IN THE INCOME TAX APPELLATE TRIBUNAL
'A' BENCH : BANGALORE

BEFORE SHRI. CHANDRA POOJARI, ACCOUNTANT MEMBER
AND
SMT. BEENA PILLAI, JUDICIAL MEMBER

IT(TP)A No. 1111/Bang/2012
Assessment Year : 2008-09

M/s. Schneider Electric IT Business India Pvt. Ltd., [formerly known as American Power Conversion (India) Pvt. Ltd.] 187/3 & 188/3, Jigani, Bangalore – 562 106. PAN: AACCA6398Q	**Vs.**	The Additional Commissioner of Income Tax, LTU, Bangalore.
APPELLANT		**RESPONDENT**

Assessee by	**:**	Shri Ketan Ved, CA
Revenue by	**:**	Shri Sumer Singh Meena, CIT DR (OSD)

Date of Hearing	**:**	20-12-2021
Date of Pronouncement	**:**	28-02-2022

ORDER

PER BEENA PILLAI, JUDICIAL MEMBER

Present appeal has been filed by assessee against final assessment order under section 143(3) read with 144C of the Act dated 06/07/2012 passed by Ld.JCIT (LTU), Bangalore for assessment year 2008-09 on following grounds of appeal:

> *"A. Transfer Pricing adjustments-*
> *The learned Assessing Officer ("AO") and the learned Transfer Pricing Officer ("TPO") grossly erred in law and facts of the case in determining the arm's length price (`ALF') of the international transaction of the Appellant*

and thereby making an adjustment with respect to payments made by the tax payer u/s 92CA of the Income Tax Act for the following international transactions:

1. *Software development services:-Rs. 42,07,843/-;*
2. *Research and development services ("R&D"):- Rs.1,33,15,066/-;*
3. *Royalty Payment:- Rs. 8,99,53,689/-; and.*
4. *Interest on Outstanding receivables:- Rs.24,30,00,000/-.*

1. Software Development Services

1.1 The learned TPO and the learned AO grossly erred in law and facts of the case in determining the ALP of the international transaction of the Appellant and thereby making an adjustment of Rs. 42,07,843/- towards software development services.

1.2 That on the facts and circumstances of the case, the learned TPO and the learned AO erred in rejecting the Transfer Pricing ("TP") documentation without appreciating the contentions, arguments, and evidentiary data put forward by the Appellant during the course of the proceedings before them, and in doing so have grossly erred:

1.2.1. in adopting the arm's length mark up to be 23.65% in respect of international transactions of the Appellant.

1.2.2. in rejecting the upper limit for sales turnover filter proposed by the Appellant without providing any empirical analysis. In doing so, the learned TPO erred in not appreciating that the software industry is clearly demarcated based on size. The learned TPO has erred considering Igate Global Solutions Limited, Mindtree Consulting Limited, Flextronics (Aricent), Infosys Technologies Limited, Persistent Systems Limited, Sasken Communication Technologies Limited (Seg.), Tata Elxsi Limited (Seg.) and Wipro Limited (Seg.) as a comparable even though they do not satisfy the sales turnover filter.

1.2.3. in accepting companies of different year end and companies with abnormal/fluctuating profit margins.

1.2.4. in not maintaining consistency in applying quantitative filters to comparable companies, rejecting companies with diminishing revenue/
persistent losses and cherry picking of high margin comparable.

1.2.5. in considering 25 percent as the threshold limit for the related party transactions filter as this number is an arbitrary number that has been adopted without any judicial precedence or reasonable basis.

1.2.6. in applying the onsite filter for selection of software comparables with the use of the data obtained under section 133(6) of the Act. In doing so the learned TPO erred in rejecting Akshay Software Technologies Limited.
1.2.7. in accepting companies like R Systems International with different year ending solely based on the data obtained under section 133(6) of the Act.
1.2.8. in accepting companies like Avani Cimcon Technologies Limited, E-zest Solutions Limited, Kals Information Systems Limited, Persistent Systems Limited and Softsol India Limited for which segmental information was not available in the public domain but were accepted based on the data obtained under section 133(6) of the Act.
1.2.9. in accepting companies like Infosys Limited and Wipro Limited as a comparable companies even though the sales of Infosys and Wipro are significantly driven based on brand developed by them, and doing so the learned TPO have incorrectly overlooked the jurisdictional Delhi Income Tax Appellate Tribunal (ITAT) ruling in Agnity India Technologies India Pvt. Limited. (reference: ITA No. 3856(Del)/2010) where the ITAT ruled that a giant company like Infosys assuming all risk leading to higher profit cannot be considered as comparable to captive services providers assuming limited risk.
1.2.10. in accepting companies engaged in the provision of software product development like KALS Information Systems Limited, Avani Cimcon Technologies Limited, Quintegra Solutions Limited, Sasken
Communications Technologies Limited, Softsol India Limited,
Persistent Systems Limited and R Systems International Limited which are functionally not comparable to the Appellant's business.
1.2.11. in accepting Tata Elxsi Limited and Flextronics Software Systems Limited as a comparable company even though the company provides product design services, which is functionally not comparable to the Appellant's business.
1.2.12. in accepting Celestial Labs Limited as a comparable company even though it is a contract research company which also engaged in bio-informatics and hence functionally dissimilar to the Appellant. Further, Celestial Labs Limited has abnormal/fluctuating profit margins. Hence, the learned TPO have disregarded the various jurisdictional ITAT rulings in case of SAP LABS India Private. Limited. Vs. ACIT (reference ITANo.

398/Bang/2008), E-Gain Communication Private Limited (reference: ITA No. 1685/PN/07 - Pune).

1.2.13. in accepting Igate Global Solutions Limited, and Thirdware Solution Limited as a comparable even though no segmental data is available.

1.2.14. in rejecting SIP Technologies and Exports Limited based on the abnormal business activity filter without demonstrating how abnormal business activity i.e. the investment made by SIP Technologies and Exports Limited will affect its working capital requirement and cause abnormal margin/loss.

1.2.15. The learned TPO and the learned AO ought to have appreciated that the comparable companies considered by the TPO are independent entrepreneurs and are exposed to market risks unlike the Appellant and hence the market risk adjustment should be granted to nullify such differences.

