

आयकर अपीलीय अधिकरण "सी" न्यायपीठ पुणे में ।
IN THE INCOME TAX APPELLATE TRIBUNAL "C" BENCH, PUNE

BEFORE SHRI R.S.SYAL, VP AND
SHRI PARTHA SARATHI CHAUDHURY, JM

आयकर अपील सं. / ITA No.189/PUN/2014

निर्धारण वर्ष / Assessment Year : 2009-10

BMC Software India Private Limited,
Tower A, ICC Tech Park,
Senapati Bapat Road,
Pune-411 016.
PAN : AABCB6110E

.....अपीलार्थी / Appellant

बनाम / V/s.

The Deputy Commissioner of Income Tax,
Circle 1(1), Pune.

.....प्रत्यर्थी / Respondent

Assessee by : Shri Madhur Agarwal

Revenue by : Shri Neeraj Bansal, CIT &
Shri Mugda Sardeshmukh, JCIT

सुनवाई की तारीख / Date of Hearing : 21.08.2019

घोषणा की तारीख / Date of Pronouncement : 22.08.2019

आदेश / ORDER

PER PARTHA SARATHI CHAUDHURY, JM :

This appeal preferred by the assessee emanates from the directions of the Ld. Dispute Resolution Panel (DRP) dated 30.10.2013 for the assessment year 2009-10 as per the grounds of appeal on record.

2. At the outset, the Ld. Counsel for the assessee submitted that broadly transfer pricing issue in this case relates to “**Software Development**” and “**ITes Services**”. The Ld. Counsel invited our attention to the facts of the case enshrined at Page 2 of the TPO’s order at Para 5 that BMC India is engaged in providing software development services and sales support services to BMC-US, BMC software Inc., which is a company based in Houston, Texas, US. BMC India solely engaged in providing software development services, ITes and sales support services to BMC group entities. BMC India can be classified as a captive software development service provider and a sales support service provider. BMC India provides software development services, ITes and sales support services to BMC, US on cost plus a margin of 10%. For the purpose of benchmarking its international transactions assessee has followed TNMM with external comparables and with operating profit over total cost as profit level indicator (PLI).

Having given this background facts, the Ld. Counsel for the assessee submitted that with regard to “**Software Development**”, if three companies i.e. (i) Bodhtree Consulting Ltd. (ii) KALs Information Technology Systems Ltd. and (iii) Infosys Technologies Ltd. are excluded from the final list of comparables then they will be in house and their grievance would be satisfied.

SOFTWARE DEVELOPMENT SERVICES SEGMENT

(A) Bodhtree Consulting Ltd. The assessee has objected to the inclusion of this company as comparable. The assessee has stated that this company is functionally different as it is a software solution company as well as it has service offerings and no revenue break up is available. The assessee has

further stated that it is a super profit company and also that its turnover for F.Y.2008-09 is Rs.17.4 Crores which is below the turnover range selected by the assessee.

3. The Ld. Counsel for the assessee submitted that in assessee's own case in ITA No.2549/PUN/2012 for the assessment year 2008-09 dated 19.08.2019, the Tribunal has decided Bodhtree Consulting Ltd. to be excluded from the list of companies by observing as under:

“(i) Bodhtree Consulting Ltd. :

8.1. *The TPO treated Bodhtree Consulting Ltd. as one of the comparables. The assessee objected to its inclusion on the ground of functional dissimilarity, extraordinary financial events and fluctuating profit margins. The TPO rejected the assessee's contention of business restructuring during the year and also held the same to be functionally similar inasmuch as it was having only one identifiable reportable segment of 'Software development services'. The assessee is aggrieved by the inclusion of this company in the final list of comparables.*

8.2. *We find from the Annual report of this company that it: "has only one segment, namely, Software development. Being a software solutions company, which is engaged in providing open and end-to-end web solutions, software consultancy, design and development of solutions, using the latest technologies." Thus, it can be seen that this company is providing end-to-end solutions and also consultancy, which is not the case with the assessee company.*

