

आयकर अपीलिय अधिकरण "ए" न्यायपीठ पुणे में ।
IN THE INCOME TAX APPELLATE TRIBUNAL "A" BENCH, PUNE

श्री डी. करुणाकरा राव, लेखा सदस्य, एवं श्री विकास अवस्थी, न्यायिक सदस्य के समक्ष ।
BEFORE SHRI D. KARUNAKARA RAO, AM AND SHRI VIKAS AWASTHY, JM

आयकर अपील सं. / ITA No. 885/PUN/2015
निर्धारण वर्ष / Assessment Year : 2005-06

M/s. Cognizant Technology Solutions India Pvt. Ltd.,
 (as a successor of Cognizant India Pvt. Ltd.),
 formerly T-Systems India Pvt. Ltd.,
 6th Floor, New No. 165, Old No. 110,
 Menon Eternity Building, St. Mary's Road,
 Alwarpet, Chennai – 600018

PAN : AACCT0773E

.....अपीलार्थी / Appellant

बनाम / V/s.

Deputy Commissioner of Income Tax,
 Circle – 7, Pune

.....प्रत्यर्थी / Respondent

आयकर अपील सं. / ITA No. 932/PUN/2015
निर्धारण वर्ष / Assessment Year : 2005-06

Dy. Commissioner of Income Tax,
 Circle – 1(1), Pune

.....अपीलार्थी / Appellant

बनाम / V/s.

Cognizant India Private Limited,
 9th Floor, Tower B, ICC Tech Park,
 S. No. 985, Senapati Bapat Road,
 Pune – 411016

PAN : AACCT0773E

.....प्रत्यर्थी / Respondent

Assessee by : Shri Percy Pardiwala
 Revenue by : Shri S.B. Prasad

सुनवाई की तारीख / Date of Hearing : 20-09-2019
 घोषणा की तारीख / Date of Pronouncement : 22-11-2019

आदेश / ORDER**PER VIKAS AWASTHY, JM :**

These cross appeals by the assessee and Revenue are directed against the order of Commissioner of Income Tax (Appeals)-13, Pune dated 26-03-2015 for the assessment year 2005-06.

2. The brief facts of the case as emanating from records are: The assessee company (formerly known as T-Systems India Private Limited) is a wholly owned subsidiary of T-Systems International GmbH, a German Company. T-Systems group is engaged in providing integrated telecommunication solutions viz. mobile communications, internet, fixed-line networks and system solutions, etc. The assessee is engaged in providing software development services to its group companies. The services provided by the assessee are broadly categorized in two segments i.e. :

- i. Software Development; and
- ii. Application Lifestyle Management (ALM) Services.

2.1 The assessment year 2005-06 is the first year of operation of assessee company. During the period relevant to assessment year 2005-06 the assessee entered into following international transactions with its group companies :

<i>Nature of the transactions</i>	<i>Amount (Rs.)</i>
<i>Provision of software development services to T-systems Group entities</i>	<i>3,22,82,358</i>
<i>Provision of application lifecycle management services to T-systems International</i>	<i>2,56,84,165</i>
<i>Provision of consultancy services by T-systems International on</i>	<i>19,58,465</i>

<i>behalf of T-systems India</i>	
<i>Procurement of IBM laptops from T-systems Singapore</i>	<i>17,20,795</i>
<i>Reimbursement of expenses and set up costs for the EPCOS project to T-systems Singapore</i>	<i>40,94,404</i>
<i>Payment of apartment rental fees to T-Systems International</i>	<i>1,35,075</i>
<i>Payment of guarantee fees to T-systems International</i>	<i>10,000</i>
<i>Procurement of licenses for software from T-systems International</i>	<i>4,41,352</i>
<i>Knowledge transfer from T-systems International</i>	<i>35,98,331</i>
<i>Provision of services by T-systems International in respect of validation and ABC analysis of curriculum Vitaes of prospective SAP consultants for T-systems India</i>	<i>8,11,913</i>
<i>Total</i>	<i>7,07,36,858</i>

2.2 To benchmark its international transactions under software development segment the assessee applied Comparable Uncontrolled Price (CUP) as the most appropriate method. The Transfer Pricing Officer (TPO) rejected the same and held that Transactional Net Margin Method (TNMM) is the most appropriate method. In ALM services segment the assessee applied TNMM as the most appropriate method which was accepted by the TPO. However, the TPO disturbed the comparables selected by the assessee to determine the Arm's Length Price (ALP) of the services rendered. The Assessing Officer passed the assessment order dated 14-11-2008 making additions in respect of international transactions as proposed by the TPO vide order dated 03-10-2008 passed u/s. 92CA(3) of the Act.

