

**IN THE INCOME TAX APPELLATE TRIBUNAL  
BANGALORE BENCHES :“A”, BANGALORE**

**BEFORE SHRI A.K.GARODIA, ACCOUNTANT MEMBER  
AND  
SMT.BEENA PILLAI, JUDICIAL MEMBER**

**IT(TP)A No.1319(Bang)/2011  
(Assessment year : 2007-08)**

M/s Schneider Electric IT Business India Pvt.Ltd.,  
(formerly known as American Power Conversion (I) Pvt.Ltd.,)  
187/3 and 188/3, Jigani,  
Bangalore-560 106  
Pan No.AACCA6398Q

Appellant

**Vs**

The Addl. Commissioner of Income Tax (LUT),  
Bangalore

Respondent

**Appellant by : Shri Sharath Rao, CA  
Revenue by : Shri C.H.Sundar Rao, CIT**

**Date of hearing : 19-08-2019**

**Date of pronouncement : 23-10-2019**

**ORDER**

**PER SMT. BEENA PILLAI, JUDICIAL MEMBER :**

1. Present appeal has been filed by assessee against final assessment order dated 18/10/11 passed by Ld.ACIT, LTU, Bangalore on following grounds of appeal:

***A. Transfer Pricing adjustments-***

*The learned Assessing Officer ("AO") and the learned Transfer Pricing Officer ("TPO") grossly erred in law and facts of the case in determining the arm's length price*

(`ALP') of the international transaction of the Appellant and thereby making an adjustment with respect to payments made by the tax payer u/s 92CA of the Income Tax Act for the following international transactions:

1. Software development services:-Rs. 31,36,792
2. Research and development services ("**R&D**"):-  
**Rs. 1,78,23,332**
3. **Royalty Payment:- Rs. 9,90,11,636**  
**Software Development Services**

1.1 The learned TPO and the learned AO grossly erred in law and facts of the case in determining the ALP of the international transaction of the Appellant as and thereby making an adjustment of Rs. 31,36,792 towards software development services.

1.2 That on the facts and circumstances of the case, the learned TPO and the learned AO erred in rejecting the Transfer Pricing (`TP') documentation without appreciating the contentions, arguments, and evidentiary data put forward by the Appellant during the course of the proceedings before them, and in doing so have grossly erred:

1.2.1. in adopting the arm's length mark up to be 23.12% in respect of international transactions of the Appellant.

1.2.2. in rejecting the upper limit for sales turnover filter proposed by the Assessee without providing any empirical analysis. In doing so, the learned TPO erred in not appreciating that the software industry is clearly demarcated based on size.

1.2.3. in not maintaining consistency in applying the filters of rejecting companies with software development revenue less than 75% of the total revenue, companies of different year end and in rejecting companies with abnormal/fluctuating profit margins.

1.2.4. in considering 25 percent as the threshold limit for the Related Party Transactions filter as this number is an arbitrary number that has been

adopted without any judicial precedence or reasonable basis.

1.2.5. *in applying the onsite filter for selection of software comparables with the use of the data obtained under section 133(6) of the Act. In doing so the learned TPO erred in rejecting Akshay Software Technologies Limited and VJIL Consulting Limited.*

1.2.6. *in accepting companies like Infosys Limited and Wipro Limited as a comparable companies even though the sales of Infosys and Wipro are driven based on brand developed by them, and doing so the learned TPO have incorrectly applied the ratio of the jurisdictional Delhi Income Tax Appellate Tribunal (ITAT) ruling in Agnity India Technologies India Pvt. Ltd. (reference: ITA No. 3856(Del)/2010).*

1.2.7. *in accepting companies engaged in the provision of software product development like Megasoft Limited, Flextronics Software Systems Limited, KALS Information Systems Limited, Avani Cimcon Technologies Limited, Lucid Software Limited, Ishir Infotech Limited, E-Zest Solutions Limited, Persistent Systems Limited and R Systems International Limited which are functionally not comparable to the Appellant's business.*

1.2.8. *in accepting Celestial Labs Limited as a comparable company even though it is a contract research company which also engaged in bio-informatics and hence functionally dissimilar to the Appellant.*

1.2.9. *in accepting Aced Transmatics Limited as a comparable company as it has sold its intellectual property and earned income from royalty and hence functionally dissimilar to the Appellant.*

1.2.10. *in accepting companies like Megasoft Limited Flextronics Software Systems Limited and Helios & Matheson Information Technology Limited which have abnormal/fluctuating profit margins. In doing so the learned TPO have disregarded the various jurisdictional ITAT rulings in case of SAP LABS India Pvt. Ltd. Vs. ACIT (reference ITA No. 398/Bang/2008), E-Gain Communication Private Limited (reference: ITA No. 1685/PN/07 - Pune).*

1.2.11. *in accepting Tata Elxsi Limited as a comparable company even though the company in its reply to the learned TPO under section 133(6) had mentioned that the company*

*provides product design services, which is functionally not comparable to the assessee's business;*

*1.2.12. in rejecting Thinksoft Global Services Limited by stating that it is not functionally comparable while ignoring the fact that Thinksoft Global Services Limited is engaged in software verification and validation services form an integral part of the software development services.*

*1.2.13. in concluding that Maars Software International Limited is not functionally comparable without even considering the fact that the IT consultancy services forms an integral part of the software development services and cannot be classified as functionally different from that of the Appellant.*

## **2. Research & Development**

*2.1 The learned TPO and learned AO grossly erred in law and facts of the case in determining the ALP of the international transaction of the appellant and thereby making an adjustment of Rs.1,78,23,332 towards R&D: services.*

*2.2 The learned TPO and learned AO erred in understanding the nature of business carried out by the Appellant. The learned TPO and learned AO have wrongly interpreted the functions of the Appellant and have wrongly compared the Appellant to pure R & D companies.*

*2.3 The learned TPO and learned AO erred in accepting Alphageo (India) Ltd, Vimta Labs Ltd, Oil Field Instrumentation (India) Limited, Celestial Labs Limited and Mindtree Consulting Limited which are functionally not comparable to the Appellant's business.*

*2.4 The learned TPO and learned AO erred in accepting Engineers India Ltd as a comparable Company by incorrectly applying the Export earnings filter.*

*2.5 The learned TPO and learned AO erred in rejecting Lurgi India Co. Pvt. Limited which is engaged in functions similar to the R&D segment of the Appellant and satisfies all the filters proposed by the TPO.*

*2.6 The learned TPO and learned AO has erred in rejecting Telecommunication consultants India Limited based on the application of the TPO's own filter of Export earnings.*

### **3. Royalty Payment**

3.1 *The learned TPO and learned AO grossly erred in law and facts of the case in determining the ALP of the international transaction of the Appellant and thereby making an adjustment of Rs 9,90,11,636 towards royalty payment.*

3.2 *The learned TPO and learned AO has erred in rejecting the adoption of Comparable Uncontrolled Price (CUP) method by the Appellant with respect to justification of ALP of Royalty transaction.*

3.3 *The Learned TPO and learned AO erred in interpreting that Transaction Net Margin Method (TNMM) was applied for justification of ALP of Royalty transaction.*

### **4 Common grounds**

4.1 *That the learned TPO and the learned AO erred in disregarding the use of multiple year data and ought to have accepted the use of contemporaneous data due to non-availability of current year data in the public domain at the time of preparing the documentation.*

4.2 *The learned TPO and the learned AO erred in computing market risk adjustment by deducting the marketing expenses from the total operating expenses without explaining the rationale of the same.*

4.3 *That the learned TPO and the learned AO erred in disregarding the fact that the Appellant has claimed tax benefits under section 10 A of the Act and has no reason to suppress its profits from its operation to manipulate the transfer prices. Therefore the adjustment proposed is not called for and is hence misplaced.*

4.4 *That the learned TPO and the learned AO erred in concluding that the Appellant is exposed to single customer risk without evaluating the business arrangement of the Appellant.*

4.5 *That the learned TPO and the learned AO erred in not allowing the benefit of range of +/- 5% as provided in proviso to Section 92C(2) of the Act to the Appellant, while determining the arm's length price.*

*B. Non-transfer pricing adjustments*

**5. Deduction under Section 10A to be allowed for unbilled revenue: Rs. 92,560,000**

5.1 The learned AO/ DRP erred in re-computing the deduction under section 10A of the Act after reducing the unbilled revenue amount of Rs. 92,560,000/-from Export Turnover.

