

**IN THE INCOME TAX APPELLATE TRIBUNAL
“C” BENCH : BANGALORE**

**BEFORE SHRI N. V. VASUDEVAN, VICE PRESIDENT AND
SHRI B. R. BASKARAN, ACCOUNTANT MEMBER**

IT(TP)A No.979/Bang/2016
Assessment year : 2010-11

M/s. Nvidia Graphics Pvt. Ltd., C1 – “Jacaranda”, Wing A, Manyata Embassy Business Park, Outer Ring Road, Bengaluru – 560 045. PAN : AABCN 9200 H	Vs.	Commissioner of Income-tax (Appeals) - 5, Bengaluru.
APPELLANT		RESPONDENT

IT(TP)A No.1090/Bang/2016
Assessment year : 2010-11

Jt. Commissioner of Income-tax, Circle 5(1)(1), Room No.233, 2 nd Floor, BMTC Complex, 80 Feet Road, Koramangala, Bengaluru – 560 095.	Vs.	M/s. Nvidia Graphics Pvt. Ltd., Bengaluru – 560 045. PAN : AABCN 9200 H
APPELLANT		RESPONDENT

Assessee by	:	Shri. Chavali Narayan, CA
Revenue by	:	Shri. Pradeep Kumar, CIT-DR(ITAT)(Bengaluru)

Date of hearing	:	10.10.2019
Date of Pronouncement	:	16.10.2019

ORDER

Per N. V. Vasudevan, Vice President:

ITA No.979/Bang/2016 is an appeal by the assessee while ITA No.1090/Bang/2016 is an appeal by the Revenue. Both these appeals are directed

against the order dated 29.06.2016 of CIT(A)-5, Bengaluru, relating to Assessment Year 2010-11. The issue that arises for consideration in the appeal by the assessee and ground Nos. 3 and 4 raised by the Revenue in its appeal relate to the determination of Arms Length Price (ALP) in respect of international transaction entered into between the assessee and its AE. Ground Nos.3 & 4 raised by the Revenue in its appeal reads as follows:

“3. Whether in the facts and circumstances of the case and in law, the Hon’ble CIT(A) was justified in seeking exact comparability while searching for comparable companies of the Assessee under TNMM method whereas requirement of law and international jurisprudence require seeking similar comparable companies.

4. Whether the Hon’ble CIT(A) was right in not accepting the quantitative filters and qualitative filters of the TPO and applied functional matrix which is narrower than the functionality matrix originally used by TPO.”

2. The assessee is a subsidiary of NVIDIA International Inc. ("NVIDIA International") US. The Assessee provides software development services to NVIDIA International, from its Bangalore, Pune and Hyderabad facilities. The assessee is compensated on a cost-plus mark-up basis for the provision of software development services to NVIDIA International. The learned AO made reference u/s 92CA(1) of the Income Tax Act, 1961 ('Act') to the Joint Commissioner of Income Tax (Transfer Pricing)-II ("Transfer Pricing Officer- or "TPO") for determination of ALP of the international transaction entered by the assessee with its Associated Enterprises ("AEs"). The TPO passed an order dated 30 January 2014 u/s 92CA of the Act making an adjustment INR 136221,840 for software development services transaction.

3. Net margin on cost earned by the Assessee as computed by the TPO in the TP Order for software development services (treating forex gain/ loss as non-operating):

Operating Revenue	Rs.2,095,934,216/-
Operating Expenses	Rs.1,871,515,097/-
Operating Profit (Op. Income —Op. Cost)	Rs.224,419.119/-
Operating profit on cost (OP/OC)	12%

4. Comparison of the TP study done by the Assessee and TPO:

Particulars	Assessee	TPO
Methodology adopted	TNMM	TNMM
Profit Level Indicator (PLI)	OP/TC	OP/TC
Database used	PROWESS & CAPITALINE PLUS	PROWESS & CAPITALINE PLUS
Comparables selected	21	14

