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

BEFORE SHRI VIKAS AWASTHY (JUDICIAL MEMBER) AND
SHRI N.K. PRADHAN (ACCOUNTANT MEMBER)

IT(TP)A No. 3262/MUM/2017
Assessment Year: 2007-08

Tata Consultancy Services Ltd. 9th Floor, Nirmal Building, Nariman Point, Mumbai – 400021.	Vs.	Addl.CIT LTU – 1, World Trade Centre, 29th Floor, Cuffe Parade, Mumbai – 400005.
PAN No. AAACR 4849 R **Appellant**		**Respondent**

IT(TP)A No. 3389/MUM/2017
Assessment Year: 2007-08

ACIT LTU – 1, World Trade Centre, Centre-1, 29th Floor, Cuffe Parade, Mumbai – 400005.	Vs.	Tata Consultancy Services Ltd. 9th Floor, Nirmal Building, Nariman Point, Mumbai – 400020
Appellant		**PAN No. AAACR 4849 R** **Respondent**

Assessee by	:	Mr. Manish Kumar Kanth, AR
Revenue by	:	Mr. Uodal Raj Singh, DR
Last Date of Hearing	:	18/08/2020
Date of Pronouncement	:	11/11/2020

ORDER

PER N.K. PRADHAN, A.M.

The captioned cross appeals-one filed by the assessee and the other by the Revenue - are directed against the order of the Commissioner of Income Tax (Appeals)-58, Mumbai [in short 'CIT(A)'] and arise out of assessment under section 143(3) of the Income Tax Act 1961, (the 'Act'). Since common

issues are involved, we are proceedings to dispose off these appeals through a consolidated order.

(ITA No. 3262/MUM/2017)

2. The 1st ground of appeal

1.1 On facts and circumstances of the case and in law, the Ld. CIT(A) erred in disallowing deduction of Rs. 13,22,52,218/- being "State Taxes" paid overseas on the ground that the payment of "State Taxes" cannot be allowed under the provisions of section 40(a)(ii) of the Act.

1.2 Without prejudice to the above, the Ld. CIT(A) failed to consider "State Taxes" paid in the USA and Canada, as eligible for the double taxation relief under the provisions of section 90 or 91 of the Act if it is held that the payment of State Taxes is not allowable as deduction.

3. The assessee-company, engaged in the business of computer software and management consultancy, filed its return of income for the assessment year (AY) 2007-08 on 29.10.2007 declaring total income of Rs. 305,52,02,180/-. The return was revised on 10.02.2009 declaring total income of Rs. 313,12,64,074/-. Now we turn to the above ground of appeal.

Briefly stated, the facts are that the assessee had claimed deduction of state taxes paid overseas of Rs.13,22,52,218/- in the return of income. The break-up of it is as under:

Country	Amount (in Rs.)
USA	12,27,39,648/-
Canada	95,12,570/-
Total	13,22,52,218/-

The Assessing Officer (AO) by relying on the decision in the case of *S. Inder Singh Gill*, 471 ITR 284 (Bom) and *Kirloskar Electric Co. Ltd*., 228 ITR 676 (Karn.) held that the payments were not liable to be allowed as deduction either u/s 37(1) or section 40(a)(ii) of the Act.

In appeal, the Ld. CIT(A) dismissed the above ground by following the order of the ITAT in assessee's own case for AY 2005-06 (ITA No. 7513/M/2010) dated 04.11.2015, wherein it is held that :

> "6. Since admittedly, the Tribunal has decided this issue against the assessee in the case of Tata Sons Ltd. (supra), and the said decision has not been stated to have been stayed on appeal, respectfully following the same, this issue is decided against the assessee. Ground No. 1 stands dismissed."

4. Before us, the Ld. counsel for the assessee submits that the claim for deduction of overseas tax was made by the assessee, based on the following ground:

- Relying on the decision of the Tribunal in the case of Tata Sons (ITA No. 89 of 1989)
- Provisions of section 40(a)(ii) r.w.s. 2(43) disallow deduction for payment of taxes paid overseas which are eligible for relief of taxes u/s 90 and 91 of the Act. Taxes paid overseas to the local states of USA and Canada are not eligible for relief u/s 90/91 of the Act.
- The CIT(A) vide his order for AY 2005-06 has upheld the assessee's contention that provisions of section 40(a)(ii) do not apply to the state tax paid in USA and Canada.

4.1 It is further stated that as per section 40(a)(ii) r.w.s 2(43) of the Act, deduction for only those taxes paid overseas is allowable which are not eligible for any relief as per the provisions of section 90 or 91 of the Act. Accordingly, the provisions of section 40(a)(ii) are not applicable to the

"state taxes". Without prejudice to the above, if the state taxes are disallowed u/s 40(a)(ii), the same should be considered eligible for double tax relief under the provisions of the Act. In this regard, reliance is placed by him on the order of the Tribunal in assessee's own case for AY 2009-10 (ITA No. 5713/M/2016).

Further, the Ld. counsel relies mainly on the decision of the Bombay High Court in *Reliance Infrastructure Ltd. v. CIT* (390 ITR 271) and the order of the Tribunal in assessee's own case for AY 2009-10 (ITA 5713/M/2016)

5. On the other hand, the Ld. Departmental Representative (DR) supports the order passed by the Ld. CIT(A) on the reason that he has followed the order of the Tribunal in assessee's own case for AY 2005-06 and has decided the issue against the assessee.

6. We have heard the rival submissions and perused the relevant materials on record. The reasons for our decisions are given below.

In *Reliance Infrastructure Ltd*. (supra), the assessee executed projects in Saudi Arabia. The income earned in Saudi Arabia had been subjected to tax in Saudi Arabia. Therefore, while determining the tax payable under the Indian law, the applicant assessee sought benefit of section 91, which gives relief from double taxation on the same income. During the assessment proceedings in India, the assessee claimed the benefit of double taxation relief also on the sums of Rs. 47.30 lakhs being the amount deducted under section 80HHB and Rs. 5.59 lakhs being the amount on which weighted deduction was claimed under section 35B. The Assessing Officer negatived the applicant's claim for relief under section 91 on the ground that it would only apply / be available when the amount of tax paid under foreign

income is again included in the taxable income earned in India *i.e.* the same income must be taxed in both the countries. On appeal, the Commissioner (Appeals), dismissed the assessee's appeal upholding the view of the Assessing Officer that the benefit of section 91 could only be given if the very income had suffered tax in both the countries *i.e.* where the project is executed and also in India and in the instant case, the amount claimed by way of deduction under section 80HHB and section 35B was not suffering any tax in India for the purposes of section 91. On further appeal, the Tribunal dismissed the appeal of the assessee holding that the sum of Rs.47.31 lakhs being the amount deducted under section 80HHB and Rs. 5.59 lakhs being the weighted deduction allowed under section 35B were to be excluded in arriving at the figure of doubly taxed income for the purpose of computing the double income tax relief under section 91. On appeal to the High Court, the applicant assessee claimed that it should be allowed a deduction of the tax paid in Saudi Arabia, if it is held that the benefit of Section 91 of the Act is not available. This deduction is claimed only to the extent tax has been paid in Saudi Arabia on the income which has accrued/arisen in India. This claim was made on the basis of 'real income theory'. The Hon'ble Bombay High Court held as under:

> "(*h*) Before dealing with the rival contentions, it would be useful to reproduce the statutory provision arising for our consideration to decide this issue.
>
> "Definitions
>
> 2. In this Act, unless the context otherwise requires, -
>
> (1) to (42)** ** **
>
> 43. "tax" in relation to the assessment year commencing on the 1st day of April, 1965, and any subsequent assessment year means income tax chargeable under the provisions of this Act, and in relation to any other assessment year income-tax and super-tax chargeable under the provisions of this Act prior to the aforesaid date [and in relation to the assessment year commencing on the 1st day of April, 2006, and any subsequent assessment year includes the fringe benefit tax payable

under Section 115WA]

"Amounts not deductible

40. Notwithstanding anything to the contrary in Section 30 to the following amounts shall not be deducted in computing the income chargeable under the head "Profits and gains of business or profession".

(*a*) In the case of any assessee –

(i), (ia), (ib), (ic)** ** **

(*ii*) Any sum paid on account of any rate or tax levied on the profits or gains of any business or profession or assessed at a proportion of, or otherwise on the basis of, any such profits and gains.

[Explanation 1. - For the removal of doubts, it is hereby declared that for the purposes of this sub-clause, any sum paid on account of any rate or tax levied includes and shall be deemed always to have included any sum eligible for relief of tax under Section 90 or, as the case may be, deduction from the Indian income-tax payable under section 91.]