5.2 The learned AO/DRP failed to appreciate the fact that the export proceeds have been repatriated into India within the time period as prescribed by RBI in accordance with Master Circular No 06/2010-11 dated 01.07.2010.

5.3 The learned AO/DRP ought to have appreciated that the Appellant has realized the foreign exchange amount prior to the completion of the assessment.

5.4 The Learned AO/DRP ought to have appreciated the fact that, section 10B contemplates repatriation of convertible foreign exchange in to India within stipulated time and does not mandatorily require the Appellant to raise the invoices.

5.5 The learned AO/DRP ought to have observed that raising of invoices is a commercial decision based on the milestone achieved by the appellant

5.6 The learned AO/DRP ought to have observed that accrual of exports based on quantum of work in progress is in accordance with accounting standards as prescribed by ICAI.

5.7 Without prejudice to the above, should the learned AO contend that invoices were raised almost a year after the exports and therefore exports could not be realized within the time permitted by the competent authority, the tax holiday benefit should be allowed in the year of realization of exports.

**6. Disallowance of royalty payment twice - Under Section 40(a) and section 92CAof the Act: Rs. 99,004,175**

6.1 The learned AO/ DRP erred in considering the disallowance of expenditure towards royalty twice — once under section 40(a) and again under section 92CA of the Act.

6.2 The learned AO/ DRP failed to appreciate that the same expenditure cannot be added back twice while determining the taxable income.

6.3 The learned AO/ DRP erred in holding that assessee is required to deduct tax at source since the nature of income does not undergo any change on account of the transfer pricing adjustment in the hands of the recipient.

**7. Deduction under Section 10A-Communication expenses: Rs. 2,791,365**

7.1 The learned AO/ DRP erred in re-computing the deduction under section 10A of the Act after reducing the communication expenses of Rs. 2,791,365/- from Export Turnover.

7.2 The learned AO/ DRP erred in considering the communication expenses as attributable to the delivery of software outside India for the purposes of computing the deduction under section 10A of the Act although it was submitted that no part of the communication expenditure was incurred specifically for the delivery of software outside India.

7.3 The learned AO/ DRP ought to have observed that the communication expenses were incurred towards lease line expenses and not specifically for the delivery of software outside India.

**7.4 Notwithstanding and without prejudice to the above, should the communication expenses be reduced from the export turnover, such expenses should also be reduced from the total turnover while arriving at the deduction under section 10A of the Act.**

**7.5 The learned AO/ DRP erred in relying on a decision of Chennai Tribunal in the case of California Software Co Ltd. Vs ACT (118-TTJ-844) which was pronounced before the decision of Sak Soft Limited.**

7.6 The learned AO/ DRP ought to have placed reliance on the decision of the Special Bench of the Chennai Tribunal in the case of Sak Soft Limited v. ITO (ITA No. 691 & 1953/Mds/2007) wherein it has been held that if the telecommunication, freight and insurance expenses are reduced from the export turnover then the same would also have to be reduced from the total turnover in order to compute the deduction under section 10A.

7.7 The appellant places reliance on the recent decision of the Honourable Karnataka High Court (Appeal no.451 of

2008), wherein it has been held that if any expenses are to be reduced from the export turnover then correspondingly such expenses should also be reduced from the total turnover.

**8. Donations for 10A units: Rs. 265,000**

8.1 The learned AO/ DRP have erred in disallowing the donation expenditure without attributing the same to the corresponding unit where it was incurred.

8.2 The learned AO/DRP ought to have observed that the said expenditure pertains to the unit eligible to avail benefit under section 10A of the Act.

**9. Calculation of Interest on resulting adjustment under section 234B of the Act: Rs.652,325**

9.1 The learned AO has erred in computing of the interest under section 234B of the Act as a consequence to the above adjustments.

**10. Calculation of Interest on resulting adjustment under section 234C of the Act: Rs. 1,359,011**

10.1 The learned AO erred in levying the interest under section 234C of the Act on the assessable income.

10.2 The learned AO ought to have considered the interest under 234C of the Act on the returned income of the Company.

**11. Levy of penalty under Section 271 of the Act**

11.1 The learned AO has erred in issuing a penalty notice to the Company consequent to above adjustments.

11.2 The learned AO ought to have observed that all necessary information and evidence on the expenditure in question as called for by the AO were duly disclosed and there has been no culpable negligence or willful omission on part of the appellant in furnishing such information.

The appellant craves leave to add, alter and modify the above grounds during the course of the appeal.

*For the above and any other grounds which may be raised at the time of hearing, it is prayed that the order of the Assessing officer be set aside.*

**2. Brief facts of the case are as under:**

2.1 Assessee filed its return of income for year under consideration on 14/11/07 declaring income of Rs.53,63,29,436/-. The same was processed under section 143 (2) and statutory notices was subsequently issued to assessee, in response to which, representative of assessee appeared before Ld.AO and filed requisite details as called for.

2.2 Ld.AO observed that assessee has three units, enjoying benefit of section 10 A known as EHTP Units-I and II and Software unit, besides a domestic unit. It was observed by Ld.AO that assessee debited sum of Rs.5,10,79,988/- towards communication charges, which formed part of deduction claimed under section 10A. Ld.AO was of opinion that, as per *Clause (iv) of Explanation 2 to Section 10A*, export turnover for purposes of claiming deduction, does not include freight, telecommunication charges, insurance attributable to the delivery of the articles or things or computer software outside India or expenses if any incurred in foreign exchange in providing technical services outside India.

2.3 Ld.AO accordingly disallowed sum of Rs.27,91,365/- being 80% of quantified communication charges relating to software unit.

2.4 Ld.AO further observed that assessee claimed deduction under section 10 A being expenses towards donation amounting to Rs.2,65,000/-. Ld. AO disallowed the sum by holding that eligibility of deduction under section 80G of the Act was not substantiated.

2.5 Ld.AO observed that assessee entered into international transaction with its associated enterprises, and therefore for determining arms length price of international transaction, case was referred to Ld.TPO.

2.5.1 Ld.TPO upon receipt of reference called for economic analysis of international transaction entered into by assessee.

2.5.2 From documentation so filed, it was observed that, assessee was a subsidiary of American Power Conversion Corporation, U.S., primarily engaged in manufacture of power protection equipment and undertakes trading of UPS and accessories. Ld.TPO observed that, assessee primarily exported by way of sales to its associated enterprises and also had sales of manufactured products in domestic market within India.

2.5.3 In TP study, it has been submitted that AE provides all technical support services in nature of software application development and maintenance and research and development in nature of software design and testing services. Ld.TPO observed that assessee entered into following international transactions with its associated enterprise:

Description	Amount (Rs.)
Purchas of components	49,76,93,029
Sale of finished goods	2040,06,39,648
Sale of components	5,41,10,918
Purchase of finished goods for trading	37,20,49,730
Provision of R&D services	2,60,42,479
Provision of tech support services	6,61,75,869
Royalty	9,90,11,636

Purchase of fixed assets	27,77,20,356
Reimbursement of expenses (paid)	19,12,10,015
Reimbursement of expenses (received)	17,29,89,512
Data communication expenses (paid)	44,17,717

2.6 Ld.TPO observed that assessee paid sum of Rs.9,90,11,636/- as royalty to its AE. From TP study, Ld.TPO observed that each of manufacturing subsidiaries of AE entered into non-exclusive license agreement with AE, for license of technology and trademark intangibles, for using manufacturing and royalty was payable on such revenues from sale of products in their local territories. Ld.TPO observed that assessee during year under consideration entered into similar exclusive license agreement with its AE, according to which royalty at 4.5 % was payable on domestic sale of manufactured products by assessee in local markets within India. It has been submitted that, it is the AE who owns all intellectual property rights, trademarks, patents, copyrights, trade secrets, confidential business information, inventions, discoveries and know-how is, manufacturing and product processes and techniques, research and development information, copyrightable works and all other proprietary rights.