5. Comparable companies ultimately selected by TPO and their arithmetic mean:

Sl. No.	Comparable	Margin (Unadjusted)	Margin (adjusted)
1.	Infosys Technologies Limited	45.01%	43.88%
2.	Larsen & Toubro Infotech Limited	19.33%	19.13%
3.	LGS Limited	11.95%	7.42%
4.	Mindtree Limited (Seg)	14.83%	14.45%
5.	Persistent Systems Private Limited	30.35%	29.21%
6.	RS (Software) India Limited	10.29%	9.96%
7.	Sasken Communication Technologies Limited	17.36%	17.17%
8.	Thinksoft Global Services Limited	17.05%	15.60%
9.	Zylog Systems Limited	19.06%	15.69%
10.	Evoke Technologies Private Limited	18.75%	18.14%
11.	e-Zest Solutions Limited	16.79%	13.86%
12.	Kals Information Systems Limited	38.37%	34.10%
13.	Persistent Systems & Solutions Ltd	15.38%	11.88%
14.	Tata Elxsi	21.88%	19.35%
Arithmetic Mean		21.17%	19.27%

6. The TPO computed the ALP in the following manner:

Arm's Length Mean Margin	21.17%
Less: Working Capital Adjustment	1.90%
Adjusted mean margin of the comparables	19.27%
Operating Cost	Rs.187,15,15,097
Arm's Length Price (ALP) 119.27% of OC	Rs.223,21,56,056
Price Received	Rs.209,59,34,216
Short fall being adjustment u/S. 92CA	Rs.136,62,21,840

7. The aforesaid sum suggested as addition on account of determination of ALP by the TPO was incorporated by the AO in the draft order of assessment passed by him and further in the final order of assessment, as the Assessee did not propose to file objections to the Dispute Resolution Panel (DRP) against the proposed addition in the draft assessment order.

8. The Assessee preferred appeal before CIT(A) against the addition made in the final assessment order on account of determination of ALP. On appeal by the assessee, the CIT(A) rejected 3 comparables (Tata Elxsi, Infosys Technologies Limited & Kals Information System Limited (Seg)) based on functionally different criteria based on the ITAT order for AY 2009-10 in the assessee's own case. The CIT(A) directed the AO/TPO to treat the foreign exchange fluctuation as operating in nature, while computing the operating margin of the Assessee as well as the comparable companies, as it has direct nexus with the business of the assessee. The CIT(A) directed AO/TPO to consider corrected receivable/payable figures for assessee and comparable companies and also directed re-computation of margins for certain comparable companies which were erroneously computed by the TPO. The assessee argued

for inclusion of certain companies forming part of TP documentation which was rejected by the CIT(A) on the following reasons:

SI No.	Comparable	Reason for rejection by CIT(A)
1.	Akshay Software Technologies Limited	The CIT(A) has rejected this company on the basis of functional difference (<i>page 23-25 of the CIT(A) order</i>)
2.	CG-VAK Software & Exports Limited	The CIT(A) has rejected this company on the basis of failing employee cost filter of 25% (<i>page 25-27 of the CIT(A) order</i>)
3.	Goldstone Technologies Limited	The CIT(A) has rejected this company on the basis of lack of segmental information (<i>page 27-28 of the CIT(A) order</i>)
4.	Helios and Matheson Information Technology Limited	The CIT(A) has rejected this company on the basis of different financial year end filter and functional difference (<i>page 19-20 of the CIT(A) order</i>)
5.	Quintegra Solutions Limited	The CIT(A) has rejected this company on the basis of lack of segmental information and extraordinary fluctuation in profits (<i>page 28-29 of the CIT(A) order</i>)

9. The assessee is aggrieved by the inclusion of certain companies in the list of comparable companies retained by the CIT(A) and is therefore in appeal before the Tribunal. The assessee has raised the following additional grounds for consideration by this Tribunal. The additional grounds reads as follows:-

“That the learned AO/ TPO failed to appreciate the fact that the following companies are not functionally comparable to the Appellant and therefore erred in law and facts in considering them as comparable companies;

- a. *Larsen & Toubro Infotech Limited:*
- b. *Persistent Systems Limited: and*

c. *Sasken Communication Technologies Limited*

In the above circumstances the Petitioner prays that this Hon'ble Tribunal be pleased to:

- i. admit and adjudicate the above additional ground,*
- ii. pass any other order that may be required in the circumstances of the case and render justice.*

10. All the aforesaid companies were chosen by the assessee in its TP analysis as a comparable company. Even before the CIT(A), the assessee had not chosen to challenge the aforesaid companies being considered as a comparable company. However the Special Bench, ITAT, Chandigarh, in the case of DCIT Vs. Quarks Systems Pvt. Ltd., 42 DTR 414 (Chandigarh-SB) has held that there cannot be estoppel against law and that non-comparable companies even if selected by the assessee in TP study can be sought to be excluded by the assessee based on functional comparability or other valid reasons. In view of the aforesaid decision of the special Bench, we admit the additional ground for adjudication.