[Explanation 2. - For the removal of doubts, it is hereby declared that for the purposes of this sub-clause, any sum paid on account of any rate or tax levied includes any sum eligible for relief of tax under Section 90A.]"

(*i*) We have considered the rival submissions. So far as the question relating to the Tribunal not following its order in the case of the applicant itself for A.Y. 1979-80, we find that there is a justification for the same. This is so as the decision of this Court in *S. Inder Singh Gill* (*supra*) was noted by the Tribunal on an identical issue while passing the order for the subject assessment year. Thus, the Tribunal had not erred in not following its order for A.Y. 1979-80. In fact, the decisions of this Court in *South East Asia Shipping Co.* (*supra*) and *Tata Sons Ltd.* (*supra*), which are being relied upon in preference to *Inder Singh Gill* (*supra*) cannot be accepted as both the orders being relied upon by the applicant was rendered not at the final hearing but on applications under Section 256(2) of the Act and at the stage of admission under Section 260A of the Act. This unlike the judgment rendered in a Reference by this Court in *S. Inder Singh Gill* (*supra*). Moreover, the decision in *South East Asia Shipping Co.* (*supra*) is not available in its entirety. Therefore, it would not be safe to rely upon it as all facts and on what consideration of law, it was rendered is not known. Similarly, the decision of this Court in *Tata Sons* (*supra*) being Income Tax Appeal No.209 of 2001 produced before us, dismissed the appeal of the Revenue by order dated 2nd April, 2004 by merely following its order dated 23rd March, 1993 rejecting the Revenue's application for Reference under Section 256(2) of the Act. Thus, it also cannot be relied upon to decide the controversy. Moreover, the order of this Court in *Tata Sons Ltd.* (*supra*) as produced before us for Assessment Year 1985-86 had not noticed the decision of this Court in *S. Inder Singh Gill* (*supra*) on a Reference. Therefore, it is rendered *per incuriam*.

(*j*) This Court in *S. Inder Singh Gill* (*supra*) was required to answer the question whether for the purpose of computing total world income of the assessee as defined in Section 2(15) of the I. T. Act, the income accruing in Uganda has to be reduced by the tax paid to the Uganda Government in respect of such income? The Court while answering the question in the negative observed that it is not aware of any commercial principle/practice which lays down that the tax paid by one on one's income is allowed as a deduction in determining the income for the purposes of taxation.

(*k*) It is axiomatic that income tax is a charge on the profits/ income. The payment of income tax is not a payment made/incurred to earn profits and gains of business. Therefore, it cannot be allowed an as expenditure to determine the profits of the business. Taxes such as Excise Duty, Customs Duty, Octroi etc., are incurred for the purpose of doing business and earning profits and/or gains from business or profession. Therefore, such expenditure is allowable as a deduction to determine the profits of the business. It is only after deducting all expenses incurred for the purpose of business from the total receipts that profits and/or gains of business/ profession are determined. It is this determined profits or gains of business/profession which are subject to tax as income tax under the Act. The main part of Section 40(a)(ii) of the Act does not allow deduction in computing the income i.e. profits and gains of business chargeable to tax to the extent, the tax is levied/ paid on the profits/ gains of business. Therefore, it was on the aforesaid general principle, universally accepted, that this Court answered the question posed to it in *S. Inder Singh Gill* (*supra*) in favour of the Revenue.

(*l*) We would have answered the question posed for our consideration by following the decision of this Court in *S. Inder Singh Gill* (*supra*). However, we notice that the decision of this Court in *S. Inder Singh Gill* (*supra*) was rendered under the Indian Income Tax Act, 1922 and not under the Act. We further note that just as Section 40(a)(ii) of the Act does not allow deduction on tax paid on profit and/or gain of business. The Indian Income Tax Act, 1922 Act also contains a similar provision in Section 10(4) thereof. However, the Indian Income Tax Act, 1922 contains no definition of "tax" as provided in Section 2(43) of the Act. Consequently, the tax paid on income/profits and gains of business/profession anywhere in the world would not be allowed as deduction for determining the profits/gains of the business under Section 10(4) of the Indian Income Tax Act, 1922. Therefore, on the state of the statutory provisions as found in the Indian Income Tax Act, 1922 the decision of this Court in *S. Inder Singh Gill* (*supra*) would be unexceptionable.

However, the ratio of the aforesaid decision in *S. Inder Singh Gill* (*supra*) cannot be applied to the present facts in view of the fact that the Act defines "tax" as income tax chargeable under the provisions of this Act. Thus, by definition, the tax which is payable under the Act alone on the profits and gains of business are not allowed to be deducted notwithstanding Sections 30 to 38 of the Act.

(*m*) It therefore, follows that the tax which has been paid abroad would not be covered with in the meaning of Section 40(a) (ii) of the Act in view of the definition of the word 'tax' in Section 2(43) of the Act. To be covered by Section

40(a)(ii) of the Act, it has to be payable under the Act. We are conscious of the fact that Section 2 of the Act, while defining the various terms used in the Act, qualifies it by preceding the definition with the word "In this Act, unless the context otherwise requires" the meaning of the word 'tax' as found in Section 2(43) of the Act would apply wherever it occurs in the Act. It is not even urged by the Revenue that the context of Section 40(a)(ii) of the Act would require it to mean tax paid anywhere in the world and not only tax payable/ paid under the Act.

(*n*) However, to the extent tax is paid abroad, the Explanation to Section 40(a)(ii) of the Act provides/clarifies that whenever an Assessee is otherwise entitled to the benefit of double income tax relief under Sections 90 or 91 of the Act, then the tax paid abroad would be governed by Section 40(a)(ii) of the Act. The occasion to insert the Explanation to Section 40(a)(ii) of the Act arose as Assessee was claiming to be entitled to obtain necessary credit to the extent of the tax paid abroad under Sections 90 or 91 of the Act and also claim the benefit of tax paid abroad as expenditure on account of not being covered by Section 40(a)(ii) of the Act. This is evident from the Explanatory notes to the Finance Act, 2006 as recorded in Circular No.14 of 2006 dated 28th December, 2006 issued by the CBDT. The above circular inter alia, records the fact that some of the assessee who are eligible for credit against the tax payable in India on the global income to the extent the tax has been paid outside India under Sections 90 or 91 of the Act, were also claiming deduction of the tax paid abroad as it was not tax under the Act. In view of the above, Explanation inserted in 2006 to Section 40(a)(ii) of the Act, would require in the context thereof that the definition of the word "tax" under the Act to mean also the tax which is eligible to the benefit of Sections 90 and 91 of the Act. However, this departure from the meaning of the word "tax" as defined in the Act is only restricted to the above and gives no license to widen the meaning of the word "tax" as defined in the Act to include all taxes on income/profits paid abroad.

(*o*) Therefore, on the Explanation being inserted in Section 40(a)(ii) of the Act, the tax paid in Saudi Arabia on income which has accrued and/or arisen in India is not eligible to deduction under Section 91 of the Act. Therefore, not hit by Section 40(a)(ii) of the Act. Section 91 of the Act, itself excludes income which is deemed to accrue or arise in India. Thus, the benefit of the Explanation would now be available and on application of real income theory, the quantum of tax paid in Saudi Arabia, attributable to income arising or accruing in India would be reduced for the purposes of computing the income on which tax is payable in India.

(*p*) It is not disputed before us that some part of the income on which the tax has been paid abroad is on the income accrued or arisen in India. Therefore, to the extent, the tax is paid abroad on income which has accrued and/or arisen in India, the benefit of Section 91 of the Act is not available. In such a case, an Assessee such as the applicant assessee is entitled to a deduction under Section 40(a)(ii) of the Act. This is so as it is a tax which has been paid abroad for the purpose of arriving global income on which the tax payable in India. Therefore, to the extent the payment of tax in Saudi Arabia on income which has arisen/accrued in India has to be considered in the nature of expenditure incurred or arisen to earn

income and not hit by the provisions of Section 40(a)(ii) of the Act.

(*q*) The Explanation to Section 40(a)(ii) of the Act was inserted into the Act by Finance Act, 2006. However, the use of the words "for removal of dobuts" it is hereby declared "...." in the Explanation inserted in Section 40(a)(ii) of the Act, makes it clear that it is declaratory in nature and would have retrospective effect. This is not even disputed by the Revenue before us as the issue of the nature of such declaratory statutes stands considered by the decision of the Supreme Court in *CIT* v. *Vatika Township (P) Ltd.* [2014] 367 ITR 466/227 Taxman 121/49 taxmann.com 249 and *CIT* v. *Gold Coin Health Foods (P.) Ltd.* [2008] 304 ITR 308/172 Taxman 386 (SC).