2.6.1 Ld.TPO on perusal of submissions advanced by assessee concluded that assessee did not prove any tangible benefit derived by paying royalty for so-called superior technology and that any independent enterprise would like to pay royalty to access superior technology, only if the same results in either reduction of cost or improved profitability. Ld.TPO concluded that, loss incurred in domestic segment was mainly due to payment of royalty, which

otherwise would not be paid between two independent enterprises, dealing at arms length.

2.6.2 Ld.TPO thus determined ALP of royalty as 'nil'. He thus proposed adjustment of Rs.9,90,11,636/- as value of these transaction in uncontrolled conditions.

### 2.7. **Software development services.**

Ld.TPO observed that during the year assessee rendered technical support services to its AE's, against which revenue amounting to Rs.15,92,01,918/- was received. It was observed in TP study that, assessee used TNMM as most appropriate method, with PLI of OP/TC and determined margin of assessee to be at 11.63%. Assessee selected following 18 comparables in transfer pricing study with average margin of 13%, and since assessee's margin was within the range of +/-5%, transaction with its AE's were considered to be at arms length.

Company Name	Markup on total cost
Bodhtree Consulting	18%
FCS Software Solutions Ltd.,	14%
Goldstone Technologies Ltd.,	3%
Larsen & Toubro Infotech Ltd.,	11%
Melstar Information Technology Ltd.,	0%
Orient Information Technology	06%
Powersoft Global Solutions Ltd.,	19%
SIP Technologies & Exports	25%
Sonata software Ltd	9%
Synetairos Technologies Ltd.,	11%
Trident Info-Tech Corpn.Ltd.,	66%
VJIL Consulting Ltd.,	7%
Akshay Software Technology Ltd.,	7%
Cambridge Technology Enterprises	21%
ICRA Techno Analytics Ltd.,	15%
Mindtree Consulting Ltd.,	11%
Computech International Ltd.,	7%
Karuturi Networks Ltd.,	4%
Average Mean	<b>13%</b>

Mean	13%
------	-----

2.7.1 Ld.TPO on examination of TP documentation filed by assessee was of opinion that assessee is mainly offshore research and development service provider and these services are akin to software development services. Ld.TPO accordingly rejected comparables selected by assessee and finalized 29 comparables with average margin of 27.96 % which are as under:

Sl.No.	Company Name	OP to Total cost %
1	Accel Transmatic Ltd.(Seg.)	21.11%
2	Avani Comcon Technologies Ltd.	52.59%
3	Bodhtree Consulting Ltd.(Seg.)	109.79%
4	Celestial Labs Ltd.,	58.35%
5	Datamatics Ltd.,	7.27%
6	E-Zest Solutins Ltd.,	36.12%
7	Flextronics Software Systems Ltd.(Seg.)	25.31%
8	Geometric Ltd.(Seg.)	10.71%
9	Helios & Matheson Information Technology Ltd.,	40.35%
10	I Gate Global Solutiond Ltd.,	7.49%
11	Infosys Technologies Ltd.,	40.30%
12	Ishir Infotech Ltd.,	30.12%
13	KALS Information Systems Ltd.(Seg.)	30.55%
14	LGS Global Ltd., (Lanco Global Solutions Ltd.,)	15.75%
15	Lucid software Ltd.,	54.85%
16	Mediasoft Solutions Ltd.,	3.66%
17	Megasoft Ltd.(Seg.)	23.11%
18	Mindtree ltd.,	16.90%
19	Persistent Systems Ltd.,	24.52%
20	Quintegra Solutions Ltd.,	12.56%
21	R S Software (India) Ltd.,	13.47%
22	R Systems International Ltd.(Seg.)	15.07%
23	Sasken CommunicationTechnologies Ltd.(Seg.)	22.16%
24	SIP Technologies & Exports Ltd.,	13.90%
25	Tata Elxsi Ltd.(Seg.)	26.51%
26	Thirdware Solutions Ltd.	25.12%
27	TVS Infotech Ltd.,	11.61%
28	Wipro Ltd. (SEg.)	33.65%
		<b>27.96%</b>

Ld.TPO thus proposed adjustment under this segment amounting to Rs.31,36,297/-.

2.8 Ld.TPO observed that assessee undertook research and development services during year. Arms length price of international transaction representing research and development services was determined by applying TNMM as most appropriate method and OP/TC as PLI. Assessee computed its margin at 10% on cost and average margin of 3 comparables were determined at 7% in TP study report. Assessee thus held that the transaction was within +/-5% of the price charged and thus was treated to be at arms length.

S.No.	Particulars	Margin
1.	Telecommunication consultants India limited	-2%
2.	Crisil research and information services Ltd	5%
3.	Engineers India limited	18%
	Average Margine	7%

2.8.1 Ld.TPO accordingly called for economic analysis and by applying various filters and rejected comparables selected by assessee and brought on new set off 7 comparables having average margin of 39.48%.

Sl.No	Name of the company	Operating Profit to Cost
1	Engineers India Ltd.,(seg.)	45.16%
2	Alphageo (India) Ltd.	38.21%
3	Vimta Labs Ltd	27.44%
4	IDC (India)Ltd.,	15.89%
5	Oil Field Instrumentation (India) Ltd.,	76.46%
6	Celestial Labs Ltd.,	58.35%
7	Mindtree Ltd.(seg.)	14.90%
	<b>Arithmetic mean</b>	<b>39.48%</b>

3.4 Ld.TPO computed adjustment for this segment at Rs.1,78,23,332/-

3. Aggrieved by adjustments proposed by Ld.TPO, under various segments assessee raised objections before DRP, who upheld view of Ld.TPO.

3.1 On receipt of DRP directions, Ld.AO passed final impugned assessment order, wherein following additions were made

- transfer pricing additions in software service development segment was made amounting to Rs.31,36,297/-
- transfer pricing addition in research and development segment was made at rupees would Rs.1,78,23,332/-
- disallowance of Royalty amounting to Rs.9,90,11,636/-.
- deduction claimed by assessee under section 10 A of the Act, was restricted to Rs.27,91,365/-, being 80% of expenses claimed.
- Donation paid amounting to Rs.2,65,000/- claimed as deduction under section 10 A

4. Aggrieved by order passed by Ld.AO, assessee is in appeal before us now.

4.1 Ld.AR submitted that **Ground No. 1.1 and 1.2** are general in nature, and therefore do not require any adjustment.

4.2 Ld.AR further submitted that **Ground No. 1.2.1-1.2.5** are to not pressed.

**Accordingly these grounds are dismissed as not pressed.**

5. Assessee has raised additional ground vide application dated 03/03/2016, seeking exclusion of Thirdware Solutions Ltd., being **Ground No. 1.2.14** which is as under:

**Additional Ground:**

**“No.1.2.14-** *Thirdware Solutions Ltd., (Thirdware) should be rejected as a comparable for the technical service segment.*

*The appellant submits that the ld.TPO has erred in including Thirdware as a functionally comparable company to the appellant while doing the comparability analysis.*

**Reason for filing Additional Ground of Appeal.**

*The appellant wishes to highlight that during the preparation of its transfer pricing report. Thirdware did not appear in the database. Thirdware a subsequently, selected as a comparable by the Ld.TPO based on fresh comparability analysis at the time of transfer pricing assessment proceedings. In the absence of any specific details in the public domain the appellant was not in a position to controvert the stand of the Ld.TPO at the time of assessment proceedings. Therefore, the inclusion of this company as a comparable was not specifically contested before the Ld.TPO at that time.*

*For the same reasons, no specific grounds objecting to the inclusion of the company in the set of comparables was taken before the Hon’ble Dispute Resolution Panel(DRP Further, no specific ground of appeal was raised before the Hon’ble Tribunal as well objecting to the inclusion of the company as a comparable while filing Form 36B before the Hon’ble Tribunal.*

*However, subsequent to the filing of the appeal, it has come to the notice of the appellant that it has been held by the Hon’ble Tribunal in various decisions that this company is in the business of product development and earns revenue from sale of license*

*and subscriptions. Hence, the company is functionally different from software development service provider and as such is functionally not comparable to that of the appellant”*

5.1 It has been submitted that alleged comparable were selected by Ld.TPO on fresh comparability analysis during Transfer Pricing assessment proceedings and in absence of any specific details in public domain and assessee was unable to controvert stand of Ld.TPO. Ld.AR submitted that it is for this reason that no specific ground was raised for exclusion of this comparable before Ld.DRP and before this *Tribunal*.