11. The learned Counsel for the assessee however submitted that out of the 3 companies sought to be excluded in the additional grounds of appeal, exclusion of Persistent Systems Ltd., from the list of comparable companies would alone be sufficient. As far as exclusion of Persistent Systems Ltd., is concerned, the learned Counsel for the assessee brought to our notice decision of the ITAT, Bangalore Bench, in the case of Cerner Health Care Solutions Pvt. Ltd., in IT(TP)A No.44/Bang/2015 for Assessment Year 2010-11 wherein this Tribunal in the case of the assessee, rendering software Development Services such as assessee in this appeal, considered the comparability of Persistent Systems Ltd., and held as follows:-

“(4) Persistent Systems Ltd.

9. *We have heard the Id. DR as well as Id. AR and considered the relevant material on record. The assessee raised objections against selection of this company on the ground that this company is functionally not comparable as engaged in the product development. The segmental information for services and product is not available. Further, the assessee has also pointed out that there was an acquisition and restructuring during the year under consideration.*

10. *The DRP has noted the fact that this company has reported the entire receipt from sales and software services and product. Therefore, no segmental information was found to be available for sale of software services and product. Further, the DRP has noted that as per Note 1 of Schedule 15, this company is predominantly engaged in outsource software development service. Apart from the revenue from software services, it also earns income from licence of products, royalty on sale of products, income from maintenance contract, etc. These facts recorded by the DRP has not been disputed before us.*

11. *There, when 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., the same cannot be considered as functionally comparable with the assessee. Further, this company also earns income from outsource product development. In the absence of any segmental data of this company, we do not find any error or illegality in the findings of the DRP that this company cannot be compared with the assessee and the same is directed to be excluded from the set of comparables.”*

12. In view of the aforesaid decision of the ITAT, we are of the view that the aforesaid company should be excluded from the list of comparable companies. No other grounds of appeal were pressed for adjudication in the assessee's appeal.

13. As far as ground Nos. 3 and 4 raised by the Revenue in its appeal are concerned, we are of the view that the aforesaid grounds are vague. It has not been spelt out as to which of the companies were similar comparable companies. It is also not correct to say that functional comparability is not material. We, therefore, find no substance in ground Nos. 3 and 4 raised by the Revenue. We direct the TPO to compute the ALP in accordance with the directions given in this order, after affording opportunity of being heard to the assessee.

14. The only other ground that remains for adjudication in this appeal is ground No.2 raised by the Revenue in its appeal as to whether the Revenue authorities were justified in reducing the travel and telecommunication charges from the export turnover without reducing the same from the total turnover while allowing deduction to the assessee under section 10A of the Act. It is not in dispute before us that the Hon'ble Karnataka High Court in the case of CIT Vs. Tata Elxsi Ltd., 349 ITR 98 (Karnataka) has held that whatever is excluded from the export turnover should also be excluded from the total turnover while computing deduction under section 10A of the Act. This view of the Hon'ble Karnataka High Court has been upheld by the Hon'ble Supreme Court in the case of CIT Vs. HCL Technologies Ltd., (2018) 93 taxmann.com 33 (SC). In view of the above, we hold that telecommunication charges should be excluded both from the export turnover as well as from the total turnover and deduction under section 10A computed accordingly.

15. In the result, the appeal by the assessee is partly allowed while the appeal by the Revenue is dismissed.

Order pronounced in the open court on this 16th day of October, 2019.

Sd/-
(B. R. BASKARAN)
Accountant Member

Sd/-
(N. V. VASUDEVAN)
Vice President

Bangalore.

Dated: 16th October, 2019.

/NS/*

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| 1. Appellants | 2. Respondent |
| 3. CIT | 4. CIT(A) |
| 5. DR | 6. Guard file |

By order

Assistant Registrar,
ITAT, Bangalore.