1.2.16. The learned TPO and the learned AO erred in concluding that the Appellant is exposed to single customer risk and such risks are adjusted by setting off the single customer risk with the market risk adjustment.

2 Research & Development Services

2.1 The learned TPO and learned AO grossly erred in law and facts of the case in determining the ALP of the international transaction of the Appellant and thereby making an adjustment of Rs.1,33,15,066/- towards R&D services.

2.2 The learned TPO and learned AO erred in understanding the nature of business carried out by the Appellant. The learned TPO and learned AO have wrongly interpreted the functions of the Appellant and have wrongly compared the Appellant to pure R & D companies.

2.3 The learned TPO and learned AO erred in accepting Celestial Labs Limited and Engineers India Limited which are functionally not comparable to Appellant's business.

2.4 The learned TPO and learned AO has erred in considering Celestial Labs Limited as a comparable for software segment as well as research and development segment and considered the margin at entity level for both the segments.

2.5 The learned AO has erred in not eliminating Honda R&D (India) Private Limited. and Oil Field Instrumentation (India) Limited from the final set of comparables in the final assessment order, which was rejected by the DRP in their directions, after taking cognizance of submission made by the Appellant. The

learned AO erroneously included both the companies in the final set of comparables in the final assessment order.

2.6 The learned TPO and the learned AO ought to have appreciated that the comparable companies considered by the TPO are independent entrepreneurs and are exposed to market risks unlike the Appellant and hence the market risk adjustment should be granted to nullify such differences.

2.7 The learned TPO and the learned AO erred in concluding that the Appellant is exposed to single customer risk and such risks are adjusted by setting off the single customer risk with the market risk adjustment.

3 Royalty Payment

3.1 The learned TPO and learned AO grossly erred in law and facts of the case in determining the ALP of the international transaction of the Appellant and thereby making an adjustment of Rs 8,99,53,689/- towards royalty payment.

3.2 The learned TPO and learned AO erred in determining the arm's length price of Royalty to be "NIL" without providing any cogent analysis for the same.

3.3 The learned TPO and learned AO erred in disregarding the benefits received by the Appellant on account of use of intangibles for which the royalty is paid.

3.4 The learned TPO and learned AO erred in rejecting the adoption of Comparable Uncontrolled Price (CUP) method by the Appellant with respect to justification of ALP of Royalty transaction.

3.5 The Learned TPO and learned AO erred in interpreting that Transaction Net Margin Method (TNMM) was applied for justification of ALP of Royalty transaction.

4 Imputed Cost

4.1 The learned TPO and learned AO grossly erred in law and facts of the case in determining the ALP of the international transaction of the Appellant and thereby making an adjustment of Rs 24,30,00,000/- towards imputed cost.

4.2 The learned TPO and learned AO has grossly erred in subjecting a hypothetical income to tax by way of imputing notional interest on the outstanding recoverable balances as shown in the books of Appellant with reference to the Associated Enterprises ("AE(s)").

4.3 The learned TPO failed to appreciate the fact that only "real income" can be brought within the ambit of taxation and that since no income has been earned or can be said to have been earned by the Appellant in respect of

interest chargeable from AEs, imputing interest with a view to realizing income would be unwarranted and unjustified.

4.4 The learned TPO and learned AO has erroneously computed the receivables balance of more than six months as Rs. 324 crores and ignoring the contentions of the Appellant highlighted in the DRP submissions and reply to the show cause notice.

4.5 Notwithstanding the arguments provided above, that on the facts and circumstances of the case, the learned TPO and the learned AO erred

4.5.1 in considering the fixed deposit rate of 10% to compute the notional interest rate. The CUP method followed by the TPO is not reflective of an arm's length interest rate since the fixed deposit rates obtained are not appropriate CUP rates for computing interest rates on trade receivables.

4.5.2 in ignoring the fact that as at 31st March 2008, there exist in the books of account, balances in the nature of payables pertaining to the dues owed by the Appellant to various. No interest has been charged by or paid to the AEs in respect of such balances. The TPO ought to have netted off the payables balance outstanding with the AEs with the receivable balance outstanding as on 31st March 2008.

4.5.3 in considering the interest for 9 months while the additional credit period granted to AEs in comparison to third party debtors, was limited to only 23 days.

5 Common grounds

5.1 That the learned TPO and the learned AO erred in disregarding the use of multiple year data and ought to have accepted the use of contemporaneous data due to non-availability of current year data in the public domain at the time of preparing the documentation.

5.2 That the learned TPO and the learned AO erred in disregarding the fact that the Appellant has claimed tax benefits under section 10 A of the Act and has no reason to suppress its profits from its operation to manipulate the transfer prices. Therefore the adjustment proposed is not called for and is hence misplaced.

5.3 That the learned TPO and the learned AO erred in not allowing the benefit of range of +/- 5% as provided in proviso to Section 92C(2) of the Act to the Appellant, while determining the arm's length price.

B. Non-transfer pricing adjustments-

6. Donations for 10A units: Rs. 18,52,713

6.1 The learned AO/ DRP has erred in disallowing the donation expenditure without attributing the same to the corresponding unit where it was incurred.

6.2 The learned AO/DRP ought to have observed that the said expenditure pertains to the unit eligible to avail benefit under section 10A of the Act.

6.3 The learned AO/DRP ought to have considered such expense recorded under the head "donations" relating to 10A unit as part of "income from business" while recomputing deduction under section 10A of the Act.

7. Disallowance of provision for warranty : Rs. 25,22,70,000

7.1 The learned AO/ DRP has erred in disallowing the unutilised warranty provision amounting to Rs.25,22,70,000.

7.2 The learned AO/ DRP has erred in stating that unavailed provisions for warranty are not reversed/written back and offered as income.

7.3 The learned AO has erred in not considering the copy of ledger extract of warranty expenses, which clearly states that the provisions for warranty created by the assessee during a particular year are reversed on the first date of the next year and fresh provisions are created for the next year based on the analysis of the position of goods sold as on the close of the next year.

