosting and substantially diversified itself into domain of business analysis and business process outsourcing, then the same cannot be regarded as functionally comparable with that of the assessee who is rendering software development services to its AE.

6. In view of the above facts, we do not find any error or illegality in the findings of the DRP that this company is functionally not comparable with that of a pure software development service provider.

(2) Infosys Ltd.

2. The assessee objected against the selection of this company on the ground that this company has a big name and brand value and therefore it has a bargaining power. It also contended that the turnover of this company is Rs.21,140 crores, which is 442 times higher than the assessee.

3. The DRP accepted the objections of the assessee and by following the decision of the Delhi Benches of the Tribunal in the case of Agnity

India Pvt. Ltd. v. ITO [2015] 58 taxmann.com 167 (Delhi – Trib), directed the TPO to exclude this company from the list of comparables.

4. We have heard the ld. DR as well as ld. AR and considered the relevant material on record. We note that in the case of Agnity India Pvt. Ltd. (supra), the Delhi Bench of the Tribunal has considered the comparability of this company and the findings of the Delhi Bench of the Tribunal has been confirmed by the Hon'ble Delhi High Court. The Hon'ble Delhi High Court has observed that this company having brand value as well as intangible assets cannot be compared with an ordinary entity provide captive service. We further note that this company provides end to end business solutions that leverage cutting edge technology thereby enabling clients to enhance business performance. This company also provides solutions that span the entire software lifecycle encompassing technical consulting, design, development, re-engineering, maintenance, systems integration, package evaluation and implementation, testing and infrastructure management service. In addition, the company offers software product for banking industry. Thus, this company is engaged in diversified services including design as well as technical consultancy, consulting, re-engineering, maintenance, systems integration as well as products for banking industry.

5. In view of the above facts that Infosys Ltd. having a huge brand value and intangibles as well as having bargaining power, the same cannot be compared with the assessee who is providing services to its AE.”

19. In this para, the Tribunal in that case has reproduced the relevant portion of the Tribunal order rendered in the case of DCIT vs. Electronics for Imaging India (P.) Ltd. (supra) as per which it was held that Infosys Ltd. is having a huge brand value and intangibles as well as having bargaining power and the same cannot be compared with the assessee who is providing only software development services to its AE. Respectfully following this Tribunal order, we hold that Infosys Ltd. should be excluded.
20. In the same para no. 12 of this Tribunal order as already reproduced above, the issue regarding exclusion of Persistent Systems Ltd. and Sasken Communication Technologies Ltd. is also discussed and decided. Regarding Persistent Systems Ltd., it was held that this company is engaged in diversified activities and earning revenue from various activities including licencing of products, royalty on sale of products as well as income from maintenance contract, etc., and therefore, this company cannot be considered as functionally comparable with the assessee. Regarding Sasken

Communication Technologies Ltd., it was held that this company earns revenue from three segments but the segmental operating margins are not available and therefore, in the absence of relevant segmental data and particularly operating margins, this composite data cannot be considered as comparable with the assessee for software development services segment. Respectfully following this Tribunal order, we hold that these two comparables i.e. Persistent Systems Ltd. and Sasken Communication Technologies Ltd. should also be excluded.

21. Regarding Larsen & Toubro Infotech Ltd., the discussion and decision is contained in para no. 13 of this Tribunal order reproduced below:-

“13. The relevant portion of the order from the case of Pegasystems Worldwide India P Ltd ay 2010-11 ITA No 1758/Hyd/2014 & 1936/Hyd/2014 dt 16.10.2015 is extracted as under :

“ L&T Infotech Ltd:

14. Assessee has objected before TPO that the department in earlier years is rejecting this comparable as it has revenue from software services and products and segmental information was not available. Further, company did not respond to the notice issued u/s. 133(6) and challenged the said notice before the Hon'ble Bombay High Court. It was further objected to on the reason that company had less margin in earlier year and therefore, rejected by the department, however, margin is high in this year, the department proposed it as a comparable and there is no consistency. These objections were rejected by TPO vide his analysis in page 40 of the order and from the earnings in foreign exchange reported, TPO considered the company as involved in software development services. The same objections were reiterated before DRP, but DRP rejected.”