8.3. *The ld. AR submitted that Bodhtree Consulting Ltd. cannot be considered as comparable because of a different model of revenue recognition. He invited our attention towards the Annual report of this company, in which it has been specifically reported under the head 'Revenue recognition', that: "Revenue from software development is recognized based on software developed and billed to clients." The ld. AR submitted that the costs incurred by this company in respect of the projects pending completion at the end of the year are booked at the time of incurring, but, the income is recognized on the raising of bills, thereby distorting the figure of operating profit for a particular year. In contrast to that, the ld. AR submitted that the assessee was recognizing revenue from software development side by side without waiting for the completion of the project.*

8.4. *Ordinarily, if some software development project is incomplete at the end of the year, there may arise two situations, viz., the first, in which the expenses incurred in respect of such software development may be capitalized, which appears to be a more rational manner of depicting the true and fair view of the profitability of the enterprise; and the second, in which such expenses may be straightway taken as revenue costs for the year of its incurring itself, which may not reflect a true and fair view of the profits on year to year basis. The contention of*

the ld. AR is that whereas Bodhtree falls into the second situation, the assessee falls in the first. Though the contention that Bodhtree was accounting for expenses in the year of incurring but considering income only on the conclusion of the project in the subsequent year sounded a little awkward, we attempted to find out the amount of capitalized expenses in respect of incomplete projects at the end of the year. Ex facie, we could not find out any such capitalized value of work-in-progress in the balance sheet of the company on standalone basis nor the ld. DR could point out any. This prima facie shows that the expenses incurred in respect of incomplete projects of software development at the end of the year, but billed in the subsequent year, were, in fact, treated as expenses for the current year alone. In the same manner, expenses incurred in the preceding year(s) for the contracts of software development remaining incomplete at the end of the year also must have been included in the expenses of the last year(s) alone, but, the income got recognized on the raising of bills in the current year.

8.5. Under the mercantile system of accounting, income is recognized at the time of its accrual and the expenses become deductible when liability to pay is incurred. The dates of actual payment of expenses or receipt of income become insignificant. This is also called 'Matching concept', as per which income is recognized with the incurring of expenses. To put it simply, if income does not accrue from a particular transaction, the expenses incurred for such transaction are excluded from the Trading and Profit & loss account by taking them to Balance sheet. To illustrate, if there is an incomplete contract worth Rs.100 for doing a particular work, and the assessee has incurred Rs.60 on this project till the close of the year, but the income is to be recognized only on the completion of the project, an event to take place in the subsequent year, then, the amount of Rs.60 is not considered as expenditure for the year, but is taken to the Balance sheet as closing work-in-progress, which becomes opening work-in-progress for the subsequent year and the income is finally computed from such project/contract in the next year on the raising of bill of Rs.100/- after allowing deduction for the expenses incurred in the earlier year at Rs. 60 and the further expenses incurred in the year of raising of the bill. In this way, profit for the earlier year in which expenses of Rs.60 were incurred and the next year in which bill is raised for Rs.100 on completing the work, gives true and fair view of the profitability of that enterprise for both the years. If an enterprise, instead of capitalizing Rs. 60 in the first year, claims deduction in the year of incurring itself but recognizes income of Rs.100 in the next year, then profit of both the years, will not give a fair view. Bodhtree is following the model of booking expenses at the time of their incurring notwithstanding the raising of bills in next year. This shows that the revenue recognition model of Bodhtree Consulting Ltd. is quite different from the assessee in as much as unless the software is fully developed and billed, it will go on debiting expenses to the Profit and loss account but the invoice will be raised only in the year of completing the project. This leads to fluctuating margins from year to year. The Hon'ble Gujarat High Court in Pr. CIT Vs. Allscripts (India) Private Ltd. (2016) 288 CTR 675 (Gujarat) considered the fluctuating margins of this company from the F.Ys. 2005-06 to 2012-13 which have been tabulated in para 6 of the judgment, viz., 13.87%, 80.15%, 19.89%, 62.27%, 33.42%, (-) 4.46%, 3.29% and (-)11.53%. Considering the fluctuating profit margins based on an altogether different revenue recognition model, the Hon'ble High Court upheld the exclusion of this company from the list of comparables. Respectfully following the precedent, we order to delete this company from the list of comparables."