7.4 The learned AO has erred in not following the directions of the learned DRP to examine the contentions of the assessee and come to a conclusion in the matter placing reliance on the decision of the Supreme Court in the case of CIT vs. Rotork Controls India Pvt., Ltd. (314 ITR 62).

8. Disallowance of provision for stock obsolescence: Rs.17,50,90,601

8.1 The learned AO/ DRP has erred in disallowing the provision for stock obsolescence created during the year amounting to Rs.17,50,90,601.

8.2 Notwithstanding and without prejudice to above, the learned AO/DRP erred in disallowing a sum of Rs. 17,50,90,601 as against the amount debited to the profit and loss account being Rs.13,96,42,250.

8.3 Notwithstanding and without prejudice to the above, the learned AO/ DRP has erred in adding back the said amount while computing the income of the non-10A unit whereas the said provision pertains to the 10A unit.

8.4 Notwithstanding and without prejudice to the above, the learned AO/ DRP has erred in not considering

such additions to form part of the "income from business" of the 10A unit.

8.5 Notwithstanding and without prejudice to the above, the learned AO/ DRP has erred in not considering such reversal of provision for stock obsolescence relating to the non-10A unit as part of "income from business" while computing the taxable income.

9. Reversal of provision for stock obsolescence: Rs. 3,54,48,351

9.1 The learned AO/ DRP has erred in not considering the reversal of expenses amounting to Rs. 3,54,48,351 (Rs.17,50,90,601 - Rs.13,96,42,250) while disallowing the amount in the computation of taxable income.

9.2 Notwithstanding and without prejudice to the above, the learned AO/ DRP has erred in not considering such reversal of provision for stock obsolescence relating to the non-10A unit as part of "income from business" while computing the taxable income.

10. Disallowance of advances written off : Rs.1,13,48,714

10.1 The learned AO has erred in disallowing the amount written off towards advances given to M/s Elecomponis Sales Pvt Ltd. amounting to Rs.1,13,48,714.

10.2 The learned AO has erred in disregarding the documentary evidences produced before him consequent to the directions given by the DRP in this regard.

10.3 The learned AO has erred in not following the directions of the learned DRP to examine the contentions of the assessee and come to a conclusion accordingly.

10.4 Notwithstanding and without prejudice to the above, the learned AO/ DRP has erred in not considering such write off relating to 10A unit as part of "income from business" while re-computing deduction under Section 10A of the Act for the relevant unit.

11. Deduction under Section 10A-Communication expenses: Rs. 57,46,868

11.1 The learned AO/ DRP erred in re-computing the deduction under section 10A of the Act after reducing the communication expenses of Rs. 57,46,868/- from Export Turnover.

11.2 The learned AO/ DRP erred in considering the communication expenses as attributable to the delivery of software outside India for the purposes of computing the deduction under section 10A of the Act.

11.3 The learned AO/ DRP ought to have observed that the communication expenses were incurred towards lease line expenses and not specifically for the delivery of software outside India.

11.4 Notwithstanding and without prejudice to the above, should the communication expenses be reduced from the export turnover, the learned AO/DRP erred in not reducing such expenses from the total turnover also while computing deduction under section 10A of the Act.

11.5 The learned AO/ DRP erred in not placing reliance on judicial precedents in this regard.

12. Calculation of Interest on resulting adjustment under section 234B of the Act: Rs. 3,68,94,858

The learned AO has erred in computing interest under section 234B of the Act consequent to the above adjustments.

13. Calculation of Interest on resulting adjustment under section 234D of the Act: Rs. 1,98,82,191

The learned AO has erred in computing interest under section 234D of the Act consequent to the above adjustments.

The appellant craves leave to add, alter and modify the above grounds during the course of the appeal.

For the above and any other grounds which may be raised at the time of hearing, it is prayed that the order of the Assessing officer be set aside."

2. <u>Brief facts of the case are as under:</u>

Assessee filed its return of income for year under consideration on 30/09/2008 declaring income of Rs.28,65,73,837/-. The same was processed under section 143(2) and statutory notices was subsequently issued to assessee, in response to which, representative of assessee appeared before Ld.AO and filed requisite details as called for.

2.2 Ld.AO observed that assessee has three units, enjoying benefit of section 10 A known as EHTP Units-I and II and Software unit II, besides a domestic unit. It was observed by Ld.AO that assessee debited sum of Rs.57,63,39,197/- towards communication charges, which formed part of deduction claimed

under section 10A. Ld.AO was of opinion that, as per Clause (iv) of Explanation 2 to Section 10A, export turnover for purposes of claiming deduction, does not include fright, telecommunication charges, insurance attributable to the delivery of the articles or things or computer software outside India or expenses if any incurred in foreign exchange in providing technical services outside India.

2.3 Ld.AO accordingly restricted the deduction amounting to Rs.57,54,42,273/-. The Ld.AO disallowed the communication charges relating to software unit amounting to Rs.8,96,924/-.

2.4 Ld.AO further observed that assessee debited expenses towards donation amounting to Rs.18,52,713/-. Ld. AO disallowed the sum by holding that eligibility of deduction under section 80G of the Act was not substantiated.

2.5 Ld.AO observed that assessee entered into international transaction with its associated enterprises, and therefore for determining arms length price of international transaction, case was referred to Ld.TPO.

2.5.1 Ld.TPO upon receipt of reference called for economic analysis of international transaction entered into by assessee.

2.5.2 From documentation so filed, it was observed that, assessee was a subsidiary of American Power Conversion Corporation, U.S., primarily engaged in manufacture of power protection equipment and undertakes trading of UPS and accessories. Ld.TPO observed that, assessee primarily exported by way of sales to its associated enterprises and also had sales of manufactured products in domestic market within India.

