

**IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCHES "C", BANGALORE**

Before Shri B.R.Baskaran, AM & Shri Pavan Kumar Gadale, JM

IT(TP)A No.1838/Bang/2016
Asst. Year : 2012-2013

M/s.Applied Materials India Private Limited, Unit – 5, 3 rd Floor, Explorer Building International Tech Park, Whitefield Road, Bangalore – 560 001. PAN : AAECA2635C.	Vs.	The Income Tax Officer Ward 1(1)(4) Bangalore.
(Appellant)		(Respondent)

Appellant by :Smt.Tanmayee Rajkumar, Advocate
Respondent by :Sri.Vilas S.Shinde, CIT-DR

Date of Hearing :04.02.2020	Date of Pronouncement : 05.02.2020
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ORDER

Per B.R.Baskaran, AM :

The assessee has filed this appeal challenging the assessment order passed for the assessment year 2012-2013 by the Assessing Officer u/s 143(3) r.w.s. 144C of the I.T.Act, in pursuance of the directions given by the learned Dispute Resolution Panel (DRP).

2. Though the assessee has raised many grounds, the learned AR restricted her arguments in respect of ground No.4, ground No.5.12 and ground No.5.13. In ground No.5.12 also, the learned AR canvassed for inclusion of only two comparable companies, viz., Powersoft Global Solutions Limited and Evoke Technologies Private Limited. The learned AR made a statement

at bar that the assessee is not pressing other grounds. The ground pressed by the learned AR, viz., ground no.4, 5.12 and 5.13 read as under:-

“4. **Determination of Net Cost Margin of the Appellant**

The Ld.AO/Ld.TPO had erred on facts and in law in not acknowledging that the sub-contracting charges incurred by the Appellant represents arm's length consideration and was thereby required to be considered as pass-through cost and that the same thus ought to have been excluded from the Appellant's operating costs and income while computing the arm's length price. The Ld.Panel erred in confirming the same.

*5.12 The Ld.AO/Ld.TPO /Ld.Panel erred in arbitrarily rejecting Akshay Software Technologies Ltd., L G S Global Ltd., Powersoft Global Solutions Ltd., Helios & Matheson Information Technology Ltd., R Systems International Ltd., and Evoke Technologies Pvt. Ltd. despite these companies being functionally comparable to the Appellant. The Ld.Panel also erred in confirming the same.***

5.13 The Ld.AO/Ld.TPO erred in including Persistent Systems Ltd. and Larsen and Toubro Limited as comparables, despite these companies being functionally incomparable to the Appellant. The Ld.Panel erred in confirming the same.”

*(** As noticed earlier, only two companies, viz., Powersoft Global solutions and Evoke Technologies P Ltd are pressed)*

3. The assessee-company is engaged in the business of providing software development and engineering services including technical product services and design services to its

holding company. It is wholly owned subsidiary of Applied Materials Inc., USA, which is a supplier of products and services to the global semiconductor industry.

4. The issues urged herein relate to the transfer pricing adjustment made in respect of providing of software development services by the assessee to its AE. The assessee had adopted TNMM method as the most appropriate method and operating cost by total cost as profit level indicator. The TPO accepted the TNMM method as well as profit level indicator of the assessee. The assessee had computed arithmetical mean of 12.52 % in respect of comparables owing PLI of the assessee was 18.16%. Accordingly, the claim that its international transactions relating to software development services is at arm's length.

5. Rejecting the TP study of the assessee, the TPO selected following 10 comparables:-

Sl. No.	Name of the Company	Mark-up on Total costs (WC-unadj) (in %)	Mark-up on Total costs (WC-adj) (in %)
1.	Datamatics Global Services Ltd.	14.57	15.25
2.	Genesys International Corporation Ltd.	30.09	25.94
3.	ICRA Techno Analytics Ltd.	17.24	16.42
4.	Infosys Ltd.	43.10	42.30
5.	Larsen & Toubro Infotech Ltd.	25.47	25.96
6.	Mindtree Ltd. (seg)	15.01	15.21
7.	Persistent Systems Ltd.	27.20	27.37
8.	R S Software (India) Ltd.	15.34	18.04
9.	Sasken Communication Technologies Ltd.	12.15	13.57
10	Spry Resources India Pvt. Ltd.	26.18	11.41
	AVERAGE MARK-UP	22.63	21.15

6. The TPO computed average mark-up of comparable companies selected by him at 21.15% after giving working capital adjustment, and accordingly, proposed transfer pricing adjustment of Rs.23.20 crore.

