

**IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCHES : "B", BANGALORE**

**BEFORE SHRI J. SUDHAKAR REDDY, AM
AND
SMT.BEENA PILLAI, JM**

**ITA No.2093(Bang)/2017
(Assessment Year : 2012-13)**

M/s iPass India Pvt.Ltd.,
Level 5, Prestige Solitaire,
Brunton Road,
Bangalore-560 025.
PANNo.AABCG3659H

Appellant

Vs

The Deputy Commissioner of Income tax,
Circle-3(1)(1),
Bangalore

Respondent

And

**ITA No.2112(B)/2017
(Assessment year : 2012-13)
(By Assessee)**

**Appellant by : Shri Chavali Narayan, CA
Revenue by : Shri R.N.Siddappaji, Add.CIT**

Date of hearing : 16-07-2019

Date of pronouncement : 19-07-2019

ORDER

PER BEENA PILLAI, JUDICIAL MEMBER :

Present cross appeals has been filed by assessee as well as revenue against order dated 31/08/17 passed by Ld. CIT (A)-3, Bangalore for assessment year 2012-13 on following grounds of appeal;

2. ITA No.2093(B)/2017 (Assessment year 2012-13)

Based on the facts and circumstances of the case and in law, iPass India Private Limited (hereinafter referred to as 'Appellant'), respectfully craves leave to prefer an appeal against the appeal order passed by the learned Commissioner of Income Tax (Appeals) — 3 [hereinafter referred to as the 'learned CIT(A)'] under section 250 of the Income Tax Act, 1961 ('the Act') on the following grounds:

On the facts and circumstances of the case and in law:

- 1. The order of the learned CIT(A) is based on incorrect interpretation of law and facts, and therefore bad in law;*
- 2. The learned CIT(A) has erred, in law and in facts, by re-determining an addition of Rs.1,83.26,121 on account of adjustment to the arm's length price in respect of the international transaction relating to provision of software development services by the Appellant to its Associated Enterprise (AE):*
- 3. The learned CIT(A) has erred, in law and in facts, by not accepting the Appellant's plea in entirety and confirming with the learned Assessing Officer ('AO') / Transfer Pricing Officer ('TPO') on not accepting the economic analysis undertaken by the **appellant in accordance** with the provisions of the Act read with the Income Tax Rules, 1962 ('Rules').*
- 4. The CIT(A) has erred, in law and in facts, by upholding the action of the learned AO / TPO in determination of the arm's length margin/ price using only FY 2011-12 data which was not available to the Appellant at the time of complying with the transfer pricing documentation requirements;*

5. *The learned CIT(A) has erred, in law and in facts, by upholding the action of the learned AO / TPO in rejecting certain comparables considered by the Appellant in the comparability analysis by applying different quantitative and qualitative filters*

a) *The learned CIT(A) has erred, in law and in facts, by upholding the action of the learned AO/TPO in rejecting companies having turnover less than Rs.1 crore as a comparability criterion;*

b) *The learned CIT(A) has erred, in law and in facts, by upholding the action of the learned AO/ TPO in rejecting certain comparable companies identified by the Appellant for having different accounting year (i.e. companies having accounting year other than March 31 or companies whose financial statements were for a period other than 12 months);*

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

d) *The learned CIT(A) has erred, in law and in facts, by upholding the action of the learned AO/ TPO in rejecting certain comparable companies identified by the Appellant using export earnings greater than 75% of the sales as a comparability criterion:*

e) *The learned CIT(A) has erred, in law and in facts, by upholding the action of the learned AO/TPO in rejecting comparable companies identified by the Appellant wherein consolidated results have been used for analysis. The appellant had considered the consolidated results only in those cases where the software development services related income of the Indian operations constituted more*

than 75% of the consolidated company-wide / segmental revenues.