Placing reliance upon decision of *Hon'ble Supreme Court* in case of *NTPC Ltd vs CIT* reported in 229 ITR 383 and *Jute Corporation of India vs CIT* reported in 53 taxman 85, submitted that comparables specified in additional grounds may be admitted.

Ld.CIT DR, though opposed admission of additional ground, could not controvert submissions advance by Ld.AR.

We have perused details relied upon by both sides

In our considered opinion comparables alleged in additional ground arises out of records and was objected before DRP for its exclusion/inclusion. Considering inadvertent mistake on behalf of assessee in raising these grounds before this Tribunal, we allow additional ground raised now.

**Accordingly additional ground no.1.2.14 in application dated 03/03/2016 stands allowed.**

6. **Ground No. 1.2.6 -1.2.11** has been raised by assessee challenging addition made by Ld.AO on account of arms length price computed for software design and development service segment being technical support services provided by assessee to

its AE's. Ld.AR submitted that only issue disputed by assessee is in respect of comparables selected by Ld.TPO. Primary, allegations regarding comparables on the ground of functional dissimilarity with assessee and does not fulfill filters applied by Ld.TPO himself.

6.1 Ld.AR submitted that following comparables have been objected by assessee for inclusion:

- Accel Transmatic Ltd. (Seg.)
- Avani Cimcom Technologies Ltd.
- Celestial Labs Ltd.
- E-Zest Solutions Ltd.
- Flextronics Software Systems Ltd. (Seg.)
- Helio and Matheson Information Technology Ltd.
- Ishir Infotech Ltd.
- Lucid Software Ltd.
- Megasoft Ltd.
- Persistent Systems Ltd
- Infosys Ltd.
- KALS Information Systems Ltd
- R.S.systems Ltd.
- Tata Elxi Ltd.
- Wipro Ltd. (seg.)
- Thirdware Solutions Ltd.

6.2 He submitted that this *Tribunal* in various decisions has excluded these comparables on functional dissimilarity. He placed reliance upon decision of assessee's own case for *Assessment year 2006-07* in *ITA No. 1415/B/2010* and *Assessment year 2009-10* in

ITA No. 299/B/2014 along with IT(TP)No.2188/B/2014, passed by Coordinate Bench of this Tribunal vide order dated 07/06/19 and 30/04/19 respectively.

6.3. Before we go into compatibility analysis of these comparables with that of assessee, it is *sine qua non* to understand functions performed, assets owned and risks assumed by assessee under this segment.

### **Functions Performed:**

#### ***Functional analysis***

##### **Information and specifications**

The technical support services performed by APC India are based on the instructions and specifications provided by APCC US. There are regular interactions with APCC US regarding project specifications and obtaining certain clarifications/information on the projects provided by APCC US to APC India.

##### **Technical assistance and clarifications**

We understand that APCC US provides technical assistance, information and certain technical clarifications in the provision of technical support services provided by APC India. There are regular weekly updates by the IDC to APCC US on the status of the projects/activity assigned by APCC US.

##### **Training**

APC India provides both internal and external training to its employees. These training programs could be organized either in the US or in India.

##### **Design and software development**

APC India does not develop software products for sale in open market. It caters to the specific needs of APCC US and its associated enterprises worldwide that help exploiting new opportunities by harnessing knowledge of business processes with proven skills in applying technology.

Technical support and maintenance activity

APC India provides internal technical support services which includes creating, maintaining or enhancing APC company-wide internal use software infrastructure.

Billing and collection

APC India is responsible for raising invoices and their subsequent collection.

**Assets Owned:**

It has been submitted in TP study that, assessee does not own any significant intangible assets. It only has technical manpower employed and trained by company being most important assets along with furniture fixtures computer peripherals etc.

**Risks Assumed:**

It is submitted that, as assessee is a captive service provider and is compensated at cost +10%, it does not bear any risks like market risk, financial risk, credit and collection risk and service liability risk. Only risk that would be assumed by assessee is in terms of foreign exchange risk as revenue received by assessee is in foreign exchange.

6.4 Thus, assessee has been categorized as a routine service provider undertaking contract software development services assuming normal risk associated with carrying out such business.

7. In our considered opinion, comparability is to be carried out on broad object of benchmarking international transaction and according to law laid down under section 92B of the Act, read with rule 10 B (2) Income tax Rules, 1963. Comparables must be similar in material aspects and must be compared on basis of products/services characteristics, functions undertaken, assets used and risk assumed. Merely because certain comparables has been upheld for its exclusion/inclusion by various decisions, does not *ipso facto* lead to exclusion/inclusion in a given set of facts. In our considered opinion, exclusion/inclusion of any comparables must be strictly analysed on basis of FAR, in accordance with rule 10 B (2). We also are of opinion that comparables selected must be for relevant year which is to be compared and unless contemporaneous data as section 92D read with Rule 10 D (4), is not available for a relevant year, multiple year data should not be used.

7.1 Based upon above FAR analysis, we shall now undertake compatibility tests of assessee with comparables under objection for inclusion.

8. With aforestated understanding, let us analyse comparables alleged to be excluded by assessee before us.

8.1 At the outset, Ld.AR submits that for year under consideration, in the event, following comparables are considered for exclusion, assessee would be within acceptable arms length margin.

- Avani Cimcom Technologies Ltd
- Celestial Labs Ltd
- E-Zest Solutions Ltd
- Flextronics Software Systems Ltd (Seg.)

- Helio and Matheson Information Technology Ltd
- Ishir Infotech Ltd
- Lucid Software Ltd
- Megasoft Ltd.
- Persistent Systems Ltd
- R.S.systems Ltd.
- Infosys Ltd.
- KALAS Information Systems Ltd
- Wipro Ltd.

8.2 In respect of remaining comparables, Ld.AR submitted that liberty may be granted to argue their exclusion in appropriate circumstances.

**8.2.1. Accel Transmatic Ltd (Seg.):**

It has been submitted that this comparable has been included by Ld.TPO even though this functionally dissimilar with that of assessee. He further submitted that this comparable has sold its intellectual property rights in “Prodigy” and receives royalties on sale of software. Ld.AR thus submitted that the segment applied by Ld.TPO itself is not identical with that of assessee.

Ld. CIT DR placed reliance upon the observations of authorities below and prayed for its inclusion.

10. We have perused submissions advanced by both sides in the light of records placed before us.

It is observed that Ld.TPO used segmental information in respect of products of this comparable. However, from various products developed by this comparable, it is observed that, they are not into contract software development, which is the case of assessee, developing software for its AE only, for which assessee is

remunerated on cost +10% markup. Further that in the process of software development, in the event any intangibles are created, the same is exclusively owned by AE. As we have already analysed the functions and the risks assumed, it is observed that assessee do not even undertake the pricing risk as the prices are decided by its AE only. Under such circumstances we do not find it functionally similar even though taking the segmental details of sale of products as there is a huge difference in the products sold by this comparable with that of assessee.

It is assessee's submission that in the revised order, Ld.TPO while considering this comparable included Rs.5.4 crores of foreign exchange gain/loss at entity level, whereas segment information has been used by Ld.TPO. It is assessee's contention that due to this anomaly, OP/TC has increased to 54.72% from 8.62% whereas the correct computation of mark-up would work out to 9.31%.

We restore this comparable to the file of the TPO to re-compute the correct margins, after due verification of the assessee's claim/computation.

**8.2.2 Accordingly, this comparable is set aside to Ld.TPO.**

**8.2.3. Avani Cimcon Technologies Ltd.**

It has been submitted that this company is functionally different from the assessee. Based on the information available in company's website, it has been submitted that this company developed a software product by name "DXchange". It was also submitted that this company has revenue from software product sales, apart from rendering of software services for which segmental information is not available. It has therefore been submitted that this company is

functionally different from assessee. It was further submitted that Mumbai Bench of *Tribunal* in case of *Telcordia Technologies Pvt. Ltd. v. ACIT in ITA No.7821/Mum/2011* accepted assessee's contention that this company has revenue from software product and observed that in absence of segmental details, Avani Cincom cannot be considered as comparable to an assessee who was rendering captive software development services.