(*r*) In the above facts and circumstances, question (iii)(a) is answered in the negative i.e. against the Revenue and in favour of the applicant assessee. Question (iii)(b) is answered in the negative i.e. against the Revenue and in favour of the applicant assessee."

6.1 Similar issue arose before the ITAT "J" Bench, Mumbai in assessee's own case for AY 2009-10 in ITA No.5713/Mum/2016. The Tribunal held as under:-

> "6. We have considered the rival submissions and perused the material on record. From the stage of the assessment proceeding itself, it is the claim of the assessee that the term "tax", as defined undersection 2(43) of the Act would only include taxes chargeable under the Indian Income Tax Act. It is the further case of the assessee that since in respect of the State taxes paid overseas, the assessee is not eligible to claim relief under section 90 or 91 of the Act, it will not be covered under section 40(a)(ii)of the Act. On a perusal of provisions of sub-section (43) of section 2 of the Act, it becomes clear that the term "tax" has been defined to mean any tax paid under the provisions of the Act. Section 40(a)(ii)of the Act says that any rate or taxes levied on the profits or gain in any business or profession would not be allowable as deduction. Explanation-1 to section 40(a)(ii) of the Act inserted by the Finance Act, 2006, w.e.f. 1st April 2006, further clarifies that any sum eligible for relief of tax either under section 90 or 91 of the Act would not be allowable as deduction under section 40(a)(ii) of the Act. It is the say of the assessee that the tax eligible for relief under section 90 of the Act are only those taxes which are levied by Federal / Central Government and not by any local authority of State, City or County. Thus, it is ineligible for any relief under section 90 of the Act. The aforesaid submissions of learned Sr.

Counsel for the assessee, prima facie, is acceptable if one has to strictly go by the meaning of "tax", defined under section 2(43) of the Act, as it only refers to tax paid under the provisions of the Act. It is also worth mentioning, the State taxes paid by the assessee in DTAA countries are not eligible for relief under section 90 of the Act. Therefore, the issue which arises is, whether it can be allowed as deduction under section 37 of the Act. No doubt, in assessee's own case in assessment year 2005-06, the Tribunal in the order referred to above following its own decision in DCIT v/s Tata Sons Ltd., [2011] 43 SOT 27 (Mum.), has held that the State taxes paid overseas cannot be allowed as deduction in view of the provisions of section 40(a)(ii) of the Act. However, the aforesaid legal position has substantially changed after the decision of the Hon'ble Jurisdictional High Court in Reliance Infrastructure Ltd. (supra). While interpreting the provisions of section 2(43) of the Act, vis-a- vis section 40(a)(ii) of the Act, the Hon'ble Court held that the tax which has been paid abroad would not be covered within the meaning of section 40(a)(ii) of the Act, since, the meaning of the word "tax" as defined under section 2(43) of the Act would mean only the tax chargeable under the Act. Thus, as per the aforesaid decision of the Hon'ble Jurisdictional High Court, taxes levied overseas which are not eligible for relief either under section 90 or 91 of the Act, would not come within the purview of section 40(a)(ii)of the Act. It is the specific plea of the assessee that the State tax is not covered either under Indo-US or Indo-Canada tax treaty, hence, not eligible for any relief under section 90 of the Act. Pertinently, unlike section 91 read with Explanation-(iv), section 90 does not provide for inclusion of tax levied by any State/ local authority of that country within the expression 'income tax'. In view of the aforesaid, we direct the Assessing Officer to verify whether the State taxes paid by the assessee overseas are eligible for any relief under section 90 of the Act and if it is not found to be so, assessee's claim of deduction should be allowed. In view of our decision above, no separate adjudication of grounds no.1.2 is required."

6.2 In *Reliance Infrastructure Ltd*. (supra), Hon'ble Bombay High Court has held that the assessee was entitled to deduction for foreign taxes paid on income accrued or arisen in India in computing its income, to the extent that such tax was not entitled to the benefit of section 91 of the Act.

Facts being identical, we follow the said judgement and also the above order of the Co-ordinate Bench and direct the AO to verify whether the State taxes paid by the assessee overseas are eligible for any relief u/s 90 of the Act and if it is not found to be so, assessee's claim of deduction should be allowed.

7. <u>The 2nd ground of appeal</u>

> 2.1 The Ld. CIT(A) erred in law and on facts in disallowing under section 40(a)(ia) of the Act, the business expenditure of an amount of Rs. 73,84,168/- being deduction towards interest, which is compensatory in nature, paid on account of delayed payment / shortfall of overseas taxes.

8. The Ld. CIT(A), observed that this ground of appeal is in consequence to the above 1st ground of appeal and held that "once the taxes itself have been held to be disallowable in the hands of the assessee, it is clear that any payment of interest thereon cannot be an allowable deduction."

9. Before us, the Ld. counsel submits that as per section 40(a)(ii) r.w.s. 2(43) of the Act, deduction for only those taxes paid overseas is allowable which are not eligible for any relief as per the provisions of section 90 or 91 of the Act. It is thus explained that accordingly, provisions of section 40(a)(ii) are not applicable to the "penal interest". Further, it is stated that the payment made by the Company on account of interest or penalty for delay in payment of federal or state taxes overseas which is compensatory in nature should be allowable as business expenditure u/s 37(1) of the Act. It is also explained that the last para to Article 2(1) of DTAA between India-USA clearly removes any amount payable in respect of any default or omission in relation to the above taxes or which represent a penalty imposed relating to those taxes.

10. On the other hand, the Ld. DR supports the order passed by the Ld. CIT(A) on the reason that "once the taxes itself have been held to be disallowable in the hands of the assessee, it is clear that any payment of interest thereon cannot be an allowable deduction.

11. We have heard the rival submissions and perused the relevant materials on record. A perusal of the records indicate that the assessee has not filed the details with supporting documents on the penal interest. It is not possible to decipher whether the penal interest is compensatory in nature or not. In view of the above, we set aside the order of the Ld. CIT(A) on the above ground and restore it to the file of the AO for deciding it afresh, keeping in mind our decision at para 6.2 hereinabove. We direct the assessee to file the documents/evidence as indicated above before the AO.

12. <u>The 3rd ground of appeal</u>

> 3.1 On facts and in circumstances of the case and in law, the Ld. CIT(A) erred in adjudicating the primary ground that tax is not required to be deducted, as per the provisions of section 195 read with the applicable Double Tax Avoidance Agreement ("DTAA"), from the payment to non-resident vendors for purchasing standard software products and consequently disallowing the said expenditure as per the provisions of section 40(a)(ia) of the Act.
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> 3.2 On facts and in circumstances of the case and in law, the Ld. CIT(A) erred in applying the provisions of section 40(a)(ia) read with section 195 of the Act to disallow the payment made by the appellant to various non-resident vendors towards import of software as a reseller by treating such payment as "royalty".
>
> 3.3 Without prejudice to the above, the Ld. CIT(A) in circumstances of the case failed to consider the expenses incurred towards purchase of software for trading purposes amounting to Rs. 17,48,99,176/- as revenue in nature.

13. The assessee had imported software products during the course of its business. The AO observed that these purchases were in the nature of software for internal use as well as for trading purposes. The break up is given below:

Software for internal use	Rs.15,43,05,676/-
Software for trading purposes	Rs.17,48,99,176/-
Total	**Rs.32,92,04,852/-**

The AO treated the software utilized for internal use as being in the nature of capital expenditure, drawing support from the order of the CIT(A) in assessee's own case in earlier years. Accordingly, the AO treated the said amount as disallowable u/s 40(a)(i) of the Act. With reference to imported software for third party sale, the AO concluded that these licenses were in the nature of royalty and since no TDS has been made by the assessee u/s 195, the consideration was liable to be disallowed u/s 40(a)(i) of the Act.

14. In appeal the Ld. CIT(A), following the order of the Tribunal in assessee's own case for AY 2005-06, held that the expenditure on software acquired for internal use is a capital expenditure and the assessee is entitled to depreciation on this amount.

In the context of payments made on software for resale, the Ld. CIT(A) observed that this is not a case of mere purchase and its subsequent sale of software as a reseller. The assessee's software package will not be complete without the software. The assessee is prohibited by the agreement to sell these software independently. These can only be supplied as a part of the package and hence, the claim of the assessee that it is operating as a third party reseller cannot be accepted. Further, it is noted by the Ld. CIT(A) that the reseller agreement between the two parties

clearly reveals that the assessee cannot distribute the purchased software independent of its own software package; the purchased software can only be distributed within the package developed by the assessee i.e. its own software program being sold to clients which incorporate the purchased program. Noting that this view is also supplemented by similar observation on this issue in OECD commentary on the subject, the Ld. CIT(A) dismissed the appeal on the above matter filed by the assessee on the reason that the payment made by the assessee for software imported treating itself as a re-seller are found to be in the nature of royalty and hence TDS was deductible on this amount by the assessee, being remitter of the sum.