6. The learned CIT(A) has erred, in law and in facts, by upholding the action of the learned AO/ TPO in accepting / rejecting companies based on unreasonable comparability criteria;

7. The learned CIT(A) has erred, in law and in facts, by not making suitable adjustments on account of differences in the risk profile of the Appellant vis-a-vis the comparables. while conducting comparability analysis;

8. The learned CIT(A) has erred, in upholding the action of the learned AO/TPO in computing the arm's length price without giving benefit of +/-5 percent under the proviso to section 92C(2) of the Act:

9. The learned CIT(A) has erred, in confirming the imposition of interest under Section 234B of the Act;

10 The learned CIT(A) has erred, by upholding the initiation of penalty proceedings u/s 271(1)(c) of the Act.

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

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

3. ITA No. 2112/Bang/2017(Assessment year: 2012-13)

The order of the Id.CIT(A) is opposed to law and facts of the case..

1. The Id.CIT(A) erred in holding that negative working capital adjustment cannot be granted in the case of the assessee.

2. *The Id.CIT(A) ought to have considered that allowing working capital adjustment would result into better comparison.*
3. *The learned CIT(A) ought to have considered the fact that working capital adjustment is computed scientifically and negative or positive working capital adjustment is only consequential.*
4. *The appellant craves leave to add, alter, amend and / or delete any of the grounds mentioned above.*

2. Brief facts of the case are as under:

Assessee filed its return of income for year under consideration on 30/11/12. Subsequently, case was selected for scrutiny and notice under section 143 (2) and 142 (1) along with questionnaire was issued to assessee. In response to statutory notices, representative of assessee appeared before Ld.AO and filed requisite details as called for.

2.1 Ld.AO observed that assessee entered into international transaction with its AE's and accordingly a reference was made to transferring officer for determination of arm's length price of international transaction. On receipt of reference under section 92CA of the Act, Ld.TPO issued notice to assessee calling for economic details in respect of international transactions under section 92CA in Form 3 CEB.

2.2 Learn TPO observed that assessee is a wholly owned subsidiary of GoRemote International Corporation, USA and assessee is engaged in providing software development services that supplements the product offerings in Internet-based mobile office Communications services, to its associated enterprises

through, a master service agreement with iPass Inc. He observed that assessee has been remunerated on cost plus basis for the services rendered during year under consideration. Ld.TPO from details filed, observed that assessee applied TNMM as most appropriate method by using OP/OC as PLI and computed margin at 14.29% as against following 25 comparables which had average mean of 19.22%.

B.4 Comparables selected by Assessee and their arithmetic mean:

Sl. No.	Name of the company	Weighted Average (%)
1	<i>Akshay Software Technologies Limited</i>	12.93%
2	<i>Blue Star Infotech Limited</i>	15.14%
3	<i>Caliber Point Business Solutions Limited</i>	7.93%
4	<i>Cat Technologies Limited</i>	6.50%
5	<i>CG-VAK Software & Exports Limited</i>	0.30%
6	<i>Cigniti Technologies Limited</i>	8.73%
7	<i>Evoke Technologies Private Limited</i>	21.21%
8	<i>e-Zest Solutions Limited</i>	35.71%
9	<i>Goldstone Technologies Limited</i>	5.50%
10	<i>Helios & Matheson Information Technology Limited</i>	20.57%
11	<i>Larsen & Toubro Infotech Limited</i>	28.11%
12	<i>Maveric Systems Limited</i>	6.80%
13	<i>Mindtree Limited</i>	23.12%
14	<i>Persistent Systems & Solutions Limited</i>	22.93%
15	<i>Persistent Systems Limited</i>	35.17%
16	<i>R S Software (India) Limited</i>	23.47%
17	<i>R Systems International Limited</i>	16.38%
18	<i>Sasken Communication Technologies Limited</i>	33.26%
19	<i>Satyam Computer Services Limited</i>	20.18%

Sl. No.	Name of the company	Weighted Average (%)
20	Saven Technologies Limited	26.00%
21	Silverline Technologies Limited	15.18%
22	Thinksoft Global Services Limited	16.37%
23	Thirdware Solutions Limited	32.75%
24	Ybrant Digital Limited (Formerly known as LGS Global Limited)	16.59%
25	Zylog Systems Limited	29.63%
Arithmetical Mean		19.22%

3. Assessee thus held its transaction to be at arms length price as margin fell within plus -5% range. Ld.TPO by applying various filters, rejected certain comparables and reduced list comprising of following 10 comparables with average margin of 28.2%:

Ld. TPO thus computed adjustment as under:

Sl. No.	Name of the Company	Mark-up on Total Costs (OP/OC) (WC-unadj) (in %)	Mark-up on Total Costs (OP/OC) (WC-adj) (in %)
1	Datamatics Global Services Limited	14.57	22.24
2	Genesys International Corp. Limited	30.09	32.70
3	ICRA Techno Analytics Limited	17.24	23.44
4	Infosys Limited	43.10	48.68
5	Larsen & Toubro Infotech Limited	25.47	32.76
6	Mindtree Limited	15.01	22.20
7	Persistent Systems Limited	27.20	34.11
8	R S Software (India) Limited	15.34	24.96

Sl. No.	Name of the Company	Mark-up on Total Costs (OP/OC) (WC-unadj) (in %)	Mark-up on Total Costs (OP/OC) (WC - adj) (in %)
9	Sasken Communication Technologies Ltd.	12.15	20.67
10	Spry Resources India Pvt. Ltd.	26.18	18.48
AVERAGE MARGIN		22.63%	28.02%

Ld.TPO also computed negative working capital adjustment.

4. Aggrieved by adjustment proposed by Ld.TPO assessee preferred appeal before Ld.CIT (A). Ld.CIT on going through objections raised by assessee excluded two comparables being, Datamatics Global Services Ltd and ICRA Techno Analytics Ltd., and upheld the balance 8 comparables.

4.1 Aggrieved by order of Ld.CIT (A) assessee as well as revenue is in appeal before us now.

Assessee's appeal

5. At the outset Ld.AR submitted that **Ground No. 1-5** are general in nature and do not require any adjudication.

Ground No. 6 is in respect of comparables objected by assessee.

It has been submitted that in the event following four comparables are excluded, assessee is within range of +/-5%:

- Genesis International Corporation Ltd
- Infosys Ltd
- Larsen and Toubro Infotech Ltd
- Persistent Systems Ltd

5.1 Before we dwelve into comparability analysis, it is *sine qua non* to understand functions performed assets owned and risk assumed by assessee before us.

6. Functions in TP study, it has been observed that assessee is a wholly owned subsidiary of GoRemot international Corporation, USA which was subsequently acquired by iPass U.S. in February 2006. Assessee is 100% export oriented unit

and is a member of STPI scheme at Bangalore. In TP study assessee has been held to be providing software development services to iPass U.S. and is remunerated on cost +16 % basis for services rendered. Functions performed by assessee under this segment are coding and documentation, project management, testing and quality assurance. It has been submitted in TP study that release of software products/feature by assessee is in form of a package. Once all software modules are fully tested and integrated, a team within the quality assurance department of assessee proceeds with packaging the features are developed and releases it to iPass U.S. iPass U.S. confirms whether modules/documentations are as per specifications provided, and if any errors are identified by AE, assessee has to correct the same and corrected version is required to be delivered within time agreed upon between assessee and AE. It is observed that AE is responsible for final release of software to customer, after approval by the Change Management Board as per the terms of contract.

Assets used: All trademarks and trade names, logos and goodwill associated with AE and assessee does not undertake any marketing activities as it does not create any marketing

intangibles. Assessee therefore owns usual assets like computers office equipments furniture fixtures etc.

Risks

It is observed in TP study that assessee undertakes bare minimal risk only in respect of remuneration as it is received in foreign exchange. Otherwise all risk service liability risk, product liability risk, credit and collection risk etc are borne by AE.

Thus assessee is characterized to be functioning in a risk mitigated environment which does not carry out significant entrepreneurial activities nor does it bear significant risk associated with such activities. Accordingly assessee has been characterised as a risk mitigated contract service provider for provision of software development services.

From TP order, it is observed that Ld.TPO do not dispute to this functional analysis carried out in TP study. With this FAR analysis of assessee, we shall undertake comparability of assessee with comparables objected for inclusion.