Ld.DR, on the other hand, relied on order of Ld.TPO.

We have considered submissions advanced by both sides and perused records placed before us.

It was submitted that this company has made unusually high profit during the financial year 2006-07. It is observed that operating revenues increased 63.03% which indicates that it was an extraordinary year for this company. Even growth of software industry for previous year as per NASSCOM was 32%. The growth rate of this company was double the industry average. In view of the above, it was argued that this company ought to have been rejected as a comparable.

It was observed by this *Tribunal* in case of *Telcordia Technologies Pvt. Ltd. v. ACIT(supra)* that margin of this company is 52.59% which represents abnormal circumstances and profits. Following figures were relied by Ld.AR, as observed by coordinate bench of this *Tribunal* in case of *First Advantage Offshore Services Pvt.Ltd. Vs DCIT(supra):-*

Particulars	05-06	06-07	07-08	08-09
Operating Revenue	21761611	35477523	29342809	28039851
Operating Expns	16417661	23249646	23359186	31108949
Operating Profit	5343950	12227877	5983623	(3069098)
Operating Margin	32.55%	52.59%	25.62%	- 9.87%

**We, therefore, direct Ld.TPO to exclude this company from final list.**

#### **8.2.4. Celestial Labs Ltd.**

It has been submitted that this research & development company. In this regard, the following submissions were made:-

As per Notes to Accounts - Schedule 15, under "Deferred Revenue Expenditure", it is mentioned that, "Expenditure incurred on research and development of new products has been treated as deferred revenue expenditure and same has been written off in 10 years equally yearly installments from the year in which it is incurred." An amount of Rs.11,692,020/- has been debited to Profit and Loss Account as "Deferred Revenue Expenditure". This amounts to nearly 8.28 percent of sales of this company.

Reliance was made to decision of *Mumbai Bench of Tribunal* in case of *Teva Pharma Private Ltd. v. Addl. CIT - ITA No.6623/Mum/2011 (for AY 2007-08)* in which comparability of this company for clinical trial research segment. The Company has developed a drug design tool "CELSUITE" to find lead molecules for drug discovery and has patented the same. It has observed that this Company developed molecule to treat Leucoderma and

multiple cancer which is also protected under IPR by filing patent. It is observed that this company is planning to set up biotechnology facility to manufacture industrial enzymes, which include research laboratories for carrying out further R & D activities to develop new drug molecules and license them to Interested Pharma and Bio Companies across the GLOBE. It is thus observed that this company is into diversified activities and therefore cannot be considered as functionally comparable with Assessee who is a captive service provider. It was thus submitted that, this company is not into software development activities, accordingly, this company should be rejected as comparable being functionally different.

Ld.DR, on the other hand, relied on order of Ld.TPO.

We have considered submissions advanced by both sides and perused records placed before us.

It has been pointed out that this company provides software products/services as well as bioinformatics services and that the segmental data for each activity is not available and therefore this company should not be treated as comparable. Besides the above, the Assessee pointed out from annual report highlighting the fact that, this company is into developing biotechnology products and provides related software development services, without any segmental details. There is no detail regarding nature of software development services performed by this company. Celestial labs had come out with a public issue of shares and in that connection issued Draft Red Herring Prospectus (DRHP) in which business of this company was explained as to clinical research. We are of the

view that in light of submissions made by Ld.AR and the fact that this company was basically/admittedly in clinical research and manufacture of bio products and other products, there is no clear basis on which it could be held that this company is mainly in the business of providing software development services.

**We therefore direct Ld.TPO to exclude this company from final list.**

#### 8.2.5 **E-Zest Solutions Ltd:**

This company has been selected by Ld.TPO and objected by assessee on the ground that, it was functionally different from assessee. Ld.TPO rejected contentions of assessee on the basis of information received in response to notice under section 133(6) of the Act, wherein it was held that this company is engaged in software development services. It was thus held by Ld.TPO that this company satisfies all filters.

Ld.AR submitted that this company ought to be excluded from the list of comparables on the ground that it is functionally different to the assessee. He submitted that this company is engaged in 'e-Business Consulting Services', consisting of Web Strategy Services, IT design services and in Technology Consulting Services including product development consulting services, and are high end ITES normally categorized as knowledge process outsourcing ('KPO') services. It is further submitted that this company has not provided segmental data in its annual Report, and does not contain detailed descriptive information on the business of the company. It is also submitted that KPO services are not comparable to software development services and therefore companies rendering KPO services ought not to be considered as comparable to software

development companies. In support of, he placed reliance on decision of *co-ordinate bench* of this *Tribunal* in case of *Hewlett Packard (I) Ltd Vs.DCIT in ITA no. 1031/Bang/2011*

On the contrary, Ld.DR supported the inclusion of this company in the list of comparables by the TPO.

We have heard rival submissions and perused and carefully considered material on record.

It is seen from record that Ld.TPO included this company on the basis of statement made by the company in its reply to notice under section 133(6) of the Act. It appears that Ld.TPO did not examine services rendered by this company to give a finding whether services performed by this company are similar to Captive software development services performed by assessee. From details on record, we find that while assessee is a captive software development service provider, this company i.e. e-Zest Solutions Ltd., is rendering product development services and high end technical services which come under category of KPO services. It has been held by *co-ordinate bench* of this *Tribunal* in case of *Hewlett Packard (I) Ltd Vs.DCIT(supra)* that KPO services are not comparable to software development services and are therefore not comparable. Following the aforesaid decision of the *co-ordinate bench* of the Hyderabad Tribunal in the aforesaid case, we hold that this company, i.e. e-Zest Solutions Ltd. be omitted from set of comparables for period under consideration

**We therefore direct Ld.TPO to exclude this company from final list.**

**8.2.6. Flextronics Software Ltd.(Seg.)**

This comparable has been selected by Ld.TPO in final list and objected by assessee due to non availability of reliable financial data for year under consideration.

He submitted that Ld.TPO obtained information u/s 133(6), which is contrary to annual report and therefore is not reliable. It has been submitted that the annual report is for year ending 31.03.2007 for a period of nine months and Ld.TPO without reconciliation between annual report and information received u/s.133(6) considered in the final list. In support of, he placed reliance on decision of co-ordinate bench of this Tribunal in case of *Hewlett Packard (I) Ltd Vs.DCIT* in *ITA no. 1031/Bang/2011*.

On the contrary, Ld.DR supported the inclusion of this company in the list of comparables by the TPO.

We have heard rival submissions and perused and carefully considered material on record.

It is seen from record that Ld.TPO included this company on the basis of statement made by company in its reply to notice under section 133(6) of the Act.

It is observed that there is no segmental information in respect of this company in annual report. We are unable to understand how segmentation was done by Ld.TPO and reconciliation of annual report. In such a situation we are of the opinion that Flextronics Software Solutions Ltd (seg) cannot not be considered as a proper comparable.

**We therefore direct Ld.TPO to exclude this company from final list.**

**8.2.7. Helios & Matheson Information Technology Ltd.**

This comparable has been included by Ld.TPO, and objected by assessee as it is functionally incomparable. It has been submitted that this company is engaged in development and sale of software products which is functionally different from services undertaken by assessee in IT-services segment. Further it has been submitted that this company has a high turnover and does not satisfy the turnover filter of 1-200 cr, as has been held by coordinate bench of this Tribunal in various cases.

Ld.AR submitted that this company is engaged in two segments namely application software segment and Training. As per Ld.TPO, application software segment is functionally comparable to assessee as this company is engaged in software services. Ld.AR submitted that a perusal of annual report of the this company for F.Y. 2006-07 reveals under software segment it is engaged in business of sale of software products and software services. It has been submitted that segmental details are not available in respect of sale of software products and software service segment, and therefore, it was not appropriate to adopt application software segment of this company for purposes of comparability with assessee.