We have perused the aforesaid order of the Co-ordinate Bench of the Tribunal, Pune and gone through the Annual Report of the company. We are in conformity with our findings given in assessee's own case hereinabove stated and hold that "Bodhtree Consulting Ltd." should be deleted from the final list of comparables.

(B) KALS Information Technology Systems Ltd. : The Transfer Pricing Officer (TPO) accepted this company as comparable. The assessee objected this company to be taken as comparable as it is functionally different since it is engaged in sale of software products and not software services. The assessee has cited Bangalore ITAT judgment in the case of Bindview India Pvt. Ltd. Vs. DCIT wherein KALS Information Technology Systems Ltd. was held to be not comparable to Bindview as the former is engaged in software product development as well as provides IT enabled services and no revenue break up for these respective business activities is available. However, both the TPO/ DRP as per reasons appearing in their respective order have held this company to be comparable company with that of the assessee.

4. The Ld. Counsel for the assessee referred to the Tribunal's order in assessee's own case for the assessment year 2008-09 (supra.) at page 17, Para 12.1 to 12.2 of the order wherein the Tribunal has held as follows:

“(v) KALS Infosystems Ltd. :

12.1. The TPO proposed to include this company in the list of comparables. The assessee objected to the same by contending that it was functionally different as also engaged in Software products. The TPO rejected the assessee's contention by observing that nothing was mentioned in the Annual Report of the company about the sale of products. The DRP upheld the action of the AO in the draft order, incorporating the inclusion of this company in the final set of comparables by the TPO. Aggrieved thereby, the assessee is in appeal before the Tribunal.

12.2. We have heard both the sides and gone through the relevant material on record. We have perused the Annual report of this company, a copy of which is available in the paper book. Note no.1 to the Notes to the Financial statements provides background of this company by stating that: "The company is engaged in Development of Software and Software products since its inception. The company consisting of STPI unit engaged in Development of Software and Software products and a Training Centre engaged in training of Software professionals on online products.' Segmental information has been given at page 19 of the Annual Report, which shows segmental revenues from "Application Software" and "Training". Profit and loss account of this company has been set out at page 14 of the Annual Report. First item under the head "Income" is "Sales, Services & Training" with the figure of Rs.2,19,82,589/-. Break-up of this amount has been given in Schedule No.12 showing 'Income from Software Development – Export' – Rs.2,05,40,685/-; 'Translation and Interpretation' – Rs.5,07,985/-; and 'Training receipts' – Rs.9,33,919/-. Under the head "Operating Expenses", an item worth Rs.27,19,495/- has been shown with narration of "Software Consumption from Inventory". Balance sheet of this company shows 'Inventories' at Rs.85,77,723/-. The above information clearly deciphers that Kals Information Technology Systems Ltd. is not only engaged in providing Software Development Services but is also dealing in Software products under the relevant segment. As the assessee is not engaged in the business of Software products but is rendering only Software services on captive basis, in our considered opinion, this company cannot be considered as comparable. The Hon'ble jurisdictional High Court in CIT vs. PTC Software (I) Pvt. Ltd. (2017) 395 ITR 0176 (Bom) has held that a Software product company cannot be compared with a company providing software services. As Kals Information Technology Systems Ltd. is engaged in selling of software products which is different from the activities undertaken by assessee, namely, rendering of software service only to its AEs, we hold the same to be incomparable and accordingly direct to exclude it from the final list of comparables."

Respectfully following our above referred decision for assessment year 2008-09, we direct "KALS Information Technology Systems Ltd." to be excluded from the final list of comparables as regards the assessee.

(C) Infosys Technologies Ltd. : It is claimed by the assessee that this company should be rejected due to very high turnover, super profit making company and significant intangible assets.

