

**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "J", MUMBAI**

**BEFORE SHRI VIKAS AWASTHY, JUDICIAL MEMBER AND
SHRI N.K. PRADHAN, ACCOUNTANT MEMBER**

ITA NO. 669/MUM/2014 : A.Y : 2009-10

DCIT-8(3),
Mumbai (Appellant)

Vs. M/s. SmartStream
Technologies India Pvt. Ltd.
B-13, 2nd floor, Plot No. B-13,
New Link Road, Andheri (W),
Mumbai 400 020.
(Respondent)

ITA NO. 1098/MUM/2014 : A.Y : 2009-10

M/s. SmartStream Technologies
India Pvt. Ltd.
B-13, 2nd floor, Plot No. B-13, New
Link Road, Andheri (W),
Mumbai 400 020. (Appellant)

Vs. DCIT-8(3),
Mumbai (Respondent)

**CO NO. 40/MUM/2014 : A.Y : 2009-10
(in ITA NO. 669/MUM/2014)**

M/s. SmartStream Technologies
India Pvt. Ltd.
B-13, 2nd floor, Plot No. B-13,
New Link Road, Andheri (W),
Mumbai 400 020. (Cross Objector)

Vs. DCIT-8(3),
Mumbai (Org. Appellant)

**Assessee by : Shri Milin D. Thakore &
Ms. Nyrica Trikannad**

**Revenue by : Shri Uodal Raj Singh &
Shri A. Mohan**

Date of Hearing : 20/01/2020

Date of Pronouncement : 31/01/2020

ORDER**PER VIKAS AWASTHY, JM**

These cross appeals by the Department and the assessee are directed against the assessment order dated 20.12.2013 passed under Section 143(3) read with section 144C of the Income Tax Act, 1961 (hereinafter referred to as 'the Act'). The assessee has also filed cross-objection in the appeal filed by the Revenue.

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2. Shri Milin D. Thakore with Ms. Nyrica Trikannad appearing on behalf of the assessee submitted at the outset that the appeal of Revenue is liable to be dismissed on account of low tax effect in the light of recent CBDT Circular No. 17/2019 dated 08.08.2019. The learned AR further submitted that if the appeal of Revenue is dismissed, the cross objection filed by assessee would become infructuous.

3. Shri Uodal Raj Singh & Shri A. Mohan representing the Department fairly admitted that the appeal of Revenue has tax effect less than Rs. 50 lacs, therefore, the same would be covered by CBDT Circular no. 17/2019 (supra).

4. Both sides heard. The learned AR has filed calculation sheet indicating tax effect involved in the appeal by Revenue. As per computation, the tax effect involved in the appeal is Rs.11,90,734/-. The learned DR has admitted that the appeal of Revenue suffers from low tax effect in view of latest CBDT Circular. Undisputedly, the tax effect involved in appeal is less than the monetary limit prescribed by the recent CBDT Circular No. 17/2019 (supra) for

filing of appeals before the Tribunal by the Department. The CBDT vide circular dated 08.08.2019 (supra) has amended para 3 of Circular no. 3 of 2018 dated 11.07.2018 thereby enhancing monetary limit of tax effect from Rs.20 lacs to Rs.50 lacs for filing of appeals by the Department before the Tribunal. Thus, without going into merit of the issues raised in the appeal, the present appeal of the Revenue is dismissed on account of low tax effect.

5. Before parting, we clarify here that the Revenue shall be at liberty to approach the Tribunal for restoration of appeal, with the requisite material to show that the appeal is protected by the exceptions provided in para 10 of the Circular dated 11.07.2018 and its amendment dated 20.08.2018. The appeal of Revenue is accordingly dismissed on account of low tax effect.

6. The assessee has filed cross objection supporting the assessment order on issues against which Revenue is in appeal. Since the appeal of Revenue has been dismissed, the cross objection filed by assessee has become infructuous and the same is dismissed as such.