7. The learned DRP directed exclusion of following comparable companies :-

Sl. No.	Name of the Company	Mark-up on Total costs (WC-unadj) (in %)	Mark-up on Total costs (WC-adj) (in %)
1.	Datamatics Global Services Ltd.	14.57	15.25
2.	Genesys International Corporation Ltd.	30.09	25.94
3.	ICRA Techno Analytics Ltd.	17.24	16.42
4.	Infosys Ltd.	43.10	42.30
5.	Sasken Communication Technologies Ltd.	12.15	13.57
6.	Spry Resources India Pvt. Ltd.	26.18	11.41

8. The Assessing Officer, accordingly, passed the order as per the directions given by the DRP. Aggrieved by the order so passed, the assessee filed this appeal before the Tribunal.

9. The ground No.4 relates to the claim of the assessee that sub-contracting charges incurred by the assessee should be given pass-through status and hence, should be excluded from the operating cost and income while computing arm's length price. The learned AR fairly admitted that the assessee made identical claim in the immediately preceding assessment year,

i.e., assessment year 2011-2012 and it has been rejected by the Tribunal.

10. We heard the learned Departmental Representative on this issue and perused the record. We noticed that identical issue was considered by the co-ordinate Bench of the Tribunal in assessee's own case for assessment year 2011-2012 in IT(TP)A No.17/Bang/2016 dated 21.09.2016 and the same has been decided against the assessee with the following observations:-

“7. We have considered the rival submissions as well as the relevant material on record. Undisputedly, the assessee is charging a mark up on the software development services provided to the AE being captive service provider. Therefore the assessee is not acting as an agent or distributor of the AE but is a provider of services of its own. It is not the case of rendering services of an agent without any value addition but the assessee is providing software development services to the AE and charging margin on the same. Therefore the cost on the software development activity is incurred by the assessee and charging the AE on the said services with a mark up of 10% on cost. The cost of sub-contracting in software development services is also charged with 10% mark up to the AE. When the margin on the cost of sub-contracting charges is part of the operating revenue of the assessee then only the cost of sub-contracting activity cannot be excluded as pass through. It would amount to artificially inflate the margins of the assessee on the other revenue from the services other than sub-contracting activity. In any case, pass through cost can be considered only when the activity of providing services to the AE does not involve value addition on the part of the AE. The decision of the Delhi Benches of the Tribunal in the case of DCIT Vs. Cheil Communications India Pvt. Ltd. (supra) would not help the case of the assessee as in the said case the activity of the assessee was only a distributor without any value addition. It is pertinent to note that outsourcing cost in software development services activity is part and parcel of cost of providing the

service to the AE and cannot be separated from the operating cost and operating revenue of the said segment of services. Accordingly, the cost of software development services cannot be treated in this fashion as claimed by the assessee. Hence we do not find any merit or substance in the contention raised by the assessee on this issue.”

10.1 Since there is no change in facts relating to this claim, consistent with the view taken by the co-ordinate Bench, we also reject this ground of the assessee.

11. In ground No.5.12, the assessee seeks inclusion of only two companies, viz., Powersoft Global Solutions Limited and Evoke Technologies Private Limited, even though some more companies also mentioned in the ground.

12. With regard to these two companies, according to the learned AR, the Tax Authorities have rejected the claim for inclusion of them as comparables only for the reason that financial data relating to these two companies are not available. The learned AR submitted that the assessee has, in fact, furnished relevant financial data of these companies before Tax Authorities, but they have overlooked the same. The learned AR submitted that the assessee has furnished the financial details of these companies in the paper book filed by the assessee.

13. We heard the learned DR on this issue and perused the record. Since the assessee submits that the financial details of these two companies are available on record, we are of the view that these two companies should be restored to the file of the AO / TPO for examining the claim of the assessee for their

inclusion as comparables. Accordingly, we restore these two companies to the file of the AO / TPO.

14. In ground No.5.13, the assessee seeks exclusion of two companies, viz., *Persistent Systems Limited and Larsen and Toubro Infotech Limited*. The learned AR submitted that these two companies have been excluded in assessee's own case in assessment year 2011-2012 by the Tribunal. However, in respect of assessment year 2012-2013, these two companies have not been considered as good comparables by the Tribunal in the case of *M/s.CGI Information Systems and Management Consultants Pvt. Ltd. v. ACIT [IT(TP)A Nos.586/Bang/2015 & 183/Bang/2017 for assessment year 2010-2011 and 2011-2012 – order dated 11.04.2018]*.