14.1. It was the submission of the Ld. Counsel that DRP at Hyderabad in the case of M/s. SumTotal Systems India Pvt. Ltd., [PAN: AABCC9379C] for the same assessment year has excluded the same by stating as under:

“We have gone through the submissions of the assessee, International Transactions involved, TP documentation of the Assessee, the most appropriate method adopted by TPO after rejecting the T P documentation of the Assessee, the filters used by TPO and also verified the financials of the comparables with reference to the notes on accounts & website notes. We noticed that certain notes on accounts made in certain cases do not do not match with that of the financials reported. We also noticed that meaning of the words used in the notes on accounts are not defined. Based on certain ITAT decisions, the earlier directions of this panel and other panels, the huge turnovers involved , huge brand value, their predominant presence in the market, in view of incomplete details

etc., this panel is of the view that the following comparables selected by TPO should be excluded from the list of final comparables chosen by TPO in the ALP computation.

- i)Infosys Technologies Ltd.,*
- ii)L&T Infotech Ltd.,*

We direct TPO to exclude the above referred comparables from the list of final comparables chosen by TPO in the ALP computation and re-compute the ALP accordingly”.

14.2. It was the submission that once DRP has accepted the objections of Assessee whereas in Assessee’s case DRP did not exclude L&T Infotech while excluding Infosys Technologies Ltd., it was the submission that similar facts exist for both the companies and DRP has excluded only Infosys Technologies and not L&T Infotech Ltd.,

14.3. After considering the objections of Assessee and perusing the order of DRP in the case of M/s. SumTotal Systems India Pvt. Ltd., (supra), as extracted above, we are of the opinion that this company cannot be selected as comparable by the same reasons which DRP in the above referred case accepted. Moreover, there are no segmental details and as seen from the annual report, revenues are reported from software development services and products, how much is from services and how much is from products could not be analysed. Even though TPO considered the software exports reported in earning in foreign currency as that of software development services, we are not sure whether the software exports reported therein exclusively pertain to services or products. As there are no segmental details, it is very difficult to analyse whether the incomes earned by the said company do really pertain to the similar services rendered by Assessee. As also seen from the income schedules, engineering services reported in earlier year were not there in this year, therefore, it is very difficult to analyse whether the company is functionally similar or not? Keeping in view of the above difficulties in analyzing the data and considering the reasons given by DRP in the case of M/s. SumTotal Systems India Pvt. Ltd., (supra), we are of the opinion that L&T Infotech Ltd., cannot be selected as a comparable company. AO/TPO is directed to exclude the same from the list of comparables. Ground No.4 is allowed for statistical purposes.....

22. Ground No.2 pertains to rejection of Infosys Technologies Ltd., from the list of comparables by DRP. We have already considered the opinion of DRP which is consistent not only in Assessee’s case but also in the case of M/s. SumTotal Systems India Pvt. Ltd., (supra), extracted above while considering the exclusion of L&T Infotech Ltd. Since DRP’s decision is consistent with the stand taken by the Revenue in other cases and also by the ITAT in a number of cases on reason of turnover,

brand equity, functional dissimilarity, we are of the opinion that DRP is correct in excluding the above company from the list of comparables. Therefore, there is no merit in the Revenue's ground and the same is rejected."

22. In this para, the Tribunal has reproduced the relevant portion of another Tribunal order rendered in the case of Pegasystems Worldwide India (P.) Ltd. in ITA Nos. 1758 & 1936/Hyd/2014. Thereafter in that case also, the tribunal considered another Tribunal order rendered in the case of M/s. SumTotal Systems India Pvt. Ltd. and held that this is not a good comparable because there are no segmental details and it is seen from the annual report that revenues are reported from software development services and products and how much is from services and how much is from products could not be analysed. Respectfully following this Tribunal order, we hold that in the present case, Larsen & Toubro Infotech Ltd. also cannot be considered as a good comparable.
23. In view of above discussion, we accept the assessee's claim regarding exclusion of four comparables i.e. 1) Infosys Ltd., 2) Larsen & Toubro Infotech Ltd., 3) Persistent Systems Ltd. and 4) Sasken Communication Technologies Ltd. and direct the AO/TPO to exclude these four comparables from the final list of comparables.
24. Now regarding the remaining the issue in respect of TP analysis i.e. consideration of foreign exchange fluctuation gain / loss as operating in nature for the purpose of computation of margin of the assessee as well as the comparable companies as per ground no. 11, we would like to observe that such foreign exchange fluctuation gain / loss of the tested party or of the comparables can be considered for TP analysis if such gain / loss is in respect of turnover of the present year because in TP analysis, we do not consider the absolute gain / loss only. We work out the profit percentage by dividing the operating profit by the turnover of such company and such profit percentage is compared between the tested party and of the comparable company. Hence if such foreign exchange fluctuation gain / loss of the tested party or of the comparable company is not in respect of the turnover of the present year, then such working of profit percentage will be incorrect because numerator is changed by including foreign exchange gain / loss arising in