7. In the result, appeal of Revenue and the cross objection of assessee are dismissed.

ITA No. 1098/Mum/2014

8. The learned AR stated at the outset that in this appeal he would not be pressing ground nos. 1, 4 to 7 and additional ground no. 8 of the appeal. Thus, the only grounds he would be pressing are ground nos. 2, 3 and additional ground no. 9.

9. The grounds for which the learned AR has made his submissions read as under :-

“2. Rejection of benchmarking analysis performed by the Appellant

2.1 The learned AO erred on facts and in law in upholding the direction of DRP in confirming the rejection of the benchmarking analysis of the Appellant presented in its Transfer Pricing documentation (‘TP Study’), without giving any cogent reason for their rejection and without establishing the deficiency or inefficiency in the documentation of the Appellant.

2.2 The learned AO erred on facts in upholding the direction of DRP in confirming the rejection of the independent comparable companies selected by the Appellant in its TP Study without providing any cogent reason.

3. Inappropriate approach adopted by the TPO

3.1 The learned AO erred on facts in upholding the direction of DRP in confirming the comparable companies selected by the TPO, without having regard to the functions performed, assets employed and risks assumed.

3.2 The learned AO erred on facts and in law in upholding the direction of DRP in confirming that the TPO had not violated the rules of natural justice by not providing/sharing the complete details of the benchmarking analysis carried out by him including the manner of obtaining and disclosure of information called for under section 133(6) of the Act.

3.3 The learned AO erred on facts and in law in upholding the direction of DRP in not appreciating that, in conducting the fresh comparability analysis, the TPO has erred in using data which was not available as on the specified date (as defined in Section 92F(iv) of the Act read with Rule 10B(4) of the Income tax Rules, 1962 (‘the Rules’).

Thus, the Appellant prays that the fresh benchmarking analysis conducted by the learned TPO is liable to be quashed.”

Additional Ground of Appeal :

“9. The appellant submits that the following comparables which are not functionally comparable with the appellant should be excluded :

- i) *Acropetal Technologies Limited*
- ii) *Cepha Imaging Private Limited*
- iii) *Polaris Retail Infotech Limited*

10. The brief facts of the case as emanating from the records are: The assessee company is a captive service provider to its parent, SmartStream Technologies Ltd., U.K (hereinafter referred to as "STL"). The assessee is engaged in the business of development and distribution of software used in banking and finance industry. During the period relevant to assessment year under appeal, the assessee entered into international transaction with its Associated Enterprise (AE) for providing software development services amounting to Rs.13,27,18,885/-. The assessee applied Transactional Net Margin Method (TNMM) as the most appropriate method to benchmark the international transactions. The assessee selected Operating Profit/Operating Cost (OP/OC) as Profit Level Indicator (PLI). The PLI of the assessee for assessment year 2009-10 was 10.25%. The assessee selected 24 companies as comparables in its Transfer Pricing Study Report to determine Arm's Length Price (ALP) of the transactions with AE. The Transfer Pricing Officer (TPO) applied turnover filter to select the comparable companies with lower range of turnover Rs.1.3 crores and upper cap of Rs.130 crores. The TPO introduced 13 fresh comparables and excluded 10 companies selected by the assessee in the list of comparables. The TPO accepted only 7 comparables selected by assessee in the final set of comparables. The TPO's final set of comparables had 23 companies with PLI of 20.69%. In light of fresh set of comparables, the TPO made adjustment of Rs. 1,25,73,179/-. Aggrieved against the order of TPO, the assessee filed objections before the Dispute Resolution Panel (DRP). The DRP, after considering the submissions of the assessee, rejected 10 companies from the TPO's final set of comparables by applying turnover filter

as adopted by the TPO. The DRP also rejected two more comparables by applying RPT filter and introduced one comparable from the list of comparables selected by the assessee. Thus, the final set of comparables as selected by the DRP is as under :-