15. Before us, the Ld. counsel for the assessee submits that the payment for purchase of software being similar to the payment for purchase of any 'product, goods' is not exigible to income tax in India. Further, it is stated by him that the payment for purchase of software is for acquiring of copy righted article and not for transfer of any right in the copyright and accordingly, it cannot be construed as 'royalty' under clause (v) of Explanation 2 to Section 9(1)(vi) of the Act and therefore, it is not taxable and hence, the provisions of section 195 of the Act do not apply and no disallowance can be made u/s 40(a)(i) of the Act. Further, it is explained by him that the amendment carried out by the Finance Act, 2012 will not have any retrospective effect based on the principle of "impossibility of performance", since the assessee cannot be expected to deduct tax at source in respect of transactions effected years back. Further, it is argued that even under the applicable DTAA, the payment for purchase of software cannot be regarded as royalty, since the definition of royalty under the DTAA is narrower than the definition in the Act.

Without prejudice to the above, it is stated that in respect of purchase of software for trading purpose, the assessee does not obtain any license from the seller and only earns margin on trading or reselling of such software and accordingly, it can be treated as royalty and no disallowance u/s 40(a)(i) can be made in respect of the same.

Without prejudice to the above, it is further submitted that provisions of section 40(a)(i) should not apply to allowance of depreciation on imported software, if treated as capital in nature.

On the above, the Ld. counsel relies *inter alia* on the order of the Tribunal in assessee's own case for AY 2005-06 (arising out of MA in ITA No. 7513 of 2010), AY 2009-10 (ITA No. 5713/M/2016) and the judgment of the Supreme Court in *Tata Consultancy Services v. State of Andhra Pradesh* (Civil Appeal No. 2582 of 1998 with CA No. 2584, 2585 & 2586 of 1998).

16. On the other hand, the Ld. DR submits that the software purchased by the assessee has been acquired for use in its products, which are then sold to clients with rights and licenses being given to the clients and such a case squarely falls within the ambit of Article 13(3) of the India-US DTAA. Further, it is stated by him that the assessee cannot be said to be trading in software and this is not a case of mere purchase and its subsequent sale of software as a reseller. Thus the Ld. DR supports the order passed by the Ld. CIT(A).

17. We have heard the rival submissions and perused the relevant materials on record. Similar issue arose before the Tribunal in assessee's own case for AY 2005-06 and AY 2009-10. For immediate reference, we

refer to the order of the Tribunal for AY 2009-10, wherein the following is held:-

> "15. We have considered rival submissions and perused the material on record. We have also applied our mind to the decisions relied upon. Undisputedly, in the year under consideration, the assessee has claimed deduction on account of expenditure incurred towards purchase of software products acquired for internal use. The expenditure relating to that has been treated as capital in nature and depreciation has been allowed by the Departmental Authorities. Insofar as software products acquired for re-sale / trading purpose, the assessee's claim of deduction in respect of expenditure incurred thereon as revenue in nature has been disallowed on the ground that the payment made being in the nature of royalty, the assessee was required to deduct tax at source under section 195 of the Act. Insofar as the expenditure incurred on the software products acquired in internal use, we, on a perusal of the facts on record are of the view that by incurring such expenditure, the assessee has acquired assets of enduring benefit. Therefore, the expenditure incurred is capital in nature and the assessee would be entitled for depreciation on the cost of such assets. The Tribunal while deciding identical issue in assessee's own case for the assessment year 2005-06 in ITA no.7513/Mum./2010, dated 4th November 2015, it has expressed similar view. Thus, following the aforesaid view of the Tribunal in assessee's own case, we uphold the decision of learned Commissioner (Appeals) on the issue. Insofar as the disallowance of expenditure incurred on acquiring software products for re-sale / trading purpose, it is noted that the Assessing Officer has not at all deliberated on the factual aspect of the issue. Simply relying upon certain judicial precedents and the statutory provisions, he has concluded that the payment made by the assessee for acquiring these software is in the nature of royalty as per section 9(1)(vi) of the Act, hence, assessee is liable to deduct tax at source under section 195(2) of the Act. Whereas, learned Commissioner (Appeals) has improved upon the reasoning of the Assessing Officer by observing that the software acquired by the assessee for trading purpose were not sold as it is by the assessee but have been utilized in programs developed by it for its clients. He has observed that the products developed by the assessee using software acquired were then sold to clients with rights and license. Thus, according to the learned Commissioner (Appeals), it is

not a case of mere purchase and subsequent sale of software as a re-seller / trader. He observed, assessee's software package will not be complete without the software acquired for trading purpose. In other words, the software acquired by the assessee is a necessary ingredient of the package being developed and supplied to the client and the assessee is prohibited by agreement to sell the software independently and they can only be supplied as a part of the package. As per section 9(1)(vi) of the Act, income in the nature of royalty shall be deemed to accrue or arise in India even in respect of a non-resident where the royalty is payable in respect of any right, property or information used or services utilized for the purpose of a business or profession carried on by a person in India or for the purpose of making or earning any income from any source in India. Pertinently, the expression "royalty" as per section 9(1)(vi) of the Act in its initial form did not specifically define computer software. By virtue of Explanation-3 to section 9(1)(vi) of the Act inserted by Finance Act w.e.f. 1st April 2010, computer software was defined to mean any computer program recorded on any disc, tape, perforated media or other information storage device and includes any such program or any customized electronic data. The scope of the term "royalty" was further explained by Explanation-4 to section 9(1)(vi) of the Act inserted by Finance Act, 2012, with retrospective effect from 1st June 1976, wherein, it was clarified that the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a computer software including granting of a license irrespective of the medium through which such right is transferred. It is the contention of the assessee that the software acquired by the assessee for the purpose of trading is a copyrighted article and the assessee has sold it to the customers as it is. It has been submitted that while re-selling / trading the software products, there is neither any transfer of right in copyright in favour of the assessee nor the assessee has transferred any right in the copyright. However, the learned Commissioner (Appeals) has recorded a categorical finding that the software products acquired by the assessee cannot be sold independently and can be sold by utilising in the package developed by it. In the aforesaid factual context, it requires examination whether the software products acquired by the assessee for trading purpose was sold as a chattel qua chattel or the assessee has made some value addition to it or has transferred the copyright relating to the software product along with the software product. No

doubt, in assessee's own case for assessment year 2005-06, the Tribunal in ITA no.7513/Mum./2010, dated 23 rd March 2017 (after recall of the original appeal order) while dealing with similar issue has held that the payment made by the assessee towards acquiring the software products is not royalty as the assessee has sold a copyrighted article and has not transferred any license or copyright. However, in the facts of the present case, in our considered opinion, further enquiry is required to be made by the Assessing Officer to factually verify the nature of transaction relating to acquisition of software product for trading purpose to find out whether it is sale of copyrighted article simpliciter or sale of copyright. In case, the payment made by the assessee is found to be royalty in view of Explanation-4 to section 9(1)(vi) of the Act, the contention of the assessee that it could not have withheld tax anticipating the change in law brought with retrospective effect, has to be considered keeping in view the decision of the Hon'ble Jurisdictional High Court in NGC Network India Pvt. Ltd. (supra). Further, assessee's contention that Explanatino-4 to section 9(1)(vi) of the Act cannot be brought into play while applying section 40(a)(i)of the Act as it only refers to Explanation-2 to section 9(1)(vi) of the Act for the definition of royalty also has to be examined keeping in view the ratio laid down in NGC Networks India Pvt. Ltd. (supra). In case, the payment made by the assessee does not fit into the definition of royalty as provided under the relevant tax treaty, the assessee certainly would get the benefit of the tax treaty and in that event the liability under section 195 of the Act cannot be fastened on the assessee. Since, all these issues have not been properly examined and deliberated upon by the Departmental Authorities, we are inclined to restore the issue to the Assessing Officer for fresh adjudication in terms with our observations hereinabove. The Assessing Officer must decide the issue after providing reasonable opportunity of being heard to the assessee."

17.1 We hold that the Ld. CIT(A), following the order of the Tribunal in assessee's own case for AY 2005-06, has rightly held that the expenditure on software acquired for internal use is a capital expenditure and the assessee is entitled to depreciation on this amount.

In the context of payments made on software for resale, having examined the relevant documents and rival submissions, we arrive at a finding that the facts in the impugned year on the above matter are identical to the AY 2009-10 in assessee's own case. Facts being identical, we follow the above order of the Co-ordinate Bench and restore the matter to the file of the AO for fresh adjudication in terms of the observations made therein. The AO would decide the issue after providing reasonable opportunity of being heard to the assessee.

