

**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.215/Bang/2017
Asst. Year : 2012-2013

M/s.Digital Juice Animations Private Limited, 18, Saleh Centre, Unit No.201, 2 nd Floor, Cunningham Road Bangalore – 560 052. PAN :AABCD9298H.	Vs.	The Asst.Commissioner of Income-tax, Circle 2(1)(2) Bangalore.
(Appellant)		(Respondent)

Appellant by :Sri.Suresh Muthukrishnan, CA
Respondent by :Sri.Vilas S.Shinde, CIT-DR

Date of Hearing :06.02.2020	Date of Pronouncement : 17.02.2020
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ORDER

Per B.R.Baskaran, AM :

This appeal filed by the assessee is directed against the assessment order passed by the Assessing Officer for assessment year 2012-2013 u/s 143(3) r.w.s. 144C(13) of the Act, in pursuance of directions given by the learned Dispute Resolution Panel (DRP).

2. Though the assessee has raised many grounds, at the time of hearing, the learned AR restricted his arguments to grounds No.5, 8.4 and 9. The learned AR also made a necessary endorsement in the grounds of appeal in support of his submission that he is pressing the above said three grounds only. The three grounds read as under:-

“5. Without prejudice to the above, the Learned TPO has erred in failing to apply the upper limit Turnover filter, absence of which has resulted in selection of improper comparables leading to the determination of a highly distorted and excessive Operating Margin under the TNMM.

8.4 Without prejudice to the above, the Ld.Panel has erred on facts and in law by retaining BNR Udyog Limited (seg) (Medical Transcription) and holding that the same is not comparable to the appellant and the same needs to be excluded from the list of comparables selected by the Ld.TPO.

9. The learned AO / TPO has erred in law and on facts by not correctly implementing the formula prescribed by the Organisation for Economic Co-operation and Development (“OECD”) and the United Nations Practice Manual for Developing Countries Model Convention to carry out working capital adjustment to the operating profit margins of the comparable companies by :

- By computing the working capital adjustment at - 6.24% based on the operating results of the eligible assessee as a whole and not considering the segmental results of the eligible assessee;*
- by discounting the Prime lending rate (“PLR”) for computing the working capital adjustment as the same is not in accordance with the guidelines provided by the Organisation for Economic Development Manual adopted by TPO for computing the working capital adjustment.”*

All the three grounds relate to Transfer Pricing Adjustment made by the TPO. The remaining grounds are dismissed as Not Pressed.

3. The assessee-company is engaged in the business of design and development of animation and graphical software and manufacture of packaging unit. It is wholly owned subsidiary of Digital Juice Inc USA. It is a contract service provider rendering ITES services and packaging services to its AE. The assessee adopted TNMM method as the most appropriate method for benchmarking its ITES services. It adopted Operating profit by operating cost (OP/OC) as profit level indicator (PLI). The assessee declared a margin of 22.57%. The TPO rejected the transfer pricing study conducted by the assessee and selected following 10 comparables:-

Sl. No.	Name of the case	Operating income	Operating cost	OP/OC
1.	Accentia Technologies Ltd.	126,38,02,000	112,89,16,000	11.75
2.	Universal Print Systems Ltd. (seg)/ (BPO)	6,17,67,000	3,87,49,000	52.46
3.	Informed Technologies India Ltd.	1,96,36,431	1,82,45,770	6.08
4.	Infosys BPO Ltd.	1316,75,11,974	962,91,06,964	36.30
5.	Jindal Intellicom Ltd.	30,27,51,875	30,29,02,990	-0.05
6.	Microgenetic Systems Ltd.	1,29,93,217	1,08,63,390	19.61
7.	TCS E-Service Ltd.	15,78,44,000	9,64,28,000	63.69
8.	BNR Udyog Ltd. (seg) / Medical Transcription)	1,47,04,000	97,87,000	41.58
9.	Excel Infoways Ltd. (seg) / (IT/BVPO)	790,96,95,000	559,06,04,000	29.79
10	e 4 e Healthcare Services P.Ltd.	89,50,04,209	74,59,23,078	19.85
	Average			28.11%