2.3 Aggrieved by the assessment order, the assessee filed appeal before the CIT(A). The CIT(A) upheld the findings of Assessing Officer in so far as the most appropriate method i.e. TNMM applied by the TPO in software development segment, however, under ALM services segment the CIT(A) included some of the comparables as suggested by the assessee, retaining

the comparables selected by the TPO. Further, the CIT(A) upheld the findings of TPO in not allowing adjustments on account of salary cost and travel cost. Now, both, the assessee and the Revenue are in appeal before the Tribunal assailing the findings of CIT(A).

3. We will first take up the appeal of assessee.

ITA No. 885/PUN/2015, (Assessee's Appeal)

4. Shri Percy Pardiwala appearing on behalf of the assessee submitted that the authorities below have erred in rejecting CUP as the most appropriate method for determining ALP of the international transactions entered into by the assessee with its group concerns under software development services. The ld. AR pointed that the TPO on the basis of information received from Syntel India has come to the conclusion that TNMM is the most appropriate method for determining ALP. The ld. AR pointed that the TPO in violation of principles of natural justice has not shared the information received from Syntel India with the assessee. The information received by the TPO from Syntel India is not available in public domain. Therefore, use of such information secretly is against the provisions of the Act. The ld. AR further submitted that the services rendered by the assessee to its group companies cannot be compared with Syntel India as the level of operation of both the companies is at variance. The ld. AR vehemently reiterated the contentions raised in paras 3.1 to 3.10 of the appeal against rejection of CUP as the most appropriate method. For the sake of ready reference we are reproducing the same :

“3.1 Ignoring the fact that differences in volume of fixed assets and turnover between the Appellant and Syntel India did not materially affect its prices in the market and therefore use of CUP was appropriate;

- 3.2 *Ignoring the significance of the average software industry billing rates published by software industry bodies and the comparability of such billing rates with the billing rates of the Appellant;*
- 3.3 *Concluding that the billing rates in the master service agreement between the Appellant and T- Systems Enterprise Services GmbH ('T - Systems Germany') should have been determined by factoring first year incremental operating costs of the Appellant and thereby completely ignoring the fact that the Appellant is not a completely risk mitigated entity earning a fixed return;*
- 3.4 *Concluding that 'individual agreements' as referred to in the master service agreement between the Appellant and T-Systems Germany and between Syntel India and T-Systems Germany were necessary for the purpose of establishing the comparability of the software development services rendered by T -System India and Syntel India and thereby completely ignoring the factual submissions of the Appellant that the terms and conditions of the services were covered by purchase orders and invoices submitted during the course of assessment proceedings;*
- 3.5 *Making a sweeping generalization that the invoices of the Appellant cannot be accepted as evidence due to variations in billing rates (on upward side) in a few invoices as compared to master service agreement and thereby ignoring the fact that the billing rates are in conformity in about 90% of the total invoices;*
- 3.6 *Presuming that the Appellant agreed to aggregation of its international transactions for TNMM analysis and thereby ignoring the Appellant's contention that the Appellant's CUP is the most appropriate method for benchmarking the international transaction pertaining to rendering of software development services;*
- 3.7 *Inferring that services rendered by the Appellant to T -Systems Germany are not comparable to the services rendered by Syntel India to T -Systems Germany based only on details of personnel charge out rates and thereby ignoring the fact that the rates for the deployed personnel are based on resource skill sets and experience and on the basis of different service platforms;*
- 3.8 *Inferring that the services rendered by the Appellant to T-Systems Germany are not comparable to the services rendered by Syntel India to T -Systems Germany without recording any specific finding of dissimilarity in the services based on the invoices, purchase orders and master service agreements;*
- 3.9 *Inferring that the services rendered by the Appellant and Syntel India are not comparable by erroneously comparing the service model and billing rates as per the EPCOS ALM service contract between the Appellant and T-Systems Germany with the service model and billing rates between Syntel India and T-Systems Germany (instead of comparing the Master Service Agreement between the Appellant and T-Systems Germany and between the master service agreements; and*

3.10 Not considering the certificate provided by T-Systems Germany certifying that the software development services provided by the Appellant and Syntel India to T-Systems Germany are similar in nature.”

5. In respect of ALM Services, the Id. AR submitted that the assessee had selected 19 companies as comparables in the TP study having average arithmetic mean of 6.08%. The TPO in transfer pricing proceedings accepted only two companies from the list of 19 companies selected by the assessee i.e. Sasken Network Systems Limited and VMF Softech Limited. The TPO selected two more companies i.e. Asian CERC Information Technology Limited and Bodhtree Consulting Ltd. The final set of comparables as per TPO are as under :

Sr. No.	Name of the company	PBIT/Operating Cost
1	Asian CERC Information Technology Limited	30.39%
2	Bodhtree Consulting Ltd.	24.01%
3	Sasken Network Systems Limited	16.19%
4	VMF Soft Tech Limited	35.70%
	ARITHMATIC MEAN	26.57%

5.1 In First Appellate proceedings the CIT(A) enlarged the list of comparables and included Gebbs Infotech Limited and Lanco Global Systems Limited taking the tally of comparables to six for determining the ALP under ALM service segments. The Id. AR furnished a chart giving the list of 12 comparables including the comparables selected by TPO and CIT(A) and submitted that if salary and travel cost adjustments are granted to the assessee, the margins would be within the tolerance limit.