2.5.3 In TP study, it has been submitted that AE provides all technical support services in nature of software application development and maintenance and research and development in nature of software design and testing services. Ld.TPO observed that assessee entered into following international transactions with its associated enterprise:

Purchase of components	Rs.196,330,739/-
Components sale	Rs. 66,430,718/-
Purchase of finished goods	Rs. 304,631,033/-
Sale of finished goods	Rs. 17,773,880,406/-
Sale of Fixed assets	Rs. 13,149,580/-
Purchase of fixed assets	Rs. 46,962,598/-
Royalty	Rs. 89,953,689/-
Provision of technical support and research and development	Rs. 129,571,302/-
Reimbursement of cost to APC India for expenses incurred for AE	Rs. 118,020,363/-
Reimbursement of cost for expenses incurred by AE	Rs. 20,555,120/-
Data communication charges and reimbursement of expenses	Rs. 8,987,400/-

Royalty

2.6. Ld.TPO observed that assessee paid sum of Rs.8,99,53,689/- as royalty to its AE. From TP study, Ld.TPO observed that each of manufacturing subsidiaries of AE entered into nonexclusive license agreement with AE, for license of technology and trademark intangibles, for using manufacturing and royalty was payable on such revenues from sale of products in their local territories. Ld.TPO observed that assessee during year under consideration entered into similar exclusive license agreement with its AE, according to which royalty at 4.5% was payable on

domestic sale of manufactured products by assessee in local markets within India. It has been submitted that, it is the AE who owns all intellectual property rights, trademarks, patents, copyrights, trade secrets, confidential business information, inventions, discoveries and know-how is, manufacturing and product processes and techniques, research and development information, copyrightable works and all other proprietary rights.

2.6.1 Ld.TPO on perusal of submissions advanced by assessee concluded that assessee did not prove any tangible benefit derived by paying royalty for so-called superior technology and that any independent enterprise would like to pay royalty to access superior technology, only if the same results in either reduction of cost or improved profitability. Ld.TPO concluded that, loss incurred in domestic segment was mainly due to payment of royalty, which otherwise would not be paid between two independent enterprises, dealing at arms length.

2.6.2 Ld.TPO thus determined ALP of royalty as 'nil". He thus proposed adjustment of Rs.8,99,53,689/- as value of these transaction in uncontrolled conditions.

Technical Support services.

2.7 Ld.TPO observed that during the year assessee rendered technical support services to its AE's, against which revenue amounting to Rs.3,64,35,403/- was received. It was observed in TP study that, assessee used TNMM as most appropriate method, with PLI of OP/TC and determined margin of assessee to be at 9.73%. Assessee selected following 16 comparables in transfer pricing study with average margin of 11.66%, and since

assessee's margin was within the range of +/-5%, transaction with its AE's were considered to be at arms length.

List of assessee's comparables:

1. Akshay Software Technologies Ltd.
2. F C S Software Solutions Ltd.
3. Goldstone Technologies Ltd.
4. ICRA Techno Analytics Ltd.
5. Indus Networks Ltd.
6. Larsen & Toubro Infotech Ltd.
7. Melstar Information Technologies Ltd.
8. P S I Data Systems Ltd.
9. Powersoft Global Solutions Ltd.
10. S I P Technologies & Exports Ltd.
11. Synetairos Technologies Ltd.
12. Computech International Ltd.
13. Karuturi Networks Ltd.

2.7.1 Ld.TPO on examination of TP documentation filed by assessee was of opinion that assessee is mainly offshore research and development service provider and these services are akin to software development services. Ld.TPO accordingly rejected comparables selected by assessee and finalized 20 comparables with average margin of 23.65% which are as under:

Sl. No.	Name of the company	OP/TC %
1	Avani Cincom Technologies	25.62
2	Bodhtree Consulting Ltd	18.72
3	Celestial Biolabs	87.94
4	e-zest Solutions Ltd	29.81
5	Flextronics(Aricent)	7.86
6	iGate Global solution ltd	13.99

7	Infosys	40.37
8	Kals Information systems ltd(seg)	41.94
9	LGS Global Ltd	27.52
10	Mindtree Ltd(seg)	16.41
11	Persistent Systems Ltd	20.31
12	Quintegra Solution Ltd	21.74
13	R systems International(seg)	15.30
14	R S Softwrare (India) Ltd	7.41
15	Sasken Communication Technologies ltd(seg)	7.58
16	Tata Elxsi(Seg)	18.97
17	Thirdware solution Ltd	19.35
18	Wipro Ltd(Seg)	28.45
19	Softsol India Ltd	17.89
20	Lucid Software Ltd	16.50
	AVERAGE	**23.65**

Ld.TPO thus proposed adjustment under this segment amounting to Rs.42,07,843/-.

Research and Development

2.8 Ld.TPO observed that assessee undertook research and development services during year. Arms length price of international transaction representing research and development services was determined by applying TNMM as most appropriate method and OP/TC as PLI. Assessee computed its margin at 10% on cost and average margin of 3 comparables were determined at 7% in TP study report. Assessee thus held that the transaction was within +/5% of the price charged and thus was treated to be at arms length.

2.8.1 Ld.TPO accordingly called for economic analysis and by applying various filters and rejected comparables selected by assessee and brought on new set of following 7 comparables having average margin of 24.33%.

Comparables selected by TPO for R&D segment

Sl.No.	Company Name	Sales	Operating Profit (OP)	Operating Cost (OC)	OP / OC	OP / Sales

1.	Honda R & D (India) Pvt. Ltd.	20.6	0.6	20	3%	2.91
2.	Research Support Intl. Pvt. Ltd.	14.54	0.94	13.6	6.91%	6.46
3.	Celestial Biolabs Ltd.	20.21	8.59	11.62	73.92%	42.50
4.	Clinigene International Ltd.	22.72	3.39	19.33	17.54%	14.92
5.	IDC (India) Ltd	15.68	2.11	13.57	15.55%	13.46
6.	Oil Field Instrumentation (India) Ltd.	27.65	8.66	18.99	45.60%	31.32
7.	Jindal Drilling & Inds. Ltd.	412.76	29.91.	382.85	7.81%	7.25
			Arithmetic Mean			

3. Aggrieved by adjustments proposed by Ld.TPO, under various segments assessee raised objections before DRP, who upheld view of Ld.TPO.