5. The Ld. Counsel for the assessee for this proposition has placed reliance on the decision in the case of M/s. Siemens Industry Software (I) P. Ltd. Vs. DCIT, Circle 8(1), New Delhi in ITA No.1307/Del/2014 for the

assessment year 2009-10 wherein the Delhi Bench of the Tribunal has categorically observed that on account of very high turnover of the Infosys Technologies Ltd., it is not matched to the assessee along with research, development and other factors. Therefore, this company was excluded from the final list of comparables for benchmarking international transaction.

5.1 That in another case of Delhi Bench of the Tribunal in ITA No.410/Del/2013 for assessment year 2008-09 and in ITA No. 1484/Del/2014 for the assessment year 2009-10, the Delhi Bench of the Tribunal has held that Infosys Technologies Ltd. was taken as comparable by the TPO/DRP to which the assessee has objected. It was analyzed by the Tribunal that this comparable have been excluded by the Tribunal even in assessment year 2006-07 which was even confirmed by the Hon'ble Delhi High Court. Similarly in the assessment year 2008-09, this company was excluded from the final list of comparable as per reasons given by the Delhi Bench of the Tribunal. That on the same reasons in the current year i.e. assessment year 2009-10, Infosys Technologies Ltd. was excluded from the final list of comparables while determining the international transaction.

6. We have perused the judicial pronouncements placed before us of the Co-ordinate Bench of the Tribunal, Delhi and also perused the Annual Report of the Company i.e. Infosys Technologies Ltd. We agree with the reasoning put forth by the Co-ordinate Bench of the Tribunal, Delhi for exclusion of this company from the final list of comparables and similarly in the case of assessee also, there is no match as compared to Infosys Technologies Ltd. with regard to huge turnover, R & D and other factors. Accordingly, we direct for exclusion of Infosys Technologies Ltd. from the final list of comparables.

ITES SERVICES SEGMENT

7. The second set of arguments of the Ld. Counsel for the assessee was with regard to “**ITes Services**”. It is the contention of the assessee that they are only doing paper work processing and back office services once the sale is done or the procurement is completed. In TP study report, the assessee has taken five comparables out of which the TPO rejected three comparables and added more five comparables which is placed at Page 59 of the TPO’s order. The DRP has confirmed the same.

The argument of the Ld. Counsel was that if three companies i.e. (i) Accentia Technologies Ltd. (ii) Cosmic Global Limited and (iii) Eclerx Services Limited are excluded from the final set of comparables of “**ITes Services**”, they will be in house and their grievance would be satisfied.

(D) Accentia Technologies Ltd. : The TPO accepted this company as comparable. The assessee objected to it on various grounds. The basic objection is that this company is engaged in providing Healthcare Receivable Cycle Management Services and Software products for business process outsourcing and is therefore, engaged in providing KPO services which are dissimilar to the BPO services provided by the assessee.

Both the TPO/DRP have taken this company as comparable. Rather DRP has held that KPO services form a sub-set of the larger set of BPO services and hence, are similar.

8. The Ld. Counsel for the assessee invited our attention to the decision of the Hon’ble Bombay High Court in the case of The Pr. Commissioner of

Income Tax-2, Pune Vs. PTC Software (I) Pvt. Ltd., Income Tax Appeal No. 598 of 2016 wherein the Hon'ble High Court has observed and held as follows:

"5. Re Question (c) :-

(i) The impugned order of the Tribunal has excluded M/s. Accentia Technologies Ltd., from the list of comparable to determine the ALP of the Respondent's transactions.

(ii) The impugned order renders findings of fact that the nature of activities carried out by M/s. Accentia Technologies Ltd. are different from that carried out by Respondent. M/s. Accentia Technologies Ltd. develops its own software and rendered Medical transcription services while the Respondent is providing BPO services. Besides, the impugned order of the Tribunal held that high profit margins of M/s. Accentia Technologies Ltd. was attributable to amalgamation which took place in the previous years relevant to subject assessment year. Therefore, not comparable.