18. <u>The 4th ground of appeal</u>

> 4.1 on facts and in circumstances of the case and in law, the Ld. CIT(A) erred in not allowing foreign tax relief as per the provisions of section 90(1)(a)(ii) of the Act read with provisions of the applicable Double Tax Avoidance Agreements, for income taxes paid in overseas jurisdiction in relation to income eligible for deduction under section 10A/10AA of the Act in India.

19. The Ld. counsel for the assessee submits that (i) foreign tax credit should also be provided for taxes paid in overseas jurisdiction, in respect of section 10A/10AA eligible income in India, as per the provisions of respective DTAA, (ii) even under MAT computation, the assessee should be allowed full credit of taxes paid overseas in respect of 10A/10AA income, (iii) since the correct legal position is that where a specific provision is made in DTAA, such provision will prevail over the general provision contained in the Income Tax Act, 1961.

It is thus stated by him that in view of the amendment by Finance Act, 2000, effective 01.04.2001, 10A/10AA is a deduction in respect of undertakings established in Software Technology Park (STP)/Special Economic Zone (SEZ).

It is stated that herein the countries involved are USA, Denmark, Hungary, Norway, Oman, South Africa, Saudi Arabia and Taiwan.

In support of his contentions, the Ld. counsel relies on the decision in *Wipro Ltd.* (2016) 382 ITR 179 (Karn.) and also the order of the Tribunal in assessee's own case for AY 2009-10.

20. On the other hand, the Ld. DR relies on the order of the CIT(A) and explains that the Hon'ble Karnataka High Court in *Wipro Ltd* (supra) has devided the Indian DTAAs with various countries into two categories- DTAAs with countries like Canada, U.K & DTAA with countries like U.S. In respect of DTAAs with countries like Canada & U.K, the Court has ruled that tax credit will be available only if the income is actually taxed in both the states. Further, it is argued that as per the above decision, the claim of DTAA benefit with respective taxes paid in other tax jurisdiction is not unfettered even in India-U.S DTAA, but is governed by the limitation clause incorporated in Article 25 which limits the scope of such benefit to the amount of tax attributable to the income, which has been taxed in other tax jurisdiction and hence, in all such cases, the tax deducted/paid on income in the foreign territory, which is tax exempt in India, being covered by section 10A/10B, the appellant shall not be entitled to treaty relief. Also, it is argued by the Ld. DR that similarly, in case of taxes paid in countries with which India does not have any agreement (cases covered by section 91), tax credit will be available only if the income is actually taxed in both the states and hence, in all such cases, the tax deducted/paid on income in the foreign territory, which is tax exempt in India, being covered by section 10A/10B, the assessee will not be entitled to treaty relief. It is further stated by him that in respect of tax deducted on income offered to tax in

U.S, where the assessee is eligible to benefits of DTAA between India & U.S, it will be eligible for treaty benefit on taxes paid/deducted on income offered in US, even if such income is tax exempt in India; however, it will be subject to the restrictions mentioned in section 90 of the Act. Referring to Article 25(2)(a) of the India-US DTAA, the Ld. DR explains that any deductions for taxes paid in US claimed by the assessee will be restricted to the income tax computed on income, which has been taxed in US and clearly such competition would be made in line with the Indian Income tax Act and after giving the assessee deduction u/s 10A/10B and charging interest at Indian rates. Thus, the Ld. DR supports the order passed by the Ld. CIT(A).

21. We have heard the rival submissions and perused the relevant material available on record. Similar issue arose before the Tribunal in assessee's own case for AY 2009-10, wherein it is held:-

> "31. We have considered rival submissions and perused the material on record. We have also applied our mind to the decisions relied upon. As could be seen, while the Assessing Officer has disallowed assessee's claim of foreign tax credit in respect of income exempt under section 10A/10AA of the Act on the reasoning that only such income which is subjected to tax in both the countries would qualify for tax credit, learned Commissioner (Appeals) has restricted the relief of foreign tax credit only in respect of tax paid in USA even in respect of income which is exempt under section 10A/10AA of the Act. The learned Commissioner (Appeals) has come to such conclusion by following the decision of the Hon'ble Karnataka High Court in Wipro Ltd. (supra). The reasoning of the learned Commissioner (Appeals) on the issue is, as per the decision of Hon'ble Karnataka High Court in Wipro Ltd. (supra), the foreign tax credit benefit under section 90(1)(a)(ii) of the Act would only be applicable under Indo-US DTAA and would not be applicable to other DTAA countries and non-DTAA countries. On a careful reading of the decision of the Hon'ble Karnataka High Court in Wipro Ltd. (supra), it is noted, while dealing with identical issue the Hon'ble Court held that

in the cases covered under section 90(1)(a)(ii) of the Act, it is not the case of income being subjected to tax or the assessee has paid tax on the income. The provision applies to a case where the income of the assessee is eligible to tax under the Act as well as in the corresponding law in force in the other country. The Court observed, though, income tax is chargeable under the Act, it is open to the Parliament to grant exemption under the Act from payment of tax for any specified period, normally, to incentivize the assessee the to carry on manufacturing activities or providing services. The Court thereafter referring to the treaty provisions with USA held that it is not the requirement of law that the assessee before he claims credit under the Indo-US convention or under the provision of the Act must pay tax in India on such income. The Court observed, as per the embargo placed in the DTAA, the assessee is entitled to such tax credit only in respect of that income which is taxed in USA. In similar context, the Court also referred to the tax treaty with Canada where the provisions does not allow credit for tax paid in Canada if the income is not subjected to tax in India. With regard to country's with which India does not have any agreement for avoidance of double taxation, the Court observed that as per section 91 of the Act, the assessee would be eligible to avail tax credit. Thus, on a careful reading of the aforesaid judgment of the Hon'ble Karnataka High Court, it becomes clear that where the respective tax treaty provides for benefit for foreign tax paid even in respect of income on which the assessee has not paid tax in India, still, it would be eligible for tax credit under section 90 of the Act. Like Article 25 of the Indo-USA treaty, treaties with various other countries such as Indo-Denmark, Indo-Hungary, Indo-Norway, Indo-Oman, Indo-US, Indo-Saudi Arabia, Indo-Taiwan also have similar provision providing for benefit of foreign tax credit even in respect of income not subjected to tax in India. However, Indo-Canada and Indo-Finland treaties do not provide for such benefit unless the income is subjected to tax in both the countries. Therefore, the foreign tax credit would be available to the assessee in all cases except the foreign tax paid in Finland and Canada. The Assessing Officer is directed to grant credit accordingly."

21.1 Facts being identical, we follow the above order of the Co-ordinate bench and hold that foreign tax credit would be available to the assessee in view of treaties India is having with USA, Denmark, Hungary, Norway,

Oman, Saudi Arabia and Taiwan. The assessee is directed to file before the AO the relevant provisions of India- South Africa Treaty.

22. The 5th ground of appeal

5.1 The assessment of income made by the AO in relation to the transfer pricing adjustments / additions / variations based on the transfer pricing order is bad in law and illegal as the transfer pricing order is passed by the Additional Commissioner of Income Tax without the authority of law as prescribed by the provisions of section 92CA of the Act.

5.2 Without prejudice to the above, the Ld. CIT(A) erred in law, on facts and in circumstances of the case in not deleting the transfer pricing adjustments / additions / variations made by the AO as being bad in law, illegal and unsustainable on the basis of the following grounds taken singly or cumulatively.

5.2.1 The transfer pricing adjustments are contrary to the principles laid down by the Hon'ble Mumbai Tribunal in the appellant's own case for the A.Y. 2005-06 (DCIT vs Tata Consultancy Services Limited) and therefore are required to be quashed and deleted.

5.2.2 a) The AO has failed to comply with the mandatory conditions stipulated in section 92C(3) of the Act and has failed to record his satisfaction before making the reference to the Transfer Pricing Officer (TPO).

b) The TPO has failed to prove that any of the conditions laid down in section 92C(3) of the Act had been satisfied which made out a case for tax evasion.

5.2.3 The AO/TPO has failed to arrive at a finding that the intention of the assessee was to evade tax and shift profits outside of India which is a condition precedent for making the Transfer Pricing Adjustment.

5.2.4 On facts and circumstances of the case and in law, the Ld. CIT(A) erred in not holding the proceedings initiated by the Ld. TPO as void authorities below initio since the Ld. AO erred in making the reference to the Ld. TPO without proper application of mind to the facts on record, without recording reasons for any necessity or expediency and without a legal and valid approval of the Ld. CIT

and therefore not being in accordance with the provisions of Section 92CA(1) of the Act.