3.1 On receipt of DRP directions, Ld.AO passed final impugned assessment order, wherein following additions were made

- transfer pricing additions in software service development segment was made amounting to Rs.42,07,843/-
- transfer pricing addition in research and development segment was made at Rs.1,33,15,066/-
- disallowance of Royalty amounting to Rs.8,99,53,689/-.
- deduction claimed by assessee under section 10 A of the Act, was restricted to Rs.57,46,868/-, being 80% of expenses claimed.
- Donation paid amounting to Rs.18,52,713/- claimed as deduction under section 10 A
- Disallowance of Provision of Warranty Rs. 25,22,70,000/-

- Disallowance of Provision of Stock Obsolescence Rs.17,50,90,601/-
- Disallowance of advances written off Rs. 1,13,48,714/-
- Disallowance of claim u/s.10A of unbilled revenue.

4. Aggrieved by order passed by Ld.AO, assessee is in appeal before us now.

4.1 Ld.AR submitted that **Ground No. 1.1 and 1.2** are general in nature, and therefore do not require any adjustment.

4.2 Ld.AR further submitted that **Ground No. 1.2.1-1.2.5** are to not pressed. Accordingly these grounds are dismissed as not pressed.

5. Assessee also raised **Additional Ground No.1.2.17 & 1.2.18 vide applications dated 04/04/2013 and 03/06/2013** that reads as under:

> *No. 1.2.17: The Appellant submits that the learned Transfer Pricing Officer("TPO") has erred in including Bodhtree Consulting Limited(Bodhtree) as a company comparable to Appellant, while doing the comparability analysis.*
>
> *No.1.2.18: The Appellant submits that the learned Transfer Pricing Officer("TPO") ought to have granted working capital adjustments to the Appellant.*

5.1. Assessee has raised **Additional ground vide application dated 21/08/2019** seeking the claim of deduction of unbilled revenue under section 10A of the Act.

Additional Ground:

> **14. Without prejudice to our claim of deduction under section 10A of the ACT of the unbilled revenue for AY 2007-08, the learned AO/DRP erred in not granting deduction under section 10A of the Act in the impugned year on the unbilled revenue**

which was disallowed for AY 2007-08 on the basis of realisation of exports, thereby permanently denying tax holiday on the said export revenue.

5.2. Assessee has raised **Additional ground vide application dated 17/12/2020**, seeking deduction in respect of educational cess, secondary and higher secondary cess on income tax, being **Ground No.14** which is as under:

Additional Ground:

"***Ground no. 14: Deduction in respect of 'education cess on income-tax' and 'secondary and higher education cess on income-tax' for the year under consideration, while assessing the total income of the Appellant***

It is submitted by the Ld.AR that above additional Grounds are purely a legal issue and no new facts needs to be visited for its adjudication.

It is submitted that at the time of transfer pricing proceedings, assessee could not get the details regarding the extraordinary events that Bodhtree underwent during the relevant year. It was for this reason that the same could not be objected before the Ld.TPO and DRP.

In respect of the non granting of working capital adjustment, the Ld.AR submitted that the Ld.AO observed that assessee had not claimed the WCA which is incorrect. And that this came to the notice of assessee post filing of appeal before this Tribunal.

Placing reliance upon decision of *Hon'ble Supreme Court* in case of *NTPC Ltd. v. CIT* reported in (*1998) 229 ITR 383* and *Jute Corpn. of India Ltd. v. CIT* reported in (*1990) 53 Taxman 85*, submitted that comparables specified in additional grounds may

be admitted. Ld.CIT DR, though opposed admission of additional ground, could not controvert submissions advance by Ld.AR.

We have perused details relied upon by both sides In our considered opinion comparables alleged in additional ground arises out of records and was objected before DRP for its exclusion/inclusion. Considering inadvertent mistake on behalf of assessee in raising these grounds before this Tribunal, we allow additional ground raised now.

Accordingly additional ground no. 1.2.17, 1.2.18 & 14 in application dated 08/04/2013, 03/06/2013, 21/08/2019 & 17/12/2020 stands allowed.

6. Ground No.1.2 -1.2.16 along with Additional Ground no.1.2.17 vide Application dared 08/04/2013 are raised by assessee challenging addition made by Ld.AO on account of arms length price computed for software design and development service segment being technical support services provided by assessee to its AE's. The Ld.AR submitted that only issue disputed by assessee in Ground nos.1.2.8 to 1.2.13, Additional Ground no.1.2.17 is in respect of comparables selected by Ld.TPO. Primary, allegations regarding comparables on the ground of functional dissimilarity with assessee and does not fulfill filters applied by Ld.TPO himself.

6.1 Ld.AR submitted that following comparables have been objected by assessee for inclusion in Ground nos.1.2.8 to 1.2.13, Additional Ground no.1.2.17:

♦ Avani Cimcom Technologies Ltd.

♦ Celestial Labs Ltd.

♦ E-Zest Solutions Ltd.

♦ KALS Information Systems Ltd

♦ Persistent Systems Ltd

♦ Softsol India Ltd.

♦ Infosys Ltd.

♦ Wipro Ltd. (seg.)

♦ R.S.Systems International Ltd

♦ Tata Elxi Ltd.

♦ Flextronics Software Systems Ltd. (Seg.)

♦ Celestial Labs Ltd.,

♦ iGate Global Solutions Ltd.,

♦ Thirdware Solutions Ltd.

♦ Bodhtree Consulting Ltd.

6.3 Before we go into compatibility analysis of these comparables with that of assessee, it is sine qua non to understand functions performed, assets owned and risks assumed by assessee under this segment.

Functions Performed:

Functional analysis Information and specifications:

The technical support services performed by APC India are based on the instructions and specifications provided by APCC US. There are regular interactions with APCC US regarding project specifications and obtaining certain clarifications/information on the projects provided by APCC US to APC India.

Technical assistance and clarifications

We understand that APCC US provides technical assistance, information and certain technical clarifications in the provision of technical support services provided by APC India. There are

regular weekly updates by the IDC to APCC US on the status of the projects/activity assigned by APCC US.

Training

APC India provides both internal and external training to its employees. These training programs could be organized either in the US or in India.

Design and software development

APC India does not develop software products for sale in open market. It caters to the specific needs of APCC US and its associated enterprises worldwide that help exploiting new opportunities by harnessing knowledge of business processes with proven skills in applying technology.