(iii) In fact, this Court in CIT Vs. Aptara Technology Ltd. (Income Tax Appeal No. 1209 of 2015) has upheld the view of the Tribunal in not accepting the Accentia Technologies Ltd. as comparable inter alia on account of fact that extra ordinary event such as merger/ amalgamation would affect the profitability of M/s. Accentia Technologies Ltd., thus, making it comparable.

(iv) Further in that case, as in this case, the Tribunal has also recorded a finding of fact that the activities of M/s. Accentia Technologies Ltd., and the Respondent are different. Thus, not comparable. The above finding of fact is not shown to be perverse.

(v) In the above view, the question as proposed does not give rise to any substantial question of law. Thus, not entertained."

Therefore, M/s. Accentia Technologies Ltd. develops its own software and rendered Medical transcription services which is different from BPO services and hence, it was held that this company was not comparable.

9. Reverting to the facts of the present case and analyzing the Annual Report of the Company vis-à-vis M/s. Accentia Technologies Ltd., we find that they are functionally substantially different and as held by the Hon'ble Bombay High Court that KPO services are not same as BPO services and hence, cannot be held to be comparable. Respectfully following the ratio laid

down by the Hon'ble Bombay High Court, we hold this company to be excluded from the final list of comparables.

(D) Cosmic Global Limited : The assessee has objected on inclusion of this company on the grounds that exceptionally high margins were earned by this company during the year as compared to the trend in other years. Moreover, it is argued that this company should be rejected as a super normal profit making company. The assessee further contended that this company outsources significant portion of its work to outside vendors and is hence not comparable.

10. The Ld. Counsel for the assessee has placed reliance on the decision of the Hon'ble Bombay High Court in the case of The Pr. Commissioner of Income Tax-2, Pune Vs. PTC Software (I) Pvt. Ltd. (supra.) wherein it has been categorically held by the Hon'ble Bombay High Court that Cosmic Global Ltd. had outsourced its services to vendors and therefore, Cosmic Global Ltd. is not functionally comparable and therefore, could not be included amongst the comparables to determine the ALP of the assessee's transactions. The Hon'ble Jurisdictional High Court has held as follows:

“(II) Cosmic Global Ltd.

(i) The impugned order of the Tribunal records the fact that Cosmic Global Ltd. had outsourced its services to vendors just as M/s. Vishal Technologies Ltd. had done. In the above facts, the impugned order held that Cosmic Global Ltd. is not functionally comparable and therefore, could not be included amongst the comparable to determine the ALP of the Respondent's transactions.

(ii) The aforesaid finding of fact by the Tribunal has not been shown to be perverse. In fact, the reasons indicated in the impugned order to hold that Vishal Technologies Ltd. is not a comparable, would equally apply to Cosmic Global Ltd.

(iii) Thus, the sub question (II) as proposed does not give rise to any substantial question of law. Thus, not entertained.

(III) Accordingly, the question as proposed does not give rise to any substantial question of law. Thus, not entertained.”

11. We have perused the judicial pronouncements placed before us and relevant material on records along with Annual Report of the Company i.e. Cosmic Global Ltd. We find that there is substantially outsourcing work conducted by this company. Respectfully following the decision of the Hon'ble Bombay High Court, we direct the Assessing Officer to exclude this company from the final list of comparables while benchmarking the international transaction of the assessee.

(E) Eclerx Services Limited : The TPO has adopted this company as comparable. The assessee has objected to the TPO's stand on several grounds. The basic ground of objection is that this company had an exceptional year of operations as it has experienced exceptional performance reflecting in higher margins. It has also been argued that this company is a super profit making company and is also functionally different being a KPO company engaged in providing data analytics and data processing solutions.

12. The Ld. Counsel for the assessee has placed reliance on the decision of the Hon'ble Bombay High Court in the case of The Pr. Commissioner of Income Tax-2, Pune Vs. PTC Software (I) Pvt. Ltd. (supra.) wherein the Hon'ble Bombay High Court has held as follows:

“6. Re. Question (d) :-

(i) The impugned order of the Tribunal held that Exlerx Services Ltd. is not a comparable to the Respondent-Assessee for the reasons that it was providing knowledge process outsourcing (KPO)-whereas Respondent is engaged in BPO services.