23. During the financial year (FY) 2006-07 relevant to the AY 2007-08, the assessee entered into certain international transactions with its Associated Enterprises (AE). The Transfer Pricing Officer (TPO) disregarded all the contentions made by the assessee with regard to Arm's Length Price (ALP) of international transactions pertaining to provision of software, technical and consultancy services to AEs, advancing of interest bearing and interest free loans to AEs and provision of guarantee and undertaking to AEs. The TPO proposed total transfer pricing adjustment of Rs.556.43 crores to the income of the assessee as under:-

Sr.No	International transactions under dispute	Amount of Adjustment (Rs.in Crores)
1	Provision of software, technical & consultancy services to AEs	466.79
2	Provision of interest bearing and interest free loans to AEs	29.74
3	Provision of guarantee in respect of AEs	55.58
4	Providing undertaking in respect of AEs	4.32
	Total adjustment	556.43

The AO completed the assessment u/s 143(3) r.w.s.144C, incorporated the proposed addition of Rs.556.43 crores to the income returned by the assessee.

24. Aggrieved by the order of the AO, the assessee filed an appeal before the Ld.CIT(A). At para 13.16.6, the Ld.CIT(A) has mentioned that the assessee submitted before him a summary chart of ALP gross margin (as

computed by it) *vis-a-vis* gross margins earned by the AEs, which is reproduced is below:-

Sr.No	Name of the Entity	Entity revenue for offshore segment (A)	Paid to TCS (3CEB) (B)	Gross Profit-Offshore segment (C=A+B)	Gross Margin (C/A)	Comparable profit-Offshore margin (as per region	Whether at ALP?
1	Tata America International Corp.	8,155.15	7,345.81	809.34	9.92%	9.62%	Yes (after +/-5% working)
2	Tata consultancy Services Sverige AB	76.92	71.15	5.77	7.50%	29.31%	Yes
3	Tata Consultancy Services Belgium S.A.	65.06	60.18	4.88	7.50%	29.31%	Yes
4	Tata Consultancy Servcies, Netherlands BV	197.79	182.96	14.83	7.50%	29.31%	Yes
5	Tata Consultancy Servcies Asia pacific Pte.Limited	139.86	132.87	6.99	5.00%	8.59%	Yes
6	Tata Consultancy Services De Mexico S.A.De C.V.	3.87	2.90	0.97	25.00%	9.62%	No
7	Tata Consultancy Services Portugal UnipessonalLimited	0.89	0.76	0.13	15.00%	29.31%	Yes

Thereafter, the ALP margins have been modified by the Ld. CIT(A) by rejection of certain comparables selected by the assessee. The margin earned by the assessee with reference to the revised ALP, after modification, is presented in the following table:-

Sr.No	Name of the Entity	Entity revenue for offshore segment(A)	Paid to TCS (3CEB) (B)	Gross Profit-Offshore segment (C=A-B)	Gross Margin (C/A)	Comparable benchmark Region	ALP Gross Margin	Whether at ALP?
1	Tata America International Corp.	8,155.15	7,345.81	809.34	9.92%	North America	9.86%	Yes (after +/-5% working)
2	Tata consultancy Services Sverige AB	76.92	71.15	5.77	7.50%	Europe	16.53%	Yes
3	Tata Consultancy Services Belgium S.A.	65.06	60.18	4.88	7.50%	Europe	16.53%	Yes

4	Tata Consultancy Servcies, Netherlands BV	197.79	182.96	14.83	7.50%	Europe	16.53%	Yes
5	Tata Consultancy Servcies Asia pacific Pte.Limited	139.86	132.87	6.99	5.00%	Asia Pacific	5.70%	Yes
6	Tata Consultancy Services De Mexico S.A.De C.V.	3.87	2.90	0.97	25.00%	North America	9.86%	No
7	Tata Consultancy Services Portugal UnipessonalLimited	0.89	0.76	0.13	15.00%	Europe	16.53%	Yes

Finally, the Ld.CIT(A) held:-

> 13.16.8 the TPO/AO is directed to compute adjustments, if any, in line with the variation in ALP as per the margins computed in the above table. It is clarified that the margins have been computed by the appellant and the same have been relied on by this office. The TPO is free to examine the veracity of the computation of margins in respect of comparables selected by the appellant as this issue has not been looked into by the TPO at the time of TP proceedings. The TPO/AO will allow the appellant benefit of proviso to section 92C(2) if admissible. The various grounds taken by the appellant on this issue are decided accordingly.
>
> 13.16.9 At ground No.8.12, the appellant has also raised the issue of use of multiple year data. The issue of multiple year data is no longer res integra. The issue stands concluded in favour of Revenue through a number of judgments from High court and Tribunals. The language of the Rules are also specific on this issue. Only the data relating to the year under benchmarking can be adopted for computation of ALP unless the assessee is able to demonstrate that the earlier year data has impacted the current year PLI. In absence of any such evidence, the issue is decided against the appellant.
>
> 13.16.10 At ground No.8.13, the appellant has sought benefit of the second proviso to section 92C(2) of the Act. The benefit of this provision will be available to the appellant if the value of adjustment is within the range specified under the section. If the adjustment exceeds the range, the benefit of the proviso will not be available. It is held accordingly.

25. Before us, the Ld. Counsel for the assessee submits that during the year under consideration, it provided software, technical and consultancy services to its AEs and received Rs.8206.87 crores from its AEs in respect of rendering such services, which constituted international transactions. Out of the various AEs of the assessee, it had substantial additional transactions

with its AEs-Tata America International Corporation (TAIC) and hence, TAIC has been taken as reference/example. The aforesaid international transaction was benchmarked considering the assessee as the tested party and selecting TNMM as the most appropriate method. During the course of transfer pricing proceedings, the TPO asked the assessee to explain (with reference to transaction of provision of software, technical and consultancy services) as to why (i) the AEs should not be considered as the tested party (ii) TNMM with net cost plus as profit level indicator may not be applied to determine the ALP and (iii) net cost plus margin of 5.35% for AE not be considered as ALP based on a set of US companies.

It is stated by him that the TPO disregarded all the contentions and submissions made by the assessee and proposed an adjustment of Rs.466.79 crores by rejecting the tested party considered by the assessee and selecting the AEs as the tested party.

The Ld. Counsel submits that the assessee had entered into similar international transactions of provision of software, technical and consultancy services with its AEs in AYs 2003-04 and 2004-05 and in the transfer pricing proceedings, the TPO/AO, after detailed scrutiny accepted the methodology adopted by the assessee and held that its international transactions were undertaken at ALP. Thus, it is stated by him that having accepted the methodology adopted by the assessee for AY 2003-04 & 2004-05, the TPO/AO erred in taking a different view for AY 2007-08, completely ignoring the fact that there was neither any change in the facts of the case nor in the nature of operations or terms of the business of the assessee in AY 2007-08.

26. On the other hand, the Ld. DR submits that the TPO has rightly held TCS America and the other AEs of the assessee to be the tested parties; TNMM as the most appropriate method for determining the ALP.

27. We have heard the rival submissions and perused the relevant materials available on record. Similar issue arose before the ITAT in assessee's own case for AY 2009-10. The Tribunal, at para 20(page 59-62) held as under:-

> "20. We have considered rival submissions and perused the material on record. We have also applied our mind to the decisions relied upon. From the grounds raised by the Revenue, the following three issues arise for consideration - (i) what should be the appropriate PLI; (ii) whether cost of outsourcing / sub-contracting to the TCS should be considered for computing the margin; and (iii) whether the alternative benchmarking furnished by the assessee by treating the AEs as tested party with comparables in the same geographical locations is acceptable. On a careful perusal of the facts on record as well as submissions of the learned Counsel for the parties in the course of hearing as well as in the written note, we are of the view that the decision of learned Commissioner (Appeals) on the aforesaid issues are unassailable. As regards the issue of appropriate PLI, we are of the view that considering the nature of activity performed by the assessee as well as the AEs, it cannot be said that the A.Es are not bearing any risk. Rather the facts on record reveal that the AEs performed the role of risk bearing distributors. It is well brought out by learned Commissioner (Appeals) in his order that the AEs are bearing credit risk and risk of default by client. In fact, the assessee through proper evidences has demonstrated instances where the credit risk with reference to part cancellation of contract has been borne by the AEs without compensation from the assessee. The documentary evidences in this regard furnished by the assessee were thoroughly examined not only by learned Commissioner (Appeals) but they were also produced before us. Thus, from the aforesaid facts, it becomes clear that significant marketing functions are being performed and distribution and marketing risk are being taken by the AEs. On examination of the financials of the subsidiaries it is revealed that some subsidiaries are still making loss at net level which signifies that some risk is being borne by the AEs. It has further been brought on record that the manpower base of AEs performed various functions relating to marketing as well as client co-ordination. The AEs have developed sufficient competency to handle the marketing work independently. The entire contract related work is performed by the AEs, though, in cooperation with the assessee. Thus, it is quite natural that for being a sufficiently motivated work force, the AEs are compensated at return on sales and not merely on value added costs. Therefore, learned Commissioner (Appeals) was justified in directing the