15. We heard the learned DR and perused the record. We noticed that *M/s.CGI Information Systems and Management Consultants Pvt. Ltd.* (supra) is also engaged in the business of providing contract software development services and information technology enabled services to its holding company, as captive service provider. We noticed that the coordinate Bench, in the above said case, has followed the decision rendered by the Delhi Bench of the Tribunal in the case of *Agilis India Technologies (P.) Ltd. v. ITO [(2018) 89 taxmann.com 440 (Delhi-Trib.)]* in excluding both the companies referred above. The co-ordinate bench noticed that *M/s.Agilis India Technologies (P.) Ltd.* was also capital service provider to its AE and the Delhi Bench of the Tribunal had excluded *Larsen & Toubro Infotech Limited* and *Persistent*

Systems Limited, holding them as not good comparables. For the sake of convenience, the decision rendered by the coordinate Bench in respect of these two companies in the case CGI Information Systems and Management Consultants Pvt. Ltd. (supra) are extracted below:-

“29. We have considered the rival submissions. In the case of Agilis Information Technologies India (P) Ltd., (supra), this Tribunal considered the comparability of the 3 companies which the Assessee seeks to exclude from the final list of comparable companies chosen by the TPO. The functional profile of the Assessee and that of the Assessee in the case of Agilis Technologies India (P) Ltd., is identical in as much as the said company was also involved in providing SWD services to its AE and the TPO had chosen some comparable companies which were also chosen by the TPO in the case of the Assessee for the purpose of comparability. In the aforesaid decision the Tribunal held on the comparability of the 3 companies which the Assessee seeks to exclude as follows:

(a).....

(b) Larsen & Toubro Infotech Ltd., was excluded from the list of comparable companies by relying on the decision of the Delhi Bench of ITAT in the case of Saxo India (P) Ltd. Vs. ACIT (2016) 67 taxmann.com 155 (Del-Tri). The discussion is contained in paragraphs 4.8 to 4.10 of the Tribunal’s order. The Tribunal held that L & T Infotech Ltd., was a software product company and segmental information on SWD services was not available. The Tribunal also noticed that the appeal filed by the revenue against the tribunal’s order was dismissed by the Hon’ble Delhi High Court in ITA No.682/2016.

(c) 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 SWD services was not available. The Tribunal in coming to the above conclusion referred to the decision rendered by ITAT Delhi Bench in the case of Cash Edge India Pvt.Ltd. Vs. ITO ITA No.64/Del/2015 order dated 23.9.2015 and the decision of Hon’ble Delhi

High Court in the case of Saxo India Pvt.Ltd. (supra). The findings in this regard are contained in Paragraphs 4.14 to 4.16 of its order.

30. Respectfully following the decision of the Tribunal we hold that the aforesaid 3 companies be excluded from the final list of comparable companies for the purpose of arriving at the arithmetic mean of comparable companies for the purpose of comparison with the profit margins. In this regard we are also of the view that the plea of the learned DR for a remand of the issue to the DRP on the ground that the DRP has not given any reasons in its directions cannot be accepted. The DRP has endorsed the view of the TPO in its directions and therefore the reasons given by the TPO should be regarded as the conclusions of the DRP.”

15.1 In the instant case also, the assessee is a captive service provider of software services to its AE. There is no dispute that the facts are identical in the assessee's case and in the cases decided by the co-ordinate bench. Accordingly, respectfully following the decision of the co-ordinate Bench rendered in the case of CGI Information Systems and Management Consultants P Ltd (supra), we direct the AO / TPO to exclude Larsen & Toubro Infotech Limited and Persistent Systems Limited from the final list of comparables.

15.2 Since the ALP of the international transaction relating to software development services are to be determined afresh in the light of our decisions rendered above, we restore this issue to the file of the AO / TPO.

16. In the result, the appeal filed by the assessee is treated as partly allowed for statistical purposes.

Order pronounced on this 05th day of February, 2020.

Sd/-
(Pavan Kumar Gadale)
JUDICIAL MEMBER

Sd/-
(B.R.Baskaran)
ACCOUNTANT MEMBER

Bangalore; Dated :05th February, 2020.
Devadas G*

Copy to :

1. The Appellant.
2. The Respondent.
3. The DRP-1, Bengaluru.
4. The Pr.CIT-1, Bengaluru.
5. The DR, ITAT, Bengaluru.
6. Guard File.

Asst.Registrar/ITAT, Bangalore