respect of the turnover of some other year but the denominator remains same because the turnover is not related to the present year and therefore, the resultant profit percentage will be incorrect. Hence such gain / loss cannot be considered for TP analysis if such gain / loss is not in respect of turnover of the present year. Since the details in this regard is not available and there is no finding of any of the authorities below in this regard, we feel it proper to restore the matter back to the file of AO / TPO for fresh decision with the direction that if it is found that foreign exchange fluctuation gain / loss of the tested party i.e. of the assessee or of the comparable companies is in respect of the current year's turnover then the same should be considered for TP analysis but if such gain / loss is not in respect of current year's turnover, then the same should be ignored in case of both i.e. the tested party and of the comparable companies. In case the data in this regard regarding comparable company is not made available by the assessee, then it should be presumed that such foreign exchange gain / loss for comparable company is not in respect of current year's turnover because generally, the accounting of foreign exchange gain / loss is considered in the sales only if such gain / loss has been received in the year of sale itself and only when such gain / loss is received and accounted for in a later year then only the same is accounted for separately as exchange fluctuation gain / loss. Accordingly, ground no. 11 is allowed for statistical purposes. The AO/TPO should decide this issue as per above discussion after providing adequate opportunity of being heard to assessee.

25. Regarding ground no. 13 of assessee's appeal in respect of working capital adjustment, reliance has been placed on two Tribunal orders rendered in the case of Apigee Technologies (India) (P.) Ltd. Vs. JCIT as reported in [2015] 63 taxmann.com 129 (Bangalore-Trib.), copy available on pages 85 to 96 of the case law paper book and in the case of DCIT Vs. Goldman Sachs Services (P.) Ltd. as reported in [2017] 82 taxmann.com 380 (Bangalore-Trib.), copy available on pages 97 to 108 of the case law paper book. In case of Apigee Technologies (India) (P.) Ltd. Vs. JCIT (supra), it was held by the Tribunal in para 19 of the Tribunal order that the claim of the assessee for providing working capital adjustment is to be upheld and AO/TPO is directed

to work out the same. In the case of DCIT Vs. Goldman Sachs Services (P.) Ltd. (supra), the issue regarding working capital adjustment is discussed by the Tribunal in para 4 of this Tribunal order which is available on page no. 99 of the case law paper book. The same is reproduced hereinbelow for ready reference.

“4. We have heard the Id. DR as well as Id. AR and considered the relevant material on record. At the outset we note that an identical issue has been considered by this Tribunal in assessee's own case for the assessment year 2010-11 vide order dated 06.01.2017 in IT(TP) Nos. 267 & 222/Bang/2015 in para 10 as under:

"10, The next issue is On the Working Capital Adjustment : The Revenue objected to the restriction of working capital adjustment to the 1.01% as against the actual working capital adjustment carried out by TPO at 2.23%, The TPO has in principle agreed to the claim of the assessee for granting the working capital adjustment and has consequently granted the same. However, it is seen that the working capital adjustment was restricted to 1.01% which is the average cost of capital of the comparable companies selected by the TPO, In this regard, the DRP held as under:

We have considered the submissions of the assessee as well as the reasons of the TPO. The argument propounded by the TPO that the average cost of comparables should provide the upper cap on the working capital adjustment is not the correct position. This implies that the average working capital of the industry is being forced upon the assessee and in other words the assessee is being asked to keep the debtors, inventory and creditors at a fixed level, defined by the level of such capital of the comparables. This would mean that the TPO is forcing the assessee to fund its working capital requirements in a specific way which is not the domain of the TPO, Another argument of the TPO is that since the debtors and inventory are zero, no adjustment should be carried out by considering only the position of creditors. In this regard we find ourselves in agreement with the contention of the assessee that the rationale of time value of money will equally apply to the creditors and consequently wherein any entity making payment in advance towards future services would expect compensatory returns towards the timing effect. Therefore, the action of keeping a cap on the working capital adjustment by the TPO is not approved. The Assessing officer is directed to carryout the working capital adjustment as per the actual figures and not apply any cap. We issue the directions accordingly.

As regards the request for risk adjustment it is noted that it involves two vital preconditions, they are that difference in the risk level exists between the tested party and the uncontrolled comparables

and that it is possible to calculate in terms of numbers the differential risk so that adjustment can be made but in the case of the taxpayer both the prerequisite conditions are missing. Further, when the average margin of the comparable companies are taken, it takes care of the differences if any in the comparable companies. Therefore, there is no rationale in allowing the risk adjustment. The objection is therefore not found acceptable."