> Transfer Pricing Officer to adopt the PLI of gross margin on sales. As regards consideration by the Transfer Pricing Officer, the outsourcing / sub-contracting cost to assessee as a pass through cost, learned Commissioner (Appeals) was absolutely correct in observing that the decision of the Transfer Pricing Officer to exclude such costs while computing the margin of the AEs is incorrect. When similar cost incurred by the comparables were not excluded while computing their margin, a different treatment cannot be given to such costs in case of the AEs. Certainly, the aforesaid approach of the Transfer Pricing Officer has resulted in distorting the correct PLI of the AEs. In the aforesaid context, the observations of learned Commissioner (Appeals) are appreciable, wherein, he has observed that the PLI of the AEs and PLI of comparables have not been computed on similar lines by the Transfer Pricing Officer, hence, comparability condition fails. It is further relevant to observe, the alternative benchmarking furnished by the assessee before the Transfer Pricing Officer by considering the AEs in different geographic locations as tested parties with the comparables selected on the basis of the respective geographic locations furnished before the Transfer Pricing Officer were not properly considered. However, in course of appeal proceedings, the learned Commissioner (Appeals) examined them in detail and after a detailed analysis approved some comparables selected by the assessee and also added some new comparables. Whereas, the comparable selected by the Transfer Pricing Officer were not on the basis of any detailed search process. At least, no such analysis is either forthcoming from the order of the Transfer Pricing Officer or could be brought to our notice by learned Departmental Representative. On the contrary, on a thorough and careful reading of the impugned order of learned Commissioner (Appeals), we are of the view that learned Commissioner (Appeals) has taken pains to examine in detail the alternative benchmarking done by the assessee with foreign comparables and after detailed analysis has shortlisted the final comparables to be considered for comparability analysis. No convincing argument or evidence has been brought on record by the learned Departmental Representative to persuade us to disturb the finding of learned Commissioner (Appeals) on these issues. In view of the aforesaid, we do not find any merit in the grounds raised by the Revenue on the issues. Accordingly, grounds are dismissed."

27.1 Facts being identical, we follow the above order of the Co-ordinate Bench and uphold the order of the Ld.CIT(A).

28. As we have affirmed the order of the Ld.CIT(A) on the matter that GP/sales is the appropriate PLI, the 6th ground of appeal, which relates to provision of software consultancy services becomes academic in nature.

29. <u>The 7th ground of appeal</u>

> 7.1 The Ld. CIT(A) erred in law and on facts in holding that the interest free loans outstanding/provided during the year by the appellant to its AEs are not at arm's length and in disregarding the fact that the loans given by the appellant are in substance "quasi-equity" in nature and as a part of shareholder's activity on which returns are not expected in the form of interest.

30. The Ld. Counsel submits that the above matter may be restored to the AO as similarly held by the Tribunal in assessee's own case for AY 2009-10. On the other hand, the Ld. DR relies on the order of the CIT(A)

We have heard the rival submissions and perused relevant materials available on record. Similar issue arose before the Tribunal in assessee's own case for AY 2009-10. The Tribunal *vide* para 37 held as under:-

> "37. We have considered rival submissions and perused the material on record. We have also carefully gone through the case law cited before us. Notably, right from the stage of transfer pricing proceeding itself the assessee has taken a stand that loans and advances to the AEs are in the nature of quasi equity, hence, cannot be treated as loan simpliciter. It is relevant to observe, the transfer pricing adjustment made on account of interest is in respect of loans advanced to four overseas AEs. From the details available on record, it is noticed that major portion of loans advanced to TCS Ibero America, is for acquisition of downstream subsidiary and about 20% of the advance was for working capital. Money advanced to TCS FNS Pty. Ltd., Australia, was purely for acquisition of downstream subsidiary. Similarly, advance to TCS Asia Pacific Pty. Ltd., is for acquisition of downstream subsidiary. Only the advance made to TCS Morocco is for working capital requirement. It is further noted, major part of advances made to TCS Ibero America, TCS FNS Pty. Ltd. and TCS Morocco have been converted to equity subsequently. It is also a fact on record that before learned Commissioner (Appeals), the assessee has filed a detailed written submission on 27th March 2014, elaborately discussing the nature of advance made to the AEs and the purpose for which such advances were made. It was submitted by the assessee that the advances made to the AEs were as a part of business strategy and not simply to help the AEs with capital infusion. The assessee has advanced detailed argument stating that advances made to the AEs is a shareholder activity and not advancement of loan. In this context, the assessee has referred to OECD Transfer Pricing Guidelines as well as UK and Australian Regulations. It is evident from the impugned order of the learned Commissioner (Appeals), though, he sketchily

> referred to some of the submissions made by the assessee, however, he has not at all dealt with them in an effective manner. The learned Commissioner (Appeals), though, has observed that the loans advanced were not merely for downstream acquisition but for a variety of purpose including working capital requirement and other business uses, however, he has not elaborated as to for what other purpose loans were advanced. Without properly dealing with the factual aspect of the issue, learned Commissioner (Appeals) has jumped to the legal aspect and has held that the amount advanced by the assessee is in the nature of loan and has to be benchmarked as such. After considering the submissions of the parties and examining the material on record, we are convinced that various submissions made by the assessee before learned Commissioner (Appeals) have not at all been dealt with. The primary contention of the assessee that the advance made to the AEs is in the nature of quasi equity and falls within shareholder's activity has not been properly addressed by the Departmental Authorities keeping in view the ratio laid down in the relevant case laws. It also requires deliberation whether it can be considered as an international transaction under section 92B r/w Explanation-1(c). Since, the aforesaid legal and factual aspects have not been considered properly, we are inclined to restore the issue to the file of the Assessing Officer for de novo adjudication after due opportunity of being heard to the assessee. The Assessing Officer must examine all relevant facts to find out the exact nature of the advances made to the AEs. He should also examine the applicability of the ratio laid down in the case of DLF Hotel Holdings Ltd. (supra) and any other case laws which may be cited before him. The assessee must be afforded reasonable opportunity of being heard. Ground is allowed for statistical purposes."

31. Facts being identical, we restore the matter to the file of the AO to make an order afresh as per the above direction given by the Co-ordinate Bench for AY 2009-10, after giving reasonable opportunity of being heard to the assessee.

32. The 8th ground of appeal

> 8.1 The Ld. CIT(A) erred in law and on facts, in holding that the provision of various guarantees by the appellant to third parties on behalf of its AEs were international transactions and in making an upward adjustment in this regard.
>
> 8.2 The Ld. CIT(A) erred in law and on facts, in not appreciating the fact that provision of guarantee is a shares holder activity and no income is generated from the same.

8.3 Without prejudice to the above, the Ld. CIT(A) erred in law and on facts in disregarding the appellant's contention that the guarantee fee should be charged based on the effective rate of insurance premium paid by the appellant as a percentage of group revenue.

8.4 Without prejudice to above, the Ld. CIT(A) erred in law and on facts in not considering guarantee fees to be charged on actual rent, for which the guarantee was provided.

33. The Ld. Counsel submits that part of the activity was performed by the assessee itself, while the remaining services are rendered by the AE; thus, if the performance guarantee is treated as chargeable services, the charges should be levied only on the component of services performed by the AE. With respective lease guarantee, it is submitted by him that part of the premises (i.e, 40% during the year under consideration) was occupied by the assessee and therefore, if lease guarantee is treated as chargeable service, the charge should be levied only for the balance (i.e, 60% during the year under consideration).

34. On the other hand, the Ld. DR relies on the order of the CIT(A) and submits that rightly the first appellate authority has directed the TPO to adopt a guarantee fee rate of 1.42% on the computed value of performance guarantee for computing the adjustment.