On the contrary, Ld.DR supported the inclusion of this company in the list of comparables by the TPO and submitted that comparability cannot be decided merely on the basis of scale of operations and the operating margins of this company have not been extraordinary. In view of this, the learned Departmental

Representative supported the decision of the TPO to include this company in the list of comparable companies..

We have heard rival submissions and perused and carefully considered material on record.

It is observed that this company has substantial revenues from software products and break-up of software product revenues is not available. This company has incurred huge research and development expenditure to the tune of approximately Rs.200 Crores. Ld.AR placed reliance on the following judicial decisions :-

*(a) ITAT, Delhi Bench decision in the case of Agnity India*

*Technologies India Pvt. Ltd. (ITA No.3856/Del/2010) and*

*(b) Trilogy E-Business Software India Pvt. Ltd. (ITA No.1054/Bang/2011)*

We find that assessee has brought on record sufficient evidence to establish that this company is functionally dis-similar and different from assessee and hence is not comparable and finding rendered in the case of Trilogy E-Business Software India Pvt. Ltd. (supra) for Assessment Year 2007-08 is applicable to this year also. The argument put forth by assessee's is that this company has huge revenues from software products. It is also seen that the break up of revenue from software services and software products is not available. In this view of the matter, we hold that this company ought to be omitted from the set of comparable companies.

**We therefore direct Ld.TPO to exclude this company from final list.**

#### 8.2.8. **Infosys Ltd:**

It has been submitted that Infosys Ltd., was selected as comparable by Ld.TPO in assessee's own case for assessment year 2008-09. However, Co-ordinate Benches of this *Tribunal* has directed exclusion of the same on the ground that it is functionally different with that of assessee. It has also been observed that this company was owning brand and having substantial intangible assets which cannot be held to be suitable comparable for assessee who was only providing contract software development services and IT staffing services. It has been submitted that functions of assessee, assets and risk profile has not undergone any change for the year under consideration. Ld.Counsel has also submitted that this company is not functionally comparable to assessee inasmuch as, it is also engaged in software development services and generate substantial revenue from the sale of its own products. Ld. counsel placed reliance upon the decision of *CIT vs. Agnity India Technologies Pvt. Ltd* in ITA No. 1204/Del/2011, wherein this Tribunal vide order dated 10/07/11 upheld exclusion of this company from list of comparables, after taking into consideration its operations as full-fledged risk taking enterprise in diversified field such as application design, development, re-engineering and maintenance integration etc cannot be equated with non-risk bearing companies. It has been submitted that this view of *Agnity India technologies Pvt.Ltd.*, has been upheld by *Hon'ble Delhi High Court* in ITA No. 3856/2010.

Ld. CIT DR placed reliance upon the order of Ld. TPO.

22. We have considered the various distinguishing features submitted by Ld.Counsel on the basis of records placed before us.

Since all the distinguishing features exist even in the year under consideration, respectfully following the order of this Tribunal in assessee's own case, we direct this company to be excluded from the final list of comparables.

**Accordingly this comparable is excluded from finalist.**

**8.2.9. Ishir Ltd.**

Ld.TPO included this company in the finalist, and objected by assessee due to functional dissimilarities. It has been submitted that as this company outsources its work, it does not satisfy 25% employee cost filter and thus has to be excluded. He placed reliance on decision of *coordinate bench* of this *Tribunal* in case of *First Advantage Offshore Services Pvt. Ltd. V DCIT in IT(TP)A No.1086/Bang/2011 for AY: 2007-08*, wherein it has been held that this company is not comparable in case of software development services provider.

On the contrary, Ld.DR supported the inclusion of this company in the list of comparables by the TPO.

We have heard the rival submissions and perused and carefully considered material on record.

Respectfully following the decision of the tribunal referred to above, we direct the AO/TPO to exclude this company from final list of comparable.

**8.2.10. KALS Information Systems Ltd**

It has been contended that this company has revenues from both software development and software products. It is also pointed out that this company is engaged in providing training and that as per the annual report, salary cost debited under software development

expenditure was Rs45,93,351/- which is less than 25% of software services revenue and therefore fails in salary cost filter test applied by Ld.TPO. Reliance has been placed on decision of this Tribunal for assessment year 2007-08, in case of *Maphasis Ltd. vs ACIT (supra)* wherein KALS as comparable was rejected being functionally different from software companies. The relevant extracts are as follows:

*“16. Another issue relating to selection of comparables by the TPO is regarding inclusion of Kals Information System Ltd. The assessee has objected to its inclusion on the basis that functionally the company is not comparable. With reference to pages 185-186 of the Paper Book, it is explained that the said company is engaged in development of software products and services and is not comparable to software development services provided by the assessee. The appellant has submitted an extract on pages 185-186 of the Paper Book from the website of the company to establish that it is engaged in providing of I T enabled services and that the said company is into development of software products, etc. All these aspects have not been factually rebutted and, in our view, the said concern is liable to be excluded from the final set of comparables, and thus on this aspect, assessee succeeds.*

*Based on all the above, it was submitted on behalf of the assessee that KALS Information Systems Limited should be rejected as a comparable.”*

Ld.DR, on the other hand, relied on order of Ld.TPO.

26. We have considered submissions advanced by both sides and perused records placed before us.

We find that Ld.TPO concluded on basis of information obtained by issue of notice u/s.133(6) of the Act. This information which was not available in public domain could not have been used by Ld.TPO, when the same is contrary to annual report of this company as highlighted by Ld.AR. We also find that in the decision referred to by Ld.AR, of this Tribunal held that this company was developing software products and not purely or mainly software development service provider.

**We therefore accept the plea of the Assessee that this company is not comparable.**

**8.2.11 Lucid Software Ltd.**

As observed, Ishir Ltd.(Supra) Lucid Software Ltd, this Company is also involved in the development of software as compared to the assessee, which is only into software services.

**8.2.12. Megasoft Ltd.:**

It has been submitted that this comparable has been included by Ld.TPO. Ld.AR submitted that the information collected by Ld.TPO is by issuing notice under section 133 (6) of the act. He has further submitted that information so paid by Ld. TPO varies with that of the information that is available on the public domain. He submitted that under such circumstances these comparable should be excluded as there is no clarity regarding the functions performed, the assets owned and the risks assumed by this comparable.

Ld. CIT DR though supported the observations of authorities below could not controvert therefore stated submissions advanced by Ld.AR.

We have perused submissions advanced by both sides in the light of the records placed before us.

It is observed that at page 386 of paper book volume 1 and page 3040 of paper book volume 5 details regarding the activities carried out by this comparable has been placed. And we observe that there is contradictions in the facts mentioned in the audited financial reports and annual reports vis-a-vis the information collected by Ld.TPO under section 133 (6). We are therefore of considered

opinion that this comparable should not be used as there exists contradictions in the details available on public domain vis-a-vis the information gathered by Ld.TPO under section 133 (6).

**Accordingly, we direct Ld.TPO to exclude this comparable from the final list.**

**8.2.13. Persistent systems Ltd.**

Ld. Counsel submitted that this comparable has been included by Ld.TPO, however in assessee's own case for assessment year 2008-09 this Tribunal in ITA No.5401/Del/2012 directed exclusion of the same on the ground that it is functionally different with that of assessee. Ld.Counsel submitted that there is lack of segmental accounting in the financials of this company. He also submitted that there are no bifurcations between the services rendered by this company. This Tribunal while considering this comparable for assessment year 2008-09 (supra) has observed that during the relevant assessment year company developed its own software products, and its revenue included licensing of software products.

Ld.CIT, DR submitted that this company is into software services and products. And segmental accounting of software services and products are available for the year under consideration.

We have perused the submissions on the basis of the records.

It is observed that assessee has developed software during the year, and has earned royalties from sale of products. Assessee has earned revenues from Licensing of products. It is also observed from the notes to the accounts of this company that the segment information has been provided on consolidated financial statements. It is also observed that assessee owns the software developed by it on which depreciation is claimed. Thus this

company has been characterized itself as engaged in providing outsourced product development services to independent software vendors and enterprises. It has been characterised to having earned significant portion of its revenues from export of software services and products. This function, the assets owned by this company and the risk assumed are not comparable with that of the present assessee and hence has to be excluded from the final list of comparables.