(ii) The impugned order of the Tribunal place reliance upon the Special Bench of the Tribunal in the case of Maersk Global Centres (India) Pvt. Ltd. (Income Tax Appeal No.7466/Mum/2012), to hold that Exlerx Services Ltd. was engaged in providing KPO services which is distinct

from the BPO services. Thus, excluded the same from the list of comparables.

(iii) The impugned order of the Tribunal, in fact, relies upon the following extract in the Special Bench's decision of the Tribunal in *Maersk Global Centres (India) Pvt. Ltd.*, as under:-

"Keeping in view the nature of services rendered by Exlerx Services Ltd. and its functional profile, we are of the view that this company is also mainly engaged in providing high end services involving specialized knowledge and domain expertise in the field and the same cannot be compared with the assessee company which is mainly engaged in providing low end services to the group concerns."

(iv) Although both are providing ITES services by virtue of that alone, both units will not become comparable as observed by this Court in *Pr. CIT Vs. Aptara Technology Pvt. Ltd.* (Income Tax Appeal No.1209 of 2015) rendered on 26th March, 2018-as follows:- 'merely because the tested party and the comparable provide ITES, they do not become comparable. The content of the services rendered by virtue of IT is to be examined before holding it to be comparable'.

(v) Further our attention is invited to the decision of the Delhi High Court in *Rampgreen Solutions P. Ltd. Vs. CIT*, 377 ITR 533 wherein Delhi High Court held that KPO services could not be compared to call centre services, although both would fall under the umbrella of ITES. Therefore,, the functions of two cannot be considered to be similar for the purpose of being comparable.

(vi) In the above view, this question also does not give rise to any substantial question of law. It is essentially a finding of fact which is not shown to be perverse. Thus, not entertained."

Respectfully following the aforesaid decision of the Hon'ble Jurisdictional High Court, we direct the Assessing Officer to exclude this company from the final list of comparables.

13. In view of our forgoing discussion, we set aside the impugned order and remit the matter of determination of ALP of Software development and ITes services afresh by the AO/TPO in accordance with law. Needless to say, AO/TPO shall grant reasonable opportunity of hearing to the assessee in compliance with the principle of natural justice.

14. In the result, appeal of the assessee is allowed for statistical purposes.

Order pronounced on 22nd day of August, 2019.

Sd/-
R.S.SYAL
VICE PRESIDENT

Sd/-
PARTHA SARATHI CHAUDHURY
JUDICIAL MEMBER

पुणे / Pune; दिनांक / Dated : 22nd August, 2019.

SB

आदेश की प्रतिलिपि अग्रेषित / Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant.
2. प्रत्यर्थी / The Respondent.
3. The CIT(Appeals)-13, Pune
4. The Pr. CIT-5, Pune.
5. विभागीय प्रतिनिधि , आयकर अपीलीय अधिकरण, "सी" बेंच,
पुणे / DR, ITAT, "C" Bench, Pune.
6. गार्ड फ़ाइल / Guard File.

// True Copy //

आदेशानुसार / BY ORDER,

निजी सचिव / Private Secretary
आयकर अपीलीय अधिकरण, पुणे / ITAT, Pune.

		Date	
1	Draft dictated on	21.08.2019	Sr.PS/PS
2	Draft placed before author	22.08.2019	Sr.PS/PS
3	Draft proposed and placed before the second Member		JM/AM
4	Draft discussed/approved by second Member		AM/JM
5	Approved draft comes to the Sr. PS/PS		Sr.PS/PS
6	Kept for pronouncement on		Sr.PS/PS
7	Date of uploading of order		Sr.PS/PS
8	File sent to Bench Clerk		Sr.PS/PS
9	Date on which the file goes to the Head Clerk		
10	Date on which file goes to the A.R		
11	Date of dispatch of order		