Technical support and maintenance activity

APC India provides internal technical support services which includes creating, maintaining or enhancing APC company-wide internal use software infrastructure.

Billing and collection

APC India is responsible for raising invoices and their subsequent collection.

Assets Owned:

It has been submitted in TP study that, assessee does not own any significant intangible assets. It only has technical manpower employed and trained by company being most important assets along with furniture fixtures computer peripherals etc.

Risks Assumed:

It is submitted that, as assessee is a captive service provider and is compensated at cost +10%, it does not bear any risks like market risk, financial risk, credit and collection risk and service

liability risk. Only risk that would be assumed by assessee is in terms of foreign exchange risk as revenue received by assessee is in foreign exchange.

6.4 Thus, assessee has been categorized as a routine service provider undertaking contract software development services assuming normal risk associated with carrying out such business.

7. In our considered opinion, comparability is to be carried out on broad object of benchmarking international transaction and according to law laid down under section 92B of the Act, read with rule 10 B (2) Income tax Rules, 1963. Comparables must be similar in material aspects and must be compared on basis of products/services characteristics, functions undertaken, assets used and risk assumed. Merely because certain comparables has been upheld for its exclusion/ inclusion by various decisions, does not ipso facto lead to exclusion/inclusion in a given set of facts. In our considered opinion, exclusion/inclusion of any comparables must be strictly analysed on basis of FAR, in accordance with rule 10 B (2). We also are of opinion that comparables selected must be for relevant year which is to be compared and unless contemporaneous data as section 92D read with Rule 10 D (4), is not available for a relevant year, multiple year data should not be used.

Characterisation:

Based upon above FAR analysis, we shall now undertake compatibility tests of assessee with comparables under objection for inclusion.

8.1 At the outset, Ld.AR submits that for year under consideration, in the event, following comparables are considered for exclusion, assessee would be within acceptable arms length margin.

♦ Avani Cimcom Technologies Ltd.

♦ Celestial Labs Ltd.

♦ E-Zest Solutions Ltd.

♦ KALS Information Systems Ltd

♦ Persistent Systems Ltd

♦ Infosys Ltd.

♦ Wipro Ltd. (seg.)

♦ R.S.Systems International Ltd

♦ Tata Elxi Ltd.

♦ Flextronics Software Systems Ltd. (Seg.)

♦ Softsol India Ltd.

♦ Celestial Labs Ltd.,

♦ iGate Global Solutions Ltd.,

♦ Thirdware Solutions Ltd.

♦ Bodhtree Consulting Ltd.

6.2 The Ld.AR submitted that this *Tribunal* in various decisions excluded these comparables on functional dissimilarity. He further placed reliance on decision of this Tribunal in assessee's own case in *Schneider Electric IT Business India (P.) Ltd. v. Dy.CIT* reported in *(2019) 109 taxmann.com 187, Schneider Electric IT Business India (P.) Ltd. vs. JCIT* reported in *(2019) 106 taxmann.com 70* and *Schneider Electric IT Business India (P.) Ltd. v.ACIT(LTU)* reported in *(2020) 113 taxmann.com 215*, wherein these comparables have stood excluded.

8.2 In respect of remaining comparables, Ld.AR submitted that liberty may be granted to argue their exclusion in appropriate circumstances.

We note that this Tribunal in assessee's own case for assessment year 2007-08 excluded following comparables on functional dissimilarity by observing as under:

8.2.3 Avani Cimcon Technologies Ltd.

It has been submitted that this company is functionally different from the assessee. Based on the information available in company's website, it has been submitted that this company developed a software product by name "DXchange". It was also submitted that this company has revenue from software product sales, apart from rendering of software services for which segmental information is not available. It has therefore been submitted that this company is functionally different from assessee. It was further submitted that Mumbai Bench of Tribunal in case of Telcordia Technologies India (P.) Ltd. v. Asstt. CIT [2012] 22 taxmann.com 96/137 ITD 1 accepted assessee's contention that this company has revenue from software product and observed that in absence of segmental details, Avani Cincom cannot be considered as comparable to an assessee who was rendering captive software development services.

Ld.DR, on the other hand, relied on order of Ld.TPO.

We have considered submissions advanced by both sides and perused records placed before us.

It was submitted that this company has made unusually high profit during the financial year 2006-07. It is observed that operating revenues increased 63.03% which indicates that it was an extraordinary year for this company. Even growth of software industry for previous year as per NASSCOM was 32%. The growth rate of this company was double the industry average. In view of the above, it was argued that this company ought to have been rejected as a comparable.

It was observed by this Tribunal in case of Telcordia Technologies India (P.) Ltd. (supra) that margin of this company is 52.59% which represents abnormal circumstances and profits. Following figures were relied by Ld.AR, as observed by coordinate bench of this Tribunal in case of First Advantage Offshore Services (P.) Ltd. v. DCIT [IT (TP) Appeal No. 1086 (Bang.) of 2011]:-

Particulars	*05-06*	*06-07*	*07-08*	*08-09*
Operating Revenue	21761611	35477523	29342809	28039851
Operating Expense	16417661	23249646	23359186	31108949
Operating	5343950	12227877	5983623	(3069098)

Profit				
Operating Margin	32.55%	52.59%	25.62%	- 9.87%

We, therefore, direct Ld.TPO to exclude this company from final list.

8.2.4 Celestial Labs Ltd.

It has been submitted that this research & development company. In this regard, the following submissions were made:-As per Notes to Accounts - Schedule 15, under "Deferred Revenue Expenditure", it is mentioned that, "Expenditure incurred on research and development of new products has been treated as deferred revenue expenditure and same has been written off in 10 years equally yearly installments from the year in which it is incurred." An amount of Rs.11,692,020/- has been debited to Profit and Loss Account as "Deferred Revenue Expenditure". This amounts to nearly 8.28 percent of sales of this company.