The assessee relied on the decision of this Tribunal in Moong Controls India (P.) Ltd. ITA 551/Bang/2015 AY 2010 dt 27.11.2015, wherein this Tribunal directed the TPO to allow actual adjustment towards the differences in the of working capital position between the assessee and the entrepreneurial companies selected as comparable. We direct the TPO to follow this decision. Thus, Revenue's appeal ground nos. 5 & 6 are dismissed"

26. From the above para reproduced from this Tribunal order, it is seen that in this case, the Tribunal has given a direction to the AO to carry out the working capital adjustment as per the actual figures and not to apply any cap. In the present case also, we restore the matter back to the file of AO/TPO to work out the working capital adjustment on actual figure without applying any cap. This ground is allowed for statistical purposes.
27. In the result, the assessee's appeal stands disposed of in the terms indicated above.
28. Now we take up the revenue's appeal for Assessment Year 2011-12. As per this appeal of revenue, the revenue has one grievance regarding corporate tax issue and it was agreed by both sides that this issue is identical with similar issue raised by revenue in Assessment Year 2010-11 and same can be decided on same line in Assessment Year 2011-12 also. This issue was decided against revenue and in favour of assessee by respectfully following the judgment of Hon'ble Karnataka High Court rendered in the case of CIT Vs. Tata Elxsi Ltd. (supra). On the same line, in the present year also, this issue is decided against revenue and in favour of the assessee on similar line.
29. In addition to this, the grievance of the revenue is regarding direction of Id. CIT(A) to exclude two comparables i.e. Tata Elxsi Ltd. and ICRA Techno Analytics Ltd. For exclusion of both these comparables i.e. Tata Elxsi Ltd. and ICRA Techno Analytics Ltd., reliance has been placed on the Tribunal order rendered in the case of AMD India P. Ltd. vs. ACIT (supra), copy

submitted and kept on record. It was submitted that the relevant finding of the Tribunal on this issue is available on page nos. 25 and 32 of this Tribunal order which is for the same Assessment Year i.e. Assessment Year 2011-12. The Id. DR of revenue supported the order of TPO.

30. We have considered the rival submissions. We find that the Tribunal has reproduced the relevant portion of earlier Tribunal order rendered in the case of DCIT vs. Electronics for Imaging India (P.) Ltd. in IT(TP)A No. 212/Bang/2015. Regarding ICRA Techno Analytics Ltd., it was held by Tribunal in that case that this company is engaged in diversified activities of software development and consultancy, engineering services, web development & hosting and substantially diversified itself into domain of business analysis and business process outsourcing, and therefore, this cannot be regarded as functionally comparable with that of assessee who is rendering software development services to its AE and on this basis, it was held that ICRA Techno Analytics Ltd. is not a good comparable. Regarding Tata Elxsi Ltd., the Tribunal has followed the decision of Bombay Bench of the Tribunal rendered in the case of Telcordia Technologies Pvt. Ltd. Vs. ACIT (supra) and the Tribunal order rendered in the case of DCIT vs. Electronics for Imaging India (P.) Ltd. (supra). As per the relevant portion of that Tribunal order rendered in the case of DCIT vs. Electronics for Imaging India (P.) Ltd. (supra) reproduced by the Tribunal, it is noted in that case that this company is engaged in various diversified activities including product design service, innovation design, engineering service, visual computing labs etc. and in the case of Telcordia Technologies Pvt. Ltd. Vs. ACIT (supra), it is noted by the Tribunal that this comparable i.e. Tata Elxsi Ltd. is engaged in development of niche product and development services which is entirely different from the assessee company, engaged in software development services and respectfully following this Tribunal order rendered in the case of DCIT vs. Electronics for Imaging India (P.) Ltd. (supra), it was held by the Tribunal that there is no error or illegality in the direction of DRP to exclude this company from the set of comparables. In the present case also, no difference in facts could be pointed out by Id. DR of revenue and therefore,

respectfully following this Tribunal order, we hold that there is no error or illegality in the order of Id. CIT(A) on this issue.

31. In the result, the appeal of the revenue for Assessment Year 2011-12 is also dismissed.
32. In the combined result, both the appeals filed by the revenue are dismissed and the appeal of the assessee is allowed in the terms indicated above.

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 31st July, 2019.
/MS/

Copy to:

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

By order

Assistant Registrar,
Income Tax Appellate Tribunal,
Bangalore.