7. At the outset Ld. AR submitted that these comparables have been considered by this Tribunal vide order dated 14/06/19 passed in case of *VeriSign Services India Pvt.Ltd., in ITA No. 3151/Bang/2018 for assessment year 2012-13 placed at page 779-790 of paper book.*

8. Genesis International Corporation Ltd

It has been submitted that this company is functionally not comparable with that of assessee as it is engaged in geophysical information systems, photogrammetry, remote sensing, cartography etc. Ld.AR submitted that all these functions

performed by this company are KPO services and owns huge intangibles.

8.1 Ld.AR also submitted that this company has been considered by this Tribunal in case of *CGI Information Systems and management consultants Ltd vs ACIT* in ITA No. 183/Bang/2017 in order dated 11/04/18, wherein this company has been excluded for the reason that it is rendering GIS-based services and does not have any segmental results. It is also been held therein that presence of intangibles are indicative of the fact that this company is not in software development services.

8.2. Ld. CIT DR on the contrary placed reliance upon the orders of authorities below.

8.3. We have perused submissions advanced by both sides in the light of the records placed before us. Assessee in the paper book has placed website extract of this company at page 338 wherein it has been shown to be developing various cutting edge applications by deploying state of the art GIS technologies and allied special data acquisition, processing and integration techniques to meet demand of customer.

8.4 Thus, we are of considered opinion, that this company is functionally not similar with that of assessee. Respectfully following decision of this Tribunal in case of *VeriSign services India private limited(Supra)* we direct Ld. TPO to exclude this company from finalist.

9. Infosys Ltd

It has been submitted by Ld.AR that this company has been included by ld.TPO though it is not comparable with that of

assessee, as it is a huge company owning large intangibles. It has been submitted that *Delhi ITAT in case of Agilis Information Technologies India Private Limited vs ACIT reported in (2018) 89 taxman.com 440* has excluded this company and the same has been upheld by *Hon 'ble Delhi High Court*.

9.1 Ld. CIT DR placed reliance upon orders passed by authorities below and insisted on the inclusion of this company.

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

It is observed that *Delhi ITAT in case of Agilis Information Technologies India Private Limited (supra)* has held as follows:

“Infosys Ltd was excluded from the list of comparable companies by following the decisions of orderable Delhi High Court in case of Agnity India technologies private limited reported in 36 Taxmann.com 289. The discussion is contained in paragraph 4.5 to 4.7 of the tribunal’s order. The tribunal accepted that Infosys is a giant risk ranking company and engaged in development and sale of software product and also owns intangible assets and therefore not comparable with a software development service provider such as assessee in that case.”

Respectfully following the same we are of considered opinion that this company deserves to be excluded from the final list.

10 Larsen and Toubro Infotech Ltd

It has been submitted by Ld. counsel that this company has been included by ld.TPO though it is not comparable with that of assessee, as it is huge company owning large intangibles. It has been submitted that *Delhi ITAT in case of Agnity Inida*

Technologies Private Limited (Supra) has excluded this company and the same has been upheld by *Hon'ble Delhi High Court*.

10.1. Ld. CIT DR placed reliance upon orders passed by authorities below and insisted on the inclusion of this company.

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

It is observed that Delhi ITAT in case of *Aginity India Technologies India private limited (supra)* has held as follows:

“Larsen and Toubro Infotech Ltd was excluded from the list of comparable companies by relying on the decision of the Delhi bench ITAT in case of Saxo India d vs ACIT. The discussion is contained at para 4 .8 to 4.10 of tribunal’s order. The tribunal held that LMT Infotech Ltd was software product company and segmental information on SWT services was not available. The tribunal also notice that appeal filed by revenue against rivals order was dismissed by orderable Delhi High Court in ITA No. 682/2016”.

Respectfully following the same we are of considered opinion that this company deserves to be excluded from the final list.

11. Persistent Systems Ltd

This company has been included by ld.TPO and assessee dispute its function similarity with assessee. It has been submitted that this company during year under consideration derived income from licensing of products, royalty and sale of products, maintenance contract, outsourced product development etc and no segmental details are available in regards to the same.

11.1. Ld. CIT DR placed reliance upon the orders passed by authorities below and insisted on the inclusion of this company.