Reliance was made to decision of Mumbai Bench of Tribunal in case of Teva Pharm (P.) Ltd. v. Addl. CIT [2012] 18 taxmann.com 148/50 SOT 150 (URO) in which comparability of this company for clinical trial research segment. The Company has developed a drug design tool "CELSUITE" to find lead molecules for drug discovery and has patented the same. It has observed that this Company developed molecule to treat Leucoderma and multiple cancer which is also protected under IPR by filing patent. It is observed that this company is planning to set up biotechnology facility to manufacture industrial enzymes, which include research laboratories for carrying out further R & D activities to develop new drug molecules and license them to Interested Pharma and Bio Companies across the GLOBE. It is thus observed that this company is into diversified activities and therefore cannot be considered as functionally comparable with Assessee who is a captive service provider. It was thus submitted that, this company is not into software development activities, accordingly, this company should be rejected as comparable being functionally different.

Ld.DR, on the other hand, relied on order of Ld.TPO.

We have considered submissions advanced by both sides and perused records placed before us.

It has been pointed out that this company provides software products/services as well as bioinformatics services and that the segmental data for each activity is not available and therefore this company should not be treated as comparable. Besides the above, the Assessee pointed out from annual report highlighting the fact that, this company is into developing biotechnology products and provides related software development services, without any segmental details. There is no detail regarding nature of software development services performed by this company. Celestial labs had come out with a public issue of shares and in that connection issued Draft Red Herring Prospectus (DRHP) in which business of this company was explained as to clinical research. We are of the view that in light of submissions made by Ld.AR and the fact that this company was basically/admittedly in clinical research and manufacture of bio products and other products, there is no clear basis on which it could be held that this company is mainly in the business of providing software development services.

We therefore direct Ld.TPO to exclude this company from final list.

8.2.5 E-Zest Solutions Ltd:

This company has been selected by Ld.TPO and objected by assessee on the ground that, it was functionally different from assessee. Ld.TPO rejected contentions of assessee on the basis of information received in response to notice under section 133(6) of the Act, wherein it was held that this company is engaged in software development services. It was thus held by Ld.TPO that this company satisfies all filters.

Ld.AR submitted that this company ought to be excluded from the list of comparables on the ground that it is functionally different to the assessee. He submitted that this company is engaged in 'e-Business Consulting Services', consisting of Web Strategy Services, IT design services and in Technology Consulting Services including product development consulting services, and are high end ITES normally categorized as knowledge process outsourcing ('KPO') services. It is further submitted that this company has not provided segmental data in its annual Report, and does not contain detailed descriptive information on the business of the company. It is also submitted that KPO services are not comparable to software development services and therefore companies rendering KPO services ought not to be considered as comparable to software development companies. In support of, he placed reliance on decision of co-ordinate bench of this Tribunal in case of Hewlett Packard (I) Globalsoft (P.) Ltd. v. Dy. CIT [2015] 63 taxmann.com 136 (Bang. - Trib.)

On the contrary, Ld.DR supported the inclusion of this company in the list of comparables by the TPO.

We have heard rival submissions and perused and carefully considered material on record.

It is seen from record that Ld.TPO included this company on the basis of statement made by the company in its reply to notice under section 133(6) of the Act. It appears that Ld.TPO did not examine services rendered by this company to give a finding whether services performed by this company are similar to Captive software development services performed by assessee. From details on record, we find that while assessee is a captive software development service provider, this company i.e. e-Zest Solutions Ltd., is rendering product development services and high end technical services which come under category of KPO services. It has been held by co-ordinate bench of this Tribunal in case of Hewlett Packard (I) Ltd. (supra) that KPO services are not comparable to software development services and are therefore not comparable. Following the aforesaid decision of the co-ordinate bench of the Hyderabad Tribunal in the aforesaid case, we hold that this company, i.e. e-Zest Solutions Ltd. be omitted from set of comparables for period under consideration

We therefore direct Ld.TPO to exclude this company from final list.

8.2.6 Flextronics Software Ltd.(Seg.)

This comparable has been selected by Ld.TPO in final list and objected by assessee due to non availability of reliable financial data for year under consideration.

He submitted that Ld.TPO obtained information us/ 133(6), which is contrary to annual report and therefore is not reliable It has been submitted that the annual report is for year ending 31.03.2007 for a period of nine months and Ld.TPO whithout reconciliation between annual report and information received u/s.133(6) considered in the final list. In support of, he placed reliance on decision of co-ordinate bench of this Tribunal in case of Hewlett Packard (I) Ltd. (supra).

On the contrary, Ld.DR supported the inclusion of this company in the list of comparables by the TPO.

We have heard rival submissions and perused and carefully considered material on record.

It is seen from record that Ld.TPO included this company on the basis of statement made by company in its reply to notice under section 133(6) of the Act.

It is observed that there is no segmental information in respect of this company in annual report. We are unable to understand how segmentation was done by Ld.TPO and reconciliation of annual report. In such a situation we are of the opinion that Flextronics Software Solutions Ltd (seg) cannot not be considered as a proper comparable.

We therefore direct Ld.TPO to exclude this company from final list.

8.2.8 Infosys Ltd:

It has been submitted that Infosys Ltd., was selected as comparable by Ld.TPO in assessee's own case for assessment year 2008-09. However, Co-ordinate Benches of this Tribunal has directed exclusion of the same on the ground that it is functionally different with that of assessee. It has also been observed that this company was owning brand and having substantial intangible assets which cannot be held to be suitable comparable for assessee who was only providing contract software development services and IT staffing services. It has been submitted that functions of assessee, assets and risk profile has not undergone any change for the year under consideration. Ld.Counsel has also submitted that this company is not functionally comparable to assessee inasmuch as, it is also engaged in software development services and generate substantial revenue from the sale of its own products. Ld. counsel placed reliance upon the decision of CIT v. Agnity India Technologies (P.) Ltd. [2013] 36 taxmann.com 289/219 Taxman 26 (Delhi), wherein this Tribunal vide order dated 10/07/11 upheld exclusion of this company from list of comparables, after taking into consideration its operations as full-fledged risk taking enterprise in diversified field such as application design, development, re-engineering and maintenance integration etc cannot be equated with non-risk bearing companies. It has been submitted that this view of Agnity India technologies (P.) Ltd. (supra), has been upheld by Hon'ble Delhi High Court in ITA No. 3856/2010. Ld. CIT DR placed reliance upon the order of Ld. TPO.