<i>Sr. No.</i>	<i>Company name</i>	<i>OP/OC % as per DRP's directions dated 29.11.2013</i>
1	<i>Acropetal Technologies Ltd.</i>	<i>21.81%</i>
2	<i>KALS Information Systems Ltd.</i>	<i>41.91%</i>
3	<i>Akshay Software Technologies Ltd.</i>	<i>8.19%</i>
4	<i>FCS Software Solutions Ltd.</i>	<i>16.11%</i>
5	<i>ICRA Techno Analytics Ltd.</i>	<i>11.13%</i>
6	<i>Cepha Imaging Pvt. Ltd.</i>	<i>20.25%</i>
7	<i>Cyber Media India online Ltd. (merged)</i>	<i>9.41%</i>
8	<i>Polaris Retail Infotech Ltd.</i>	<i>28.42%</i>
9	<i>Servion Global Solutions Ltd.</i>	<i>6.66%</i>
10	<i>E-Zest Solutions Ltd.</i>	<i>22.97%</i>
11	<i>Quintegra Solutions Ltd.</i>	<i>16.70%</i>
12	<i>R S Software India Ltd.</i>	<i>9.79%</i>
	<i>Arithmetic mean of the comparables</i>	<i>17.78%</i>

11. The DRP vide directions dated 29.11.2013 made adjustment of Rs.90,69,990/- to international transactions. On the basis of the directions of the DRP, the Assessing Officer made final assessment order, against which the assessee is in appeal before us.

12. The learned AR submitted that assessee in the present appeal has confined his submissions only to inclusion and exclusion of some of the comparables selected by the TPO/DRP. The learned AR pointed that assessee wants inclusion of :

(i) PSI Data Systems Ltd.;

- (ii) SIP Technologies & Exports Ltd.; and,
- (iii) TVS Infotech Ltd.

The TPO and the DRP have excluded the aforesaid three companies from the list of comparables only on the ground that these are loss making companies. The learned AR submitted that admittedly the aforesaid three companies have incurred loss in assessment year 2009-10, but all these companies are not 'persistent loss' making companies. The Tribunal in various decisions have held that comparables should be rejected only if they are persistent loss making, i.e. the comparable is having loss in three consecutive financial years including the relevant assessment year and immediately two preceding years. In support of his contention, the learned AR placed reliance on the decision of *John Deere India Pvt. Ltd. vs ACIT in ITA No. 2236/PUN/2012, assessment year 2008-09 decided on 18.11.2015*. To further buttress his argument, the learned AR referred to summary of the financials of comparables at page 279 of the Paper Book. The learned AR submitted that in financial years 2006-07 and 2007-08, PSI Data Systems Ltd. had positive income whereas, the other two companies, i.e. SIP Technologies & Export Ltd. and TVS Infotech Ltd. had positive income in financial year 2006-07. Thus, these companies do not fall within the meaning of 'persistent loss' making companies as has been enunciated by various decisions of the Tribunal.

13. The learned AR submitted that assessee wants exclusion of KALS Information Systems Ltd. (in short 'KALS') and E-Zest Solutions Ltd. (in short 'E-Zest') The learned AR submitted that KALS is predominantly a product company and cannot be functionally compared to a software development services company. The learned AR referred to Annual Report of KALS for financial year 2008-09 at page 98 to 103 of the Paper Book and submitted that

the company has reported inventory amounting to Rs.71,47,977/-. The turnover of the said company during the financial year 2008-09 is Rs.2,14,04,686/-. Thus, the total inventory held by KALS is 33.39% of the total turnover. The functional profile of KALS is also different from that of the assessee. Therefore, the said company cannot be compared for FAR analysis with the assessee. The learned AR pointed that the Tribunal in various cases has held that KALS being a product development company cannot be compared to a software development company. To support his contentions, the learned AR placed reliance on the following decisions :-