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

It is observed that Delhi ITAT in case of *Aginity India Technologies India private limited (supra)* has held as follows:

“Persistent systems Ltd was excluded from the list of comparable companies on the ground that this company was a software product company and segmental information on SWT services was not available. The tribunal in coming to the above conclusion referred to the decisions rendered by ITAT Delhi benches in case of cash edge India private limited vs ITU in ITA No. 64/del/2015 wide order dated 23/09/15 and the details of orderable Delhi High Court in case of sexual India private limited (supra). The findings in this regard are contained in paragraph 4.14 to 4.16 of its order.”

Respectfully following the same we are of considered opinion that this company deserves to be excluded from the final list.

Accordingly ground No. 6 of assessee’s appeal stands allowed.

It has been submitted that **Ground No. 7-10** are not pressed and accordingly they are dismissed.

In the result appeal filed by assessee stands partly allowed.

Revenue’s appeal

12. **Ground No. 1** is general in nature and therefore do not require any adjudication.

13. Both parties submitted that only effective ground in revenue's appeal is in respect of **Ground No. 2-4** is in respect of negative working capital adjustment worked out by the Ld. AO/TPO.

14. Ld.AR submits that this issue stands covered in favour of assessee by decision of this Tribunal in case of *F & F India Private Limited in ITA No.195/Bang/2016 & 495/Bang/2017 for assessment year 2011-12 and 2012-13 passed on 03/07/19.*

14.1 Ld. CIT DR placed reliance upon the authorities below however could not controvert that this issue is covered by decisions relied upon by Ld.AR.

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

14.2 We have also perused the decision relied upon by Ld. counsel. It is observed that this issue has been decided by this Tribunal in *F & F India Pvt.Ltd.,(Supra)* as under:

"14. Ground No.11 : Negative Working Capital adjustment - Making a negative working capital adjustment without appreciating the fact that the company does not bear any working capital risks. On this issue, the assessee submitted as under :

"The learned TPO determined the ALP for the international transactions with A.Es by making a negative working capital adjustment for the differences in working capital between the assessee and the companies considered as comparables. The assessee does not agree with the learned TPO as the company does not bear any working capital risk since it is been fully funded by it's A.E. from its inception and has no working capital

contingencies. The company has never taken any loans till date from the date of incorporation nor has incurred any expense for meeting the working capital requirement."

We have gone through the submissions and the order of the TPO. The assessee pleaded that the DRP has acceded such a plea in some other case. On examination, we find that the DRP, Hyderabad in the case of Cordys Software India P. ltd., for A.Y. 2008-09 in its directions dated 03.08.2012 has given a finding as under :

"7.7. 4 Thus, working capital adjustment is made for the time value of money lost when credit time is provided to the customers. The applicant is not an entrepreneur but a captive service provider. Its entire funding needs are provided by the A.E. This being so, the applicant does not stand to lose anything as it is compensated on a total cost plus basis. The TPO probably was carried away by the large amount of receivables appearing in the books of the applicant. But the applicant is running its business without any working capital risk while comparable companies have such a risk for them. If at all any working capital adjustment is to be made to this situation, only a positive adjustment has to be made to the comparables so that they are brought on par with the applicant. In view of the same, the Panel directs that negative working capital adjustment to the arithmetic mean margin of the comparables shall not be made."

In view of the above, the Panel directs that negative working capital adjustment to the arithmetic mean margin of the comparables shall not be made."

In view of the above, we are of the opinion that assessee's case being similar, there is no need for making any negative working capital adjustment when assessee does not carry any working capital risk. In fact, TPO should have done necessary working capital adjustment to the profits of the selected comparables so as to make them comparable to the assessee. In view of this, we direct the TPO not to make negative working capital adjustment".

Respectfully following the same we direct Ld.AO to grant working capital adjustment as discussed hereinabove. Accordingly this ground raised by revenue stands dismissed. In the result, the appeal filed revenue stands dismissed.

Order pronounced in the open court on 19-07-2019

Sd/-
(J. SUDHAKAR REDDY)
ACCOUNTANT MEMBER
Dated: the 19th July, 2019.

Sd/-
(BEENA PILLAI)
JUDICIAL MEMBER

***am**

Copy of the Order forwarded to:

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

By Order

Asst.Registrar