**Accordingly, this comparable is directed to be excluded from finalist.**

**8.2.14. R Systems International Ltd.**

Ld.Counsel submitted that this Tribunal while deciding the case of *Hewlett-Packard (India) Global Soft Pvt.Ltd (supra)* held this comparable to be excluded since this company has a different year ending. Assessee has submitted this comparable to be into IT related and BPO services. However on perusal of annual report placed at page 831-994 of paper book volume- 2, we observe that this comparable has income from software development and customization services and to a lesser extent from BPO services. It has been submitted that this comparable derives its revenue from 2 segments and has provided segmental information at page 888 of paper book. Under such circumstances, merely because comparable has a different year ending, cannot lead to the conclusion, of it being non-comparable with that of assessee. In the event quarterly results are available and the same can be extrapolated, this comparable should be considered.

We therefore, set aside R Systems International Ltd., which is functionally similar, to Ld. AO/TPO to consider the quarterly report

and extrapolate the same for purposes of comparing its margin with assessee.

**Accordingly, we set aside this comparable to Ld.TPO.**

8.2.15. **Wipro Ltd (Seg)**

This Comparable has been included by Ld.TPO.

This is TPO's comparable in which segmental details has been obtained u/s. 133(6) of the Act. However, assessee has sought its exclusion on grounds of significantly higher turnover, abnormal margins, presence of intellectual property, diversified business, brand value and turnover. He placed reliance upon the decision of *ICC India Pvt.Ltd., vs. ACIT (supra)*..

On the contrary, Ld.DR submitted that there is no related party transaction during the year under consideration.

We have heard rival submissions of both sides in the light of records placed before us.

It is observed that Co-ordinate Bench of the Delhi Tribunal *in ICC India Pvt.Ltd., vs. ACIT (supra)* has excluded this comparable by placing reliance upon *Calibrated Healthcare Systems (I) (P) Ltd. Vs ACIT (OSD) reported in (2015) 54 Taxmann.com 53*. It is observed that in this decision this tribunal has examined comparability of WIPRO and ordered its exclusion on the ground that this is a giant entity with marked differences as regards risk profile, nature of services, ownership of IP rights, expenditure on R&D, etc. So, following the decision rendered by co-ordinate bench as well as the fact that the assessee company is a captive service provider taking minimum risk having no intangibles cannot be compared with

WIPRO which is having diversified business, ownership of significant intangibles and huge expenditure on R&D etc.

**We thus, direct Ld.TPO to exclude this company from final list of comparables.**

We also mention that not considering of other comparables alleged by assessee does not *ipso facto* lead to upholding their inclusion, as with exclusion of comparables considered herein above, assessee falls into +/- 5% range. However, we grant liberty to assessee to allege other comparables, not considered by us in an appropriate instance.

**Accordingly we allow Ground no.1.26 to 1.21 as discussed herein above.**

**9. Ground No.2.1 to 2.6**

Both sides submitted that identical issue has been considered by Co-ordinate Bench of this *Tribunal* in assessee's own case for assessment year 2009-10 vide *order dated 30/04/19 in ITA No. 299/Bang/2014 and 218/Bang/2014*, wherein this issue has been set aside to Ld.TPO. It has been submitted that following the same the issue may be set aside to Ld.TPO.

35. We have perused the order passed by this *Tribunal* in assessee's own case for *assessment year 2009-10 (supra)* and observed that the issue has been decided by observing as under:

**RESEARCH AND DEVELOPMENT SERVICES SEGMENT:**

*14. As far as determination of ALP in this segment is concerned, the disputes raised by the Assessee are that the nature of services rendered by the Assessee to its AE was SWD services and it is not correct to characterize the*

same as R & D Services. Though this was the basis on which the TP study was undertaken by the Assessee, the Assessee submits that there is no estoppels in the matter of determination of ALP. The learned counsel in this regard has also pointed out that the TPO in AY 10-11 & 2011-12 accepted the claim of the Assessee in this regard and the relevant order's of TPO was also placed before us. The other grievance projected by the Assessee is that even assuming that the Assessee is to be regarded as rendering R & D services to its AE, the comparable companies chosen by the TPO and retained by the DRP are not comparable functionally and otherwise. The other grievance projected by the Assessee is regarding not granting working capital adjustment to the profit margins of comparable companies and the profit margins of the Assessee before comparing the profit margins with comparable companies to arrive at ALP.

15. The learned DR on the other hand while pointing out that the Assessee in his TP Study has chosen to characterize the transaction with AE as R & D Services cannot now be permitted to say that the nature of services is akin to SWD services. In this regard he also drew our attention to the Agreement between the Assessee and its AE under which the services in question were rendered by drawing our attention to Page 4997 of the Assessee's paper book.

16. We have heard the rival contentions and the nature of service as set out in the note filed as part of the written submission before us. We are not reproducing the note filed by the parties before us and the contentions put

*forth therein because it requires examination by the AO/TPO. We are of the view that in the light of the TPO's acceptance in AY 20010-11 & 2011-12 that the nature of services rendered was akin to SWD services, the entire comparability criteria will change and the comparable companies already retained in the SWD segment will hold good for this segment also. We therefore feel that it would be just and appropriate to remand for fresh consideration by the AO/TPO of the nature of services rendered by the Assessee in this segment. This will depend upon the terms of the Agreement between the Assessee and AE for rendering services which are in dispute. The TPO will decide on the character of services rendered by the Assessee whether it is R & D or SWD, after affording opportunity of being heard to the Assessee and after considering all relevant factors. If the TPO comes to the conclusion that the nature of services rendered is SWD services, then the comparable companies chosen in the SWD services segment, which we have already decided in the earlier paragraphs, would be applicable. If he comes to the conclusion that the services rendered were in the nature of **R & D** and not SWD services, then the issue with regard to comparability of companies already chosen by the TPO/DRP on the basis of assumption that the Assessee is rendering R & D services and working adjustment to be made to the profit margin of comparable companies chosen on that basis are left open for consideration de novo by the TPO in the set aside proceedings.*

Respectfully following the same, we direct Ld.TPO to compute ALP as directed hereinabove.

**Accordingly these grounds raised by assessee stands allowed for statistical purposes.**

10. **Ground No.3.1- 3.7** is in respect of the treatment of royalty paid by assessee to its AE by the authorities below.

10.1 The contentions raised by assessee is that assessee in its manufacturing activity uses various marketing intangibles, technology intangibles, process manuals and standards, quality standards etc which is owned by its AE-UK. It has been submitted that assessee also has access to subsequent product improvements and development through the licensing agreement which is significant benefit received by assessee which enables assessee to update the technological development in the market. He submitted that the license agreement entered into by assessee with its AE for use of these technologies in the manufacturing of products also grants assessee license to sell such manufactured products in India in domestic market. Ld.AR further submitted that on such sale in the domestic market, assessee is to pay 4.5% of the net revenues earned as per the terms and conditions of the exclusive license agreement.

10.2 He thus submitted that assessee while benchmarking the payment of royalty used CUP as most appropriate method. Referring to page 59 of TP documentation filed before us he demonstrated most appropriate method adopted by assessee. Ld.AR then pointed out that in TP order Ld. TPO wrongly held that assessee applied TNMM as most appropriate method for

benchmarking the transaction which is evident from page 9 of TP order. It has been submitted that Ld.TPO while concluding his remark on this issue proceeded on the footing that TNMM has been used as the most appropriate method.

10.3 Before DRP, it has been acknowledged that assessee has used CUP as the most appropriate method to determined arm's length rate of royalties paid to AE.

10.4 Ld.AR submitted that, both authorities below proceeded on the footing that, no evidence has been provided by assessee to prove any tangible benefit derived from being the royalty for the so-called superior technology.

10.5 Referring to pages of small paper book filed by Ld.AR submitted as additional evidences at the time of haring, which includes documents to establishes assessee as a licensed manufacturer, that products manufactured by assessee cannot be carried out without technological and R & D assistance from its AE, details establishing actual receipt of technical knowhow from its AE against which royalty is paid, details to prove that IPRs and know-how received from AE are confidential property of AE being guidelines, directions, screenshots etc, that helps assessee to manufacture the products.