- i) PTC Software (India) Pvt. Ltd. vs DCIT, 52 taxmann.com 351 (Pune)
- ii) QAD India (P.) Ltd. vs DCIT, 75 taxmann.com 280 (Mumbai)
- iii) UCB India (P.) Ltd. vs Addl. CIT, 73 taxmann.com 389 (Mumbai)
- iv) NetHawk Networks India (P.) Ltd. vs ITO, 41 taxmann.com 250 (Mumbai)
- v) Trilogy E-Business Software India Pvt. Ltd. vs DCIT, 29 taxmann.com 310 (Bangalore)
- vi) Sumtotal Systems India (P.) Ltd. vs ACIT, 46 taxmann.com 231 (Hyderabad)
- vii) 3DPLM Software Solutions Ltd. vs DCIT, 42 taxmann.com 333 (Bangalore)
- viii) Telcordia Technologies India (P.) Ltd. vs DCIT, 72 taxmann.com 67 (Mumbai)
- ix) ITO vs Prana Studios (P.) Ltd., 69 SOT 12 (Mumbai)
- x) Lionbridge Technologies (P.) Ltd. vs ITO, 64 taxmann.com 461 (Mumbai)
- xi) Tesco Hindustan Service Centre (P.) Ltd. vs DCIT, 77 taxmann.com 48 (Bangalore)
- xii) Sharp Software Development (P.) Ltd. vs DCIT, 76 taxmann.com 340 (Bangalore)
- xiii) John Deere India (P.) Ltd. vs DCIT, 77 taxmann.com 7 (Pune)

14. In respect of E-Zest, the learned AR submitted that the said company is engaged in Knowledge Processing Outsourcing (KPO) and ITeS services. It is a

product engineering and software development company having expertise in cloud, SAAS and business intelligence. The said company is also engaged in implementing ERP and related consultancy services. Since financial statement for the year ended 31.03.2009 was not available in public domain, the information of financial performance was obtained from the official website of the company. The learned AR further pointed that the TPO selected E-Zest as comparable without affording opportunity to assessee to file objections against selection of the said company. The learned AR referred to para 6.1.4 of the order of TPO to contend that the TPO had issued show cause only in respect of inclusion of KALS and Ocimum Bio Solutions India Ltd. There was no reference to E-Zest in the said show cause notice. Thus, proper opportunity was not afforded to the assessee to file objections against selection of E-Zest as comparable by the TPO. The learned AR submitted that Pune Bench of the Tribunal in the case of *John Deere (supra)* has held that E-Zest is not comparable to a software development company and hence, rejected the same from the final list of comparables.

15. In respect of additional ground no. 9, the learned AR submitted that the assessee is seeking exclusion of Acropetal Technologies Ltd., Cepha Imaging Pvt. Ltd. and Polaris Retail Infotech Ltd. from the list of comparables. The learned AR fairly admitted that these companies were selected as comparables by the assessee in Transfer Pricing study, however, later on assessee realised that these companies are functionally not comparable. The assessee has assailed inclusion of said companies as comparables by raising additional ground as the assessee had not taken objection to their inclusion before the DRP. The learned AR submitted that this ground may be restored to the TPO for re-examination in the light of decisions rendered by Hon'ble Bombay High

Court in the case of *CIT vs Tata Power Solar Systems Ltd.*, 77 taxmann.com 326 (Bom.) and *PCIT vs Pfizer Ltd.* in ITA No. 1731 of 2016 decided on 04.03.2019 by the Hon'ble Bombay High Court.

16. *Per contra*, the learned DR vehemently defended the impugned order on exclusion of PSI Data Systems Ltd., SIP Technologies & Exports Ltd. and TVS Infotech Ltd. The learned DR submitted that all the three companies are huge loss making companies. The inclusion of these companies would not give correct average mean of the comparables as the quantum of loss of these three companies is substantial. The learned DR submitted that not only consistent loss but the margin of loss should also be considered while selecting/rejecting a company as comparable.

17. In respect of additional ground no. 9, the learned DR vehemently opposed the admission of the same. The learned DR submitted that it is not a legal ground, but a factual ground which would involve examination of facts afresh.

18. We have heard the submissions made by rival sides. The only issue raised before us in appeal by the assessee is inclusion/exclusion of comparables in the final list of comparables to determine arm's length price of assessee's international transactions with its AE.