5.2 The ld. AR submitted that the assessment year under appeal is the first year of operation therefore, there is exorbitant cost on account of travel of the employees. Since, most of the technical staff had to undergo training it resulted in significant loss of working hours and additional cost of travel. There was underutilization of resources due to non-availability of staff in the initial years. Further, to coordinate and establish the business in India the top management persons had to travel between India and Germany. The ld. AR further pointed that in the subsequent assessment years the expenditure on salary and cost of travel substantially reduced. In support of his contentions the ld. AR referred to chart giving details of travel and personal cost in the Financial Years 2004-05 to 2007-08. The same is reproduced herein below:

(Amount in Rs.)

Particulars	2004-05	2005-06	2006-07	2007-08	Total
Operating Revenue	6,14,33,854	47,35,20,494	96,45,18,087	1,78,52,65,951	3,28,47,38,386
Operating Cost	8,96,43,362	41,60,79,784	88,82,28,064	1,39,14,76,239	2,78,54,27,449
Travel Cost	3,59,37,113	8,35,49,049	12,33,99,805	20,46,94,855	44,75,80,822
Personnel Cost	4,36,52,943	23,85,82,773	52,18,41,443	77,09,50,328	1,57,50,27,487
% of Travel Cost to Operating Revenue	58	18	13	11	14
% of personnel cost to Operating Revenue	71	50	54	43	48

5.3 The ld. AR submitted that the Tribunal in various cases has allowed adjustments on account of under utilization of capacity in the first year of

operation. To support of his contentions the ld. AR placed reliance on the following decisions :

- i. Skoka Auto India (P) Ltd. Vs. Assistant Commissioner of Income-tax, 30 SOT 319 (Pune);
- ii. Ariston Thermo India Limited Vs. Dy. Commissioner of Income Tax in ITA No. 1455/PN/2010 for assessment year 2006-07 decided on 25-06-2013;
- iii. Ventura (India) Pvt. Ltd. Vs. Asst. Commissioner of Income Tax in ITA No. 1788/PUN/2014 for assessment year 2009-10 decided on 09-03-2018;
- iv. M/s. Saggezza India P Ltd. Vs. DCIT in ITA No. 3323/Mds/2016 for assessment year 2012-13 decided on 22-03-2017.

5.4 The ld. AR further submitted that the CIT(A) in Appellate proceedings has rejected assessee's claim of adjustment on the ground that if at all adjustment is to be made, it should be made to the comparables and not the tested party. The ld. AR submitted that even if adjustment is applied to the comparables, the assessee would be within the tolerance limits. The ld. AR contended that in so far as quantum of travel cost and salary expenditure is concerned they have not been disputed by the Department. It is only the allowability of adjustment while calculating operating cost is the point of contention.

6. On the other hand Shri S.B. Prasad representing the Department vehemently defended the impugned order. The ld. AR submitted that the assessee has merely reiterated the contentions raised before the CIT(A). The CIT(A) has considered all the submissions of assessee and has thereafter passed an order. The CIT(A) has granted substantial relief to the assessee by

including some of the comparables that are now being agitated by the Department in the cross appeals.

7. We have heard the submissions made by the representatives of rival sides and have perused the orders of the authorities below. The assessee is providing services to its overseas group companies under two segments i.e. :

- i. Software Development; and
- ii. Application Lifestyle Management (ALM) Services.

Software Development segment

8. Under this segment the assessee to benchmark its international transactions had selected CUP as the most appropriate method. The TPO rejected CUP applied by the assessee and adopted TNMM as the most appropriate method. The findings of TPO were upheld by the CIT(A). The contention of assessee is that the TPO had secretly received information from Syntel India. The said information was not available in public domain and hence the same cannot be applied against the assessee. We find merit in the primary contentions of assessee. No material can be utilized against the assessee without affording opportunity of proper representation. Since, the information from Syntel India was not available in public domain, the assessee was deprived of information being used against it. We are of considered view that fair opportunity should have been granted by the authorities below in line with the principles of natural justice. Accordingly, ground Nos. 3 to 5 of the appeal are restored back to the file of Assessing Officer/TPO for fresh adjudication. Accordingly, grounds of appeal No.3 to 5 are allowed for statistical purpose.

Application Lifestyle Management (ALM) Services.