It has been submitted that these documents were not placed before the authorities below and therefore requires consideration.

10.6 Ld.CIT DR supported Ld.AR, that based upon these documents, the issue needs to be reconsidered for establishing actual nature of payments made by assessee.

10.7. We have perused submissions advanced by both sides in the light of the records placed before us.

It is observed that assessee has placed substantial evidence which was not before the authorities below. We are therefore inclined to set aside this issue back to Ld.TPO/AO, for determination of this issue in the light of these documents vis-a-vis the agreement entered into by assessee with its AE under which the royalty has been paid. It has been observed that for assessment year 2006-07 in assessee's own case in *ITA No. 1415/be a NG/2010* vide order dated 07/06/19, the issue has been set aside on the basis of additional evidence filed by assessee for verification of the same. Respectfully following the same we are also inclined to set aside this issue back to Ld. TPO to verify the issue on basis of documents filed by assessee and to establish true nature of transaction regarding payment of royalty by assessee to its AE. Ld.TPO is directed to verify details and if necessary called for any further documents in order to establish the true nature of the transaction regarding the payment of royalties by assessee to its AE and consider the claim of assessee as per law.

**Accordingly these grounds raised by assessee stands allowed for statistical purposes.**

11. **Ground No. 4** has been not pressed by Ld.AR.

**Accordingly this ground stands dismissed as not pressed.**

12. **Grounds 5.1-5.7**

It is submitted that assessee during year accounted for sum of Rs.9,25 60,000/- as export turnover being unbilled revenue, which was yet to be billed and also claimed deduction under section 10 A.

It has been submitted that invoices were raised in the month of March 2008, and said amount has been realised by assessee during September 2008. The Ld. AO disallowed the claim of assessee by holding that assessee did not raise invoices within time stipulated under *Master circular No. 6/2010-11 dated 01/07/10 issued by RBI*. The view was held by DRP.

12.1 Ld.AR submits that assessee fulfilled requirement prescribed under RBI circular (supra). He submitted that assessee realised the sum within period of 6 months from the end of financial year or such further period as the competent authority May allow in this behalf. He submitted that 10A being a beneficial provision was introduced for purpose of increasing exports from India and to encourage establishment of export-oriented industrial undertaking in free trade zone

12.2 Ld.AR in support of his argument placed reliance upon decision of *Mumbai Tribunal dated 15/05/18* in case of *M/s.Tech Mahindra R&D Services Ltd vs DCIT* in *ITA No. 4462/M/2016* for *assessment year 2008-09*.

12.3 On the contrary Ld.DR submitted that, facts in case of assessee is distinguishable with that facts in case of *M/s.Tech Mahindra R&D Services Ltd vs DCIT(supra)* . It has been submitted that *M/s.Tech Mahindra R&D Services Ltd vs DCIT (supra)* in turn relied upon decision of *Madras Tribunal* in case of *iNautix Technologies India Pvt.Ltd., vs ACIT* in *ITA No. 541/Mds/2006* for *AY 2002-03 vide order dated 9/08/2011*. It has been submitted that in present case, income has not accrued to assessee of which invoices has been raised in March 2008.

12.4. We have perused submissions advanced by both sides in light of records placed before us.

Unbilled revenue means revenue that has been earned but not yet billed to customers as of the end of accounting year. It is very different from unearned revenue. When goods or services has been transferred to customers but customer payment is contingent based on a future event, this amount is generally referred to as an unbilled revenue. In our considered opinion export proceeds received on or brought into India in accordance with RBI guidelines satisfy requirements of section 10 A (3). Further

Section 10A (3) provides that competent authority being RBI can grant extension of time to receive unbilled amounts by assessee pertaining to a particular year.

40.1 Before us assessee has not been able to establish that RBI extended time period to receive income arising out of export of services declared during the year under consideration. In decisions relied upon by Ld.AR in case of *Tech Mahindra R&D Services Ltd* (supra), assessee therein received income within 6 months of invoice being raised and therefore this *Tribunal* held that revenue should be included in export turnover and also the total turnover.

In the facts of present case, assessee raised invoice in March 2008 that is end of subsequent financial year, for which assessee do not have any permission from RBI regarding extension of time. We are therefore unable to concur with the argument advanced by Ld.AR.

**Accordingly this ground raised by assessee stands dismissed.**

13. **Ground no.6**

This ground has been raised by assessee against disallowance of expenditure towards royalty under section 40 (a) which has already been disallowed under section 92CA of the Act.

It has been submitted that Ld.TPO made adjustment towards royalty under section 92CA of the Act holding that entire expenditure is not at arms length. Ld.AR submitted that assessee on its own disallowed the same under section 40 (a) (i) for non-deduction of TDS while determining total taxable income.

As we have already set aside the issue of royalty back to Ld.TPO for verification, this issue becomes academic in nature at this moment. Ld.AO is directed to verify submission in respect of suo-moto disallowance made by assessee under section 40 (a) (i) and to consider the claim as per law.

**Accordingly this ground raised by assessee stands allowed for statistical purposes.**

#### 14. **Ground No.7**

These grounds has been raised by assessee, is in respect of exclusion of telecommunication expenses while computing deduction under section 10 A of the act upheld by Ld. CIT (A).

Ld.AR placed reliance upon the decision of *Hon'ble Karnataka High Court* in case of *CIT vs Tata Elxsi Ltd* reported in 349 ITR 98 and submitted that this issue stands covered in favour of assessee.

On the contrary,Ld.CIT DR placed reliance upon the order passed by Ld.AO.

44. We have perused submissions advanced by both sides in the light of the records placed before us.

It is observed that, *Hon'ble Karnataka High Court* in case of *CIT vs Tata Elxsi Ltd(supra)* on identical issue held that telecommunication

expenses is to be included while computing deduction under section 10 A of the act as it is directly linked with earning of income. Ld CIT DR has not brought before us any contradictory/distinguishable facts in respect of present case before us.

Respectfully following *Hon'ble Karnataka High Court* in case of *CIT vs Tata Elxsi Ltd(supra)*, we direct Ld.AO to include telecommunication expenses while computing exempt income u/s10A of the Act.

**Accordingly the grounds raised by assessee stands allowed.**

**15. Ground No.8**

This issue has been raised by assessee against the disallowance made by Ld. AO of expenses incurred towards donation amounting Rs.2,65,000/-.

It has been submitted that assessee may donation to KIADB which was for Jigani welfare activities, where all manufacturing units of the company was situated. Assessee had two manufacturing units which claimed deduction under section 10A. It was submitted that if any disallowance was to be made it should have been made in respect of units as per the segmental financial statement filed by assessee. Ld.AR placed reliance upon decision of *Hon'ble Bombay High Court* in case of *CIT vs Gem Plus Jewellery India Ltd.*, reported in *(2011) 194 Taxmann 192* where it was held that exemption under section 10A had to be granted on enhanced income. The alternative plea thus raised by assessee was that consequential benefit under section 10A should be allowed if such disallowance is to be made.

Ld. DR submitted that the issue requires verification by Ld.AO.

We have perused submissions advanced by both sides in light of records placed before us.

It is observed that Ld.AO and DRP upheld disallowance for want of evidence.

Assessee is directed to file all requisite details and Ld.AO is directed to verify the same and consider the claim as per law.

**Accordingly this ground raised by assessee stands allowed for statistical purposes.**

16. **Ground nos.9-10** are consequential in nature and therefore do not require adjudication.

**In the result appeal filed by assessee stands partly allowed as indicated herein above.**

Order pronounced in the open court on 23-10-2019

Sd/-  
**(A.K.GARODIA)**  
**ACCOUNTANT MEMBER**

Dated: 23-10-2019

**\*am**

Copy of the Order forwarded to:

- 1.Appellant;
- 2.Respondent;
- 3.CIT;
- 4.CIT(A);
5. DR
6. ITO (TDS)
- 7.Guard File

Sd/-  
**(BEENA PILLAI)**  
**JUDICIAL MEMBER**

By Order

Asstt.Registrar