3.1 The average PLI of the above said companies worked out to 28.11%. The TPO noticed that the assessee is having negative working capital. Accordingly, he increased the average margin by 6.24%. Accordingly, adjusted margin was

worked out at 34.35% and transfer pricing adjustment of Rs.83.74 lakh was made by the TPO. The learned DRP gave partial relief to the assessee, which resulted in deduction of transfer pricing adjustment to Rs.66.24 lakh. Still aggrieved, the assessee has filed this appeal before us.

4. In ground No.5, the assessee is praying for application of turnover filter. The learned AR submitted that the turnover of the assessee from ITES segment is around 9 crores and hence it falls under the category of 1 to 200 crores category. Accordingly, the companies, which are having turnover exceeding 200 crores cannot be considered as comparable companies. In support of this proposition, he placed reliance on the decision rendered by the co-ordinate Bench in the case of *Micro Focus Software India (P) Ltd. v. ACIT [(2020) 113 taxmann.com 244 (Bangalore – Trib.)]*. The learned AR submitted that, if the turnover filter is applied, following companies will get excluded:-

- (i) Infosys BPO Limited
- (ii) TCS E-Service Limited
- (iii) Excel Infoways Ltd.

5. We have heard the learned Departmental Representative and perused the record. Admittedly, the assessee-company falls in the bracket of companies having turnover exceeding 1 crore but not exceeding 200 crores. It has been held in the case of *Autodesk India (P) Ltd. v. DCIT [(2018) 96 taxmann.com 263 (Bang. – Trib.)]* that the companies having turnover exceeding Rs.200 crores cannot be considered as comparable

companies in respect of those companies having turnover of less than Rs.200 crores. The above said decision was followed in the case of *Micro Focus Software India (P) Ltd. (supra)*. Accordingly, by following the decision rendered by the co-ordinate Bench in the case of *Autodesk India (P) Ltd. (supra)*, we direct the AO / TPO to exclude companies having turnover exceeding Rs.200 crore.

6. Ground No.8.4 relates to a comparable company, viz., BNR Udyog Limited. The learned AR submitted that the above said company was considered by the co-ordinate Bench in the case of FNF India (P.) Ltd. [IT(TP)A No.195/Bang/2016 and 459/Bang/2017 dated 03.07.2019 and the Tribunal has restored the issue to the file of the Assessing Officer.

7. We heard the learned DR on this issue and perused the record. We noticed that the co-ordinate Bench in the case of FNF India (P.) Ltd. (supra) has followed the decision rendered by another co-ordinate Bench in the case of *Mobily Indotech India (P.) Ltd. v. Dy.CIT [(2018) 97 taxmann.com 2 (Bang.-Trib)* wherein the company M/s.BNR Udyog Limited was examined. The relevant observation made in respect of the above said company by the co-ordinate Bench has been extracted as under:-

“BNR Udyog Ltd. (Segment – Medical Transcription)

The contentions of the assessee that the company BNR Udyog Ltd., is functionally different and fails the RPT filter at the entity level. It was found from the record that the benchmarking of selected company 'BNR' has been done only at the medical transcription segment and issue of RPT has not been urged before the Assessing Officer/DRP. Following the decision of the co-ordinate bench of ITAT Bangalore in

the case of Indegene (P.) Ltd. v. Asstt. CIT [2017] 85 taxmann.com 60 for asst. year 2012- 13, the issue of comparability of 'BNR' was remanded to the file for the TPO for fresh consideration on ground that in the year under consideration, there were 3 segments. How much of the RPT expenses pertain to each of the segments required examination and this aspect had not been analyzed by either the TPO or the assessee. While it is clear from the TPO's order that if the benchmarking is done only for the medical transcription segment, then the RPT pertaining to that segment only should be considered. However, since how much of the RPT pertain to the medical transcription segment has not been determined by either the TPO or the assessee, the Bench thought it appropriate and proper to remand the matter of comparability of this company BNR Udyog Ltd., to the file of the TPO for determination of the issue afresh in line with observation above. Following the above decision of the co-ordinate bench in the case of Indegene (P.) Ltd. (supra) and considering the factual matrix involved, that how much RPT pertains to the medical transcription has not been determined by either the TPO or the assessee, it was felt appropriate and proper to remand the issue of comparability of this company, BNR Udyog Ltd. to the file of the TPO for determination afresh. [Para 8.3.2]."