19. The assessee is seeking inclusion of PSI Data Systems Ltd., SIP Technologies & Exports Ltd. and TVS Infotech Ltd. in the list of comparables. The said companies have been excluded by the DRP on the ground that they are loss making companies. However, the learned AR has pointed from the financials of these companies that they were profit making companies in

financial year 2006-07. The Tribunal, in the case of *John Deere (supra)* has held that only persistent loss making companies are to be excluded from the list of comparables. The relevant extract of the findings of the Tribunal on this issue reads as under :-

“21.2 The contention of the assessee is that the said company is not a persistent loss making company. Only for the reason that the comparable has suffered loss in one year the same should not be rejected. We find merit in the submission of the Ld. A.R. In the case of Bobst India Pvt. Ltd. Vs. DCIT in ITA No. 1380/PN/2010 for A.Y. 2006-07 the Tribunal has observed that only persistent loss making companies should be held as not good comparable. The Tribunal held that the ‘persistent loss’ means, continuous loss for more than 3 years. Thus, where the comparable entity is not under persistent loss, the same should not be rejected as comparable. Similar view has been taken in the case of Goldman Sachs (India) Securities Pvt. Ltd. Vs. ACIT, ITA No. 7724/Mum/2011, and Brigade Global Vs. ITO, ITA No. 1494/Hyd/2010. In the present case, the comparable entity SIP Technologies & Exports Ltd. has suffered loss in F.Y. 2007-08 only. Therefore, it cannot be said to be a persistent loss making company. The authorities below have thus erred in excluding the same from the list of comparable entities. We direct the TPO/AO to include the aforesaid company as comparable entity.”

20. In the present case, we find that all the three companies in question were having positive income in assessment year 2006-07. The operating margin of the companies in three consecutive financial years including the financial year relevant to assessment year 2009-10 are as under :-

Sr. No.	Name of comparable companies	March 2007	March 2008	March 2009	Average
1	PSI Data Systems Ltd.	6.36%	5.84%	-3.06%	3.05%
2	SIP Technologies & Exports Ltd.	10.14%	-33.44%	NA	-11.65%
3	TVS Infotech Ltd.	8.91%	-10.45%	NA	-0.77%

21. At this juncture, we may point that while ascertaining whether the companies are persistent loss making or not, the quantum of loss suffered during the period under consideration is immaterial. The Tribunal in various decisions have only considered the period of loss and not the quantum of loss. Therefore, respectfully following the order of Tribunal in the case of *John Deere (supra)*, we reject the objections raised by the learned DR on this issue and direct the TPO/Assessing Officer to include PSI Data Systems Ltd., SIP Technologies & Exports Ltd. and TVS Infotech Ltd. in the final set of comparables as they are not persistent loss making companies.

22. The assessee has also assailed exclusion of KALS and E-Zest from the list of comparables. The learned AR asserted that since both these companies are functionally different, therefore, they should be excluded from the list of comparables.

KALS : The assessee is seeking exclusion of KALS as it is product development company. This fact is evident from the inventory at the end of the financial year 2008-09. As per Balance-sheet of the company as on 31.03.2009, the said company is having inventory of Rs.71,47,977/-. We further find that in the case of *PTC Software India Pvt. Ltd. vs DCIT (supra)*, the Pune Bench of Tribunal has considered the issue whether KALS is comparable to software development company. The Tribunal held that KALS is engaged in sale of software products and hence, the said company is not functionally comparable with entity engaged in designing and developing software. The decision of the Tribunal has been upheld by the Hon'ble Bombay High Court in the case of *PCIT vs PTC Software India Pvt. Ltd., [2019] 101 taxmann.com 117*. Similar view has been taken by the Pune Bench of Tribunal in the case of *John Deere (supra)*, though the assessment year under consideration was

assessment year 2008-09. No material has been placed on record by the Revenue to show that there was change in the activities carried out by the assessee or KALS, respectively in assessment year 2009-10. We find merit in the contentions of the assessee. Hence, we hold that KALS being functionally different should be excluded from the list of comparables.