35. We have heard the rival submissions and perused the relevant materials available on record. Similar issue arose before the Tribunal in assessee's own case for AY 2009-10, wherein it is held:-

"43. We have considered rival submissions and perused the material on record. We have also applied our mind to the decisions relied upon. Insofar as the contention of learned Sr. Counsel for the assessee that provision of guarantee is not an international transaction as per section 92B of the Act, we are unable to accept such contention. In our considered opinion, after introduction of

> Explanation-(i)(c) to section 92B of the Act, with retrospective effect from 1st April 2002, provision of guarantee to AEs has to be considered as an international transaction. Different Benches of the Tribunal have also expressed similar view on the issue. Therefore, we hold that the provision of guarantee to the AEs is an international transaction. In fact, the aforesaid view has been expressed by the Co-ordinate Bench in WNS Global Services Pvt. Ltd. (supra). Therefore, following the aforesaid decision of the Co- ordinate Bench and the decision of the Hon'ble Jurisdictional High Court in Everest Canto Cylinders Ltd. (supra), we direct the Assessing Officer to charge guarantee commission @ 0.5% per annum both on performance / lease guarantee as well as financial guarantee."

Facts being identical, we follow the above order of the Co-ordinate Bench and direct the AO to charge guarantee commission @0.5% per annum both on performance / lease guarantee as well as financial guarantee. In this context , we direct the AO to examine the contentions of the assessee that (i)part of the activity with respective performance guarantee, was performed by the assessee itself, while the remaining services are rendered by the AE and thus, if the performance guarantee is treated a chargeable services, the charges should be levied only on the component of services performed by the AE (ii) part of the premises i.e. 40% during the year under consideration was occupied by the assessee and thus, if lease guarantee is treated as chargeable services, the charge should be levied only for the balance i.e. 60% during the year under consideration.

We direct the assessee to file the relevant documents/evidence on the above contentions before the AO.

36. <u>The 9th ground of appeal</u>:-

> 9.1 The Ld. CIT(A) erred in law and on facts in holding that the provision of undertaking by the appellant on behalf of its AE – Financial Network Services Pty. Ltd. Australia is an international transaction and making an upward adjustment in this regard.

> 9.2 The Ld. CIT(A) erred in law and on facts, in holding that the provision of undertaking by the appellant is similar to the provision of corporate guarantee, without appreciating the underlying facts.

37. The Ld. Counsel submits that the guarantee fee rate determined in case of performance guarantee, is found to be at arm's length charge in case of the undertaking.

On the other hand, the Ld. DR supports the order passed by the CIT(A).

38. As mentioned earlier, the Tribunal in assessee's own case has directed the AO to charge guarantee commission @0.5% per annum both on performance / lease guarantee as well as financial guarantee. Facts being identical, we follow the above order of the Co-ordinate Bench and direct the AO to adopt guarantee fee rate @0.5% per annum for the performance guarantee.

39. An additional ground has been filed by the assessee reads as under:-

> On facts and in circumstances of the case and in law, the 'education cess' paid by the appellant during AY 2007-08 being not covered by definition of tax under section 40(a)(ii) of the Income Tax Act shall be allowed as a deduction from its income.

40. As the above additional ground calls for determination of a legal point, we admit it for adjudication.

It is held by the Hon'ble Bombay High Court in *Sesa Goa Limited v. JCIT* (2020) 117 taxmann.com 96 (Bom.) that "education cess and higher and secondary education cess are liable for deduction in computing income chargeable under the head 'profits and gains of business or profession'."

Following the above decision, we allow the above additional ground.

41. In the result, the appeal filed by the assessee is partly allowed.

(ITA No. 3389/MUM/2017)

42. Now, we turn to the grounds of appeal filed by the revenue.

The 1st ground of appeal

> 1. On the facts and in the circumstances of the case and in law, the Ld.CIT(A) erred in deleting the addition of Rs.15,43,05,676/- disallowed u/s.40(a)(ia) of the Act, being payment for software imported from non-residents for internal use, relying on the decision of the Hon'ble Tribunal in assessee's own case for AY 2005-06 whereas the issue has not been decided by the Hon'ble Tribunal for A.Y. 2005-06.

43. As mentioned earlier at para 17.1, facts being identical, we have followed the order of the Co-ordinate Bench in assessee's own case for AY 2009-10. Following the same, this ground of appeal is dismissed.

44. The 2nd ground of appeal

> 2. On the facts and circumstances of the case and in law, the Ld.CIT(A) has erred in allowing claim u/s 10A of IT Act on units which deduction u/s 80HHE of IT Act was being claimed.

45. The Hon'ble Bombay High Court in assessee's own case in ITA.No.1778 of 2016 vide order dated 18/03/2019 has held that:

> "10. Coming to the revenue's contention in relation to the computation of benefit of section 10A of the Act, this issue is squarely covered by the judgment of Supreme Court in the case of Commissioner of Income Tax vs. HCL Technologies, reported in 404 ITR 719, in which the Court held that the total turnover for the purpose of section 10 of the Act cannot be understood as defined for the purpose of section 80HHE. It was further held that thus the expenses which are to be

excluded from the export turnover, would also have to be excluded for the purpose of computing total turnover."

Following the above decision, the second ground of appeal is dismissed.

46. The 3rd & 4th ground of appeal

3. On the facts and circumstances of the case and in law, the Ld.CIT(A) has erred in not upholding the order of the AO on the method of computation of deduction u/s 10A of IT Act.

4. On the facts and circumstances of the case in law, the Ld.CIT(A) has erred in not appreciating the fact that 30% of the expenses incurred in foreign currency on account of software development expenditure incurred abroad is in the nature of providing technical services and hence it is rightly reduced from export turnover computed u/s 10A.

47. In view of the order of the Tribunal, dated 04/11/2015 in assessee's own case for AY 2005-06 (ITA No.7513/M/2010), upholding that the expenditures which are required to be reduced from the export turnover as per the provisions of section 10A of the Act should also be reduced from the total turnover, we dismiss the above grounds of appeal.

48. The 5th ground of appeal:-

5. On the facts and circumstances of the case, the ld.CIT(A) erred in directing the AO to grant DIT relief u/s 90/91 of the Income Tax Act, 1961 in respect of income on which no income tax under Income Tax Act, 1961 was payable by the assessee.

49. As mentioned earlier at para 21 and 21.1, facts being identical, we have followed the order of the Co-ordinate Bench in assessee's own case for

AY 2009-10 and allowed similar grounds of appeal filed by the assessee. Following the same, the above ground of appeal is dismissed.

50. <u>The 6th to 9th grounds of appeal</u>

> 6 On the facts and circumstances of the case, Ld.CIT(A) erred in holding that the payments made to TCS are not be treated as pass through costs and thereby, holding OP/OC to the appropriate PLI instead of OP/VAE as determined by TPO.
>
> 7. On the facts and circumstances of the case, the Ld.CIT(A) has erred in giving direction to work out margin (OP/OC) of AE including cost incurred on (offshore) transaction assigned to TCS as against the decision of the TPO of adding margin only on cost incurred by the AE (excluding cost incurred by TCS) though it was held by CIT(A) himself in para 19.5 of the order that AEs are engaged in marketing and distribution liable to be compensated for limited function.
>
> 8. The Ld.CIT(A) has erred in rejecting comparables on the ground that third party cost is not excluded in comparables cases.
>
> 9. On the facts and circumstances of the case, the Ld.CIT(A) erred in giving finding in acceptability of ALP based on comparables selected separately for North America, Europe and Asia Pacific region ignoring comparables selected by TPO.

51. As we have affirmed at para 27, 27.1 & 28 hereinbefore the order of the Ld.CIT(A) on the matter that GP/sales is the appropriate PLI, the 6th to 9th grounds of appeal are dismissed.

52. <u>The 10th & 11th grounds of appeal</u>

> 10. On the facts and circumstances of the case, the Ld. CIT(A) erred in giving direction to charge guarantee commission on amount excluding approximately

68.66% of the revenue from offshore activities carried out by TCS though it was integral part of total contract amount of AE.

11. On the facts and circumstances of the case, the Ld. CIT(A) has erred in giving direction to chare guarantee commission @1.42% of lease financial guarantee in place of 3% charged by TPO.

53. As mentioned earlier at para 35, facts being identical, we have followed the order of the Co-ordinate Bench in assessee's own case for AY 2009-10. Following the same, the 10th & 11th grounds of appeal are dismissed.

54. In the result, the appeal filed by the Revenue is dismissed.

55. To sum up, the appeal filed by the assessee is partly allowed whereas the appeal filed by the Revenue is dismissed.

Order pronounced in the open Court on 11/11/2020.

Sd/-	Sd/-
(VIKAS AWASTHY)	(N.K. PRADHAN)
JUDICIAL MEMBER	ACCOUNTANT MEMBER

Mumbai;
Dated: 11/11/2020
Rahul Sharma, Sr. P.S.

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent.
3. The CIT(A)-
4. CIT
5. DR, ITAT, Mumbai
6. Guard file.

BY ORDER,

//True Copy//

(Dy./Asstt. Registrar)
ITAT, Mumbai