7.1 In the case of *Mobily Indotech India (P.) Ltd. (supra)* as well as *FNF India (P.) Ltd.*, the above said company has been restored to the file of the AO / TPO for examining it afresh. Following the above said decisions, we also restore *FNF India (P.) Ltd.*, to the file of AO / TPO with similar directions.

8. Ground No.9 relates to adjustment made by the learned TPO in respect of negative working capital. The learned AR submitted that the co-ordinate Bench in the case of *FNF India (P.) Ltd. (supra)* has held that there is no necessity to make working capital adjustments, since the company does not bear any working capital risk. The relevant discussions made by the co-ordinate Bench on this issue are extracted below:-

“14. In Gr.No.11 the Assessee has contended that the TPO and the DRP erred in adding to the average arithmetic profit margin of the comparable companies chosen by the TPO, negative working capital adjustment. On the above ground, it is undisputed that the Hyderabad Bench of the for Assessment Year 2009-2010 in the case of Adaptec (India) P. Ltd. Vs. The ACIT, Circle 1(1), order dated 25.3.2015 held that no such addition can be made for the following reasons:-

"Ground No.8 pertains to the issue of negative working capital. As briefly stated above, after arriving at the arithmetic mean of all comparables at 22.03%, the A.O. worked out negative working capital adjustment of 3.22% thereby, making arms length price at 25.25%. Even though, DRP refused to interfere with the objections of the assessee in its order, we were informed that DRP has directed the TPO/A.O. not to make any negative working capital adjustment in some of the cases in the next assessment year, in the cases of Market Tools Research P. Ltd., and Mega Systems Worldwide India P. Ltd., assessee placed on record copies of orders of DRP. In that DRP considered the issue and directed the TPO 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."

15. 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."

9. The learned AR submitted that the assessee herein is a captive service provider and it does not have any borrowing. Since it deals with its AEs and not outsiders, there is no working capital risk as presumed by the TPO.

10. We have heard the learned DR on this issue and perused the record. We noticed that the co-ordinate Bench in the case of FNF India (P.) Ltd. (supra) has followed the decision rendered by the Hyderabad Bench of the Tribunal in the case of *Autodesk India (P) Ltd. (supra)*, in order to hold that working capital adjustment in respect of negative working capital is not called for. Following the same, we direct the A.O. to delete the adjustment made towards negative working capital.

11. In the result, the appeal filed by the assessee is treated as partly allowed.

Order pronounced on this 17th day of February, 2020.

Sd/-
(Pavan Kumar Gadale)
JUDICIAL MEMBER

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

Bangalore; Dated : 17th February, 2020.
Devadas G*

Copy to :

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

Asst.Registrar/ITAT, Bangalore

		Date	Initial	
1.	Draft dictated on	06.02.2020		Sr.PS
2.	Draft placed before author	06.02.2020		Sr.PS
3.	Draft proposed & placed before the second member			JM/AM
4.	Draft discussed/approved by Second Member.			JM/AM
5.	Approved Draft comes to the Sr.PS/PS			Sr.PS/PS
6.	Kept for pronouncement on			Sr.PS
7.	Date of uploading the order on website			
8.	If not uploaded, furnish the reason			
8.	File sent to the Bench Clerk			Sr.PS
9.	Date on which file goes to the AR			
10.	Date on which file goes to the Head Clerk.			
11.	Date of dispatch of Order.			
12.	Draft dictation sheets are attached			Sr.PS