E-Zest : The assessee is seeking exclusion of E-Zest on the ground that it is engaged in KPO and ITeS services, hence it is functionally different from the assessee. We find that the Pune Bench of Tribunal in the case of *Amber Point Technology India Pvt. Ltd. vs DCIT*, ITA No. 761/PUN/2014 for assessment year 2008-09 has held that E-Zest is a product company and hence, cannot be compared with the assessee engaged in software development services. The relevant extract of findings of the Tribunal are as under :-

“23. The third concern whose inclusion has been objected to by the assessee is e-Zest. The case of assessee is that the said concern is engaged in diversified activity and is a product company. The learned Authorised Representative for the assessee referred to the decision of Pune Bench of Tribunal in MSC Software Corporation India (P.) Ltd. Vs. ACIT (supra) relating to the year under appeal and pointed out that the said concern was excluded because of its being a product company. The relevant findings of the Tribunal are in para 18, which read as under :-

“18. On perusal of record and the order of Tribunal in John Deere India Pvt. Ltd. Vs. ACIT (supra), we find that the concern E-zest Solutions Ltd. is a product company and is engaged in both the provision of software services and sale of software services. On the other hand assessee is engaged in Software development services where the segmental details are not available, accordingly, E-zest Solutions Ltd. is functionally not comparable. Accordingly, we hold that the said concern is to be excluded from the final set of comparables.”

24. In view of similarity of reasoning, we hold that the said concern e-Zest being a product company is not to be included as comparable to the

assessee, which is engaged in providing IT services to its associated enterprises, hence the same is to be excluded from final list of comparables.”

23. Similar view has been expressed by Pune Bench of Tribunal in the case of *John Deere (supra)*. The Tribunal has held that E-Zest is engaged in ITeS and KPO services that cannot be compared with software development services. Thus, in view of our above observations, we direct the TPO/Assessing Officer to exclude E-Zest from the list of comparables. Accordingly, the assessee succeeds on ground nos. 2 and 3 of the appeal.

24. In respect of additional ground of appeal no. 9, the learned AR has prayed to restore the same to the TPO for afresh examination as assessee had not objected to inclusion of these companies, i.e. Acropetal Technologies Limited, Cepha Imaging Private Limited and Polaris Retail Infotech Limited before the DRP. The contention of the assessee is that these companies are functionally different and hence should be excluded from the list of comparables.

25. The exercise of conducting transfer pricing study is to ascertain arm's length price of international transactions of assessee with its AE. If in the process, the assessee has selected any wrong comparable, it is the duty of TPO to examine and reject the same before ascertaining arm's length price of the international transactions. An inclusion of certain entity in the list of comparables by the assessee in transfer pricing study report cannot act as estoppel against the assessee if, at a later stage, assessee seeks exclusion of the said comparable on account of functional disparity or it fails to qualify any of the filters applied. Our view is fortified by the decision of Tribunal in the case of *DCIT vs Quark Systems Pvt. Ltd., 38 SOT 307 (Chandigarh)(SB)*.

Therefore, we admit the additional ground of appeal raised by the assessee and restore it to the file of TPO/Assessing Officer for *de novo* examination of the comparables. Accordingly, additional ground no. 9 of the appeal is allowed for statistical purposes.

26. The learned AR has stated at Bar that he is not pressing ground nos. 1, 4 to 7 and additional ground no. 8. Thus, in view of the statement made by the learned AR at the Bar, the said grounds of appeal are dismissed as not pressed. In the result, the appeal of assessee is partly allowed in the terms aforesaid.

27. To sum up, the appeal of the Revenue and the cross objection of the assessee are dismissed. The appeal of the assessee is partly allowed.

Order pronounced in open Court on Friday, the 31st day of January, 2020.

Sd/-
(N.K. PRADHAN)
ACCOUNTANT MEMBER

Sd/-
(VIKAS AWASTHY)
JUDICIAL MEMBER

Mumbai, Date : 31st January, 2020

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Copy to :

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- 2) The Respondent
- 3) The CIT(A) concerned
- 4) The CIT concerned
- 5) The D.R, "J" Bench, Mumbai
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By Order

Dy./Asstt. Registrar
I.T.A.T, Mumbai