9. In ground Nos. 6 and 7 of the appeal the assessee has assailed inclusion/exclusion of comparables for determining ALP of the transactions under ALM segment. However, during the course of submissions the ld. AR of assessee has not specified the comparables that need to be included/excluded in the final list of comparables. Accordingly, ground Nos. 6 and 7 of the appeal are dismissed.

10. In ground Nos. 8 and 9 of the appeal the assessee has assailed the method of computation of operating profit margin. The contention of assessee is that the authorities below have failed to grant adjustment on account of travel cost and salary cost of the employees. The assessment year under appeal is the first year of operation. The assessee has incurred substantial expenditure on training and travel of employees. The expenditure on training and travel has not been disputed by the Department. It is allowability of adjustment that has been denied to the assessee by the authorities below.

11. The Co-ordinate Bench of Tribunal in the case of *Ariston Thermo India Limited Vs. Dy. Commissioner of Income Tax (supra)* has allowed adjustment in the operating margin of assessee for low capacity utilization and high fixed operation cost in the initial year of operation. Similarly, in the case of *Ventura (India) Pvt. Ltd. Vs. Asst. Commissioner of Income Tax (supra)*, the Co-ordinate Bench has granted capacity utilization adjustment in the initial year of operation. Similar view has been taken in the cases of *Skoda Auto India (P) Ltd. Vs. Assistant Commissioner of Income Tax (supra)* and *M/s. Saggezza India P Ltd. Vs. DCIT (supra)*. Taking into consideration entirety of

facts and the decisions mentioned above, we are of considered view that the assessee deserves the benefit of adjustment in operating margins on account of substantial salary and travel cost in initial year of operation. The ground Nos. 8 and 9 of the appeal are restored back to the file of Assessing Officer/TPO for recomputation of operating margin after allowing adjustments as mentioned above. The assessee is directed to produce all relevant documents before the Assessing Officer/TPO in support of its claim. The Assessing Officer/TPO shall grant reasonable opportunity of hearing to the assessee before re-adjudicate the issue, in accordance with law. The ground No.8 and 9 of the appeal are allowed for statistical purpose.

12. In ground No. 10 of the appeal, the assessee has assailed the action of authorities below in not considering multiple year data. It is a well settled legal position that only data relevant to the corresponding single year has to be considered. We do not find any merit in ground No. 10 of the appeal. Accordingly, the same is dismissed.

13. In ground No. 11 of the appeal the assessee has assailed the initiation of penalty levied u/s. 271(1)(c) of the Act. The ground No. 11 of the appeal is pre-mature at this stage. Accordingly, the same is dismissed as such.

14. In ground No. 12 of the appeal, the assessee has assailed charging of interest u/s. 234B of the Act. Charging of interest u/s. 234B is consequential and mandatory, hence, ground No. 12 raised in appeal by the assessee is dismissed being devoid of any merit.

15. The ground Nos. 1 and 2 are general in nature, hence, require no adjudication.

16. In the result, appeal of the assessee is partly allowed for statistical purpose in the terms aforesaid.

ITA No. 932/PUN/2015, (Revenue's Appeal)

17. The Department in appeal has assailed inclusion of :

- i. Lanco Global Systems Limited;
- ii. Gebbs Infotech Limited; and
- iii. Asian CERC Information Technology Limited.

18. Both sides heard. Orders of the authorities below perused. In so far as the Lanco Global Systems Limited and Gebbs Infotech Limited, we do not find any infirmity in the order of CIT(A) in including the said companies in the list of comparables. The objection raised by the assessee i.e. information in respect of Gebbs Infotech Limited is not available in public domain is without any merit. The assessee at pages 468 to 479 of the paper book has furnished information regarding the services of Gebbs Infotech Limited. Accordingly, ground Nos. 2 and 3 of the appeal are dismissed being without any merit.

19. As regards inclusion of Asian CERC Information Technology Limited is concerned the said company has been included in the list of comparables by TPO itself. The same has been accepted by the CIT(A). We do not see any prejudice caused to the Revenue in CIT(A) accepting the comparable selected by the TPO. In our considered view the ground No. 4 of the appeal is misconceived and hence, needs to be rejected.

20. The ground Nos. 1, 5 and 6 of the appeal by Revenue are general in nature, hence, require no adjudication.

21. In the result, the appeal of Revenue is dismissed.

22. To sum up, the appeal of the assessee is partly allowed for statistical purpose and the appeal of Revenue is dismissed.

Order pronounced on Friday, the 22nd day of November, 2019.

Sd/-	Sd/-
(डी. करुणाकरा राव/D. Karunakara Rao)	(विकास अवस्थी / Vikas Awasthy)
लेखा सदस्य / ACCOUNTANT MEMBER	न्यायिक सदस्य / JUDICIAL MEMBER

पुणे / Pune; दिनांक / Dated : 22nd November, 2019
RK/GCVSR

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

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

//सत्यापित प्रति // True Copy//

आदेशानुसार / BY ORDER,

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