22. We have considered the various distinguishing features submitted by Ld.Counsel on the basis of records placed before us.

Since all the distinguishing features exist even in the year under consideration, respectfully following the order of this Tribunal in assessee's own case, we direct this company to be excluded from the final list of comparables.

Accordingly this comparable is excluded from finalist.

8.2.10 KALS Information Systems Ltd

It has been contended that this company has revenues from both software development and software products. It is also pointed out that this company is engaged in providing training and that as per the annual repot, salary cost debited under software development expenditure was Rs45,93,351/- which is less than 25% of software services revenue and therefore fails in salary cost filter testapplied by Ld.TPO. Reliance has been placed on decision of this Tribunal for assessment year 2007-08, in case of Mphasis Ltd. v. Asstt. CIT [2017] 83 taxmann.com 362 (Benguluru - Trib.) wherein KALS as comparable was rejected being functionally different from software companies. The relevant extract are as follows:

"16. Another issue relating to selection of comparables by the TPO is regarding inclusion of Kals Information System Ltd. The assessee has objected to its inclusion

on the basis that functionally the company is not comparable. With reference to pages 185-186 of the Paper Book, it is explained that the said company is engaged in development of software products and services and is not comparable to software development services provided by the assessee. The appellant has submitted an extract on pages 185-186 of the Paper Book from the website of the company to establish that it is engaged in providing of I T enabled services and that the said company is into development of software products, etc. All these aspects have not been factually rebutted and, in our view, the said concern is liable to be excluded from the final set of comparables, and thus on this aspect, assessee succeeds.

Based on all the above, it was submitted on behalf of the assessee that KALS Information Systems Limited should be rejected as a comparable."

Ld.DR, on the other hand, relied on order of Ld.TPO.

26. We have considered submissions advanced by both sides and perused records placed before us.

We find that Ld.TPO concluded on basis of information obtained by issue of notice u/s.133(6) of the Act. This information which was not available in public domain could not have been used by Ld.TPO, when the same is contrary to annual report of this company as highlighted by Ld.AR. We also find that in the decision referred to by Ld.AR, of this Tribunal held that this company was developing software products and not purely or mainly software development service provider.

We therefore accept the plea of the Assessee that this company is not comparable.

8.2.13 <u>Persistent systems Ltd.</u>

Ld. Counsel submitted that this comparable has been included by Ld.TPO, however in assessee's own case for assessment year 2008- 09 this Tribunal in ITA No.5401/Del/2012 directed exclusion of the same on the ground that it is functionally different with that of assessee. Ld.Counsel submitted that there is lack of segmental accounting in the financials of this company. He also submitted that there are no bifurcations between the services rendered by this company. This Tribunal while considering this comparable for assessment year 2008-09 (supra) has observed that during the relevant assessment year company developed its own software products, and its revenue included licensing of software products. Ld.CIT, DR submitted that this company is into software services and products. And segmental accounting of software services and products are available for the year under consideration. We have perused the submissions on the basis of the records. It is observed that assessee has developed software during the year, and has earned royalties from sale of products. Assessee has earned revenues from Licensing of products. It is also observed from the notes to the accounts of this company that the segment information has been provided on consolidated financial statements. It is also observed that assessee owns the software developed by it on which depreciation is claimed. Thus this company has been characterized itself as engaged in providing outsourced product development services to independent software vendors and enterprises. It has been characterised to having earned significant portion of its revenues from export of software services and products. This function, the assets owned by this company and the risk assumed are not comparable with that of the present assessee and hence has to be excluded from the final list of comparables.

Accordingly, this comparable is directed to be excluded from finalist.

8.2.14 <u>R Systems International Ltd.</u>

Ld.Counsel submitted that this Tribunal while deciding the case of Hewlett-Packard (India) Globalsoft (P.) Ltd. (supra) held this comparable to be excluded since this

company has a different year ending. Assessee has submitted this comparable to be into IT related and BPO services. However on perusal of annual report placed at page 831-994 of paper book volume- 2, we observe that this comparable has income from software development and customization services and to a lesser extent from BPO services. It has been submitted that this comparable derives its revenue from 2 segments and has provided segmental information at page 888 of paper book. Under such circumstances, merely because comparable has a different year ending, cannot lead to the conclusion, of it being non-comparable with that of assessee. In the event quarterly results are available and the same can be extrapolated, this comparable should be considered.

We therefore, set aside R Systems International Ltd., which is functionally similar, to Ld. AO/TPO to consider the quarterly report and extrapolate the same for purposes of comparing its margin with assessee.

Accordingly, we set aside this comparable to Ld.TPO.

8.2.15 Wipro Ltd (Seg)

This Comparable has been included by Ld.TPO.

This is TPO's comparable in which segmental details has been obtained u/s. 133(6) of the Act. However, assessee has sought its exclusion on grounds of significantly higher turnover, abnormal margins, presence of intellectual property, diversified business, brand value and turnover. He placed reliance upon the decision of ICC India (P.) Ltd., v. ACIT (supra)..

On the contrary, Ld.DR submitted that there is no related party transaction during the year under consideration.

We have heard rival submissions of both sides in the light of records placed before us. It is observed that Co-ordinate Bench of the Delhi Tribunal in ICC India (P.) Ltd. (supra) has excluded this comparable by placing reliance upon Calibrated Healthcare Systems India (P.) Ltd. v. Asstt. CIT [2015] 54 taxmann.com 53. It is observed that in this decision this tribunal has examined comparability of WIPRO and ordered its exclusion on the ground that this is a giant entity with marked differences as regards risk profile, nature of services, ownership of IP rights, expenditure on R&D, etc. So, following the decision rendered by co-ordinate bench as well as the fact that the assessee company is a captive service provider taking minimum risk having no intangibles cannot be compared with WIPRO which is having diversified business, ownership of significant intangibles and huge expenditure on R&D etc.

We thus, direct Ld.TPO to exclude this company from final list of comparables.

We also mention that not considering of other comparables alleged by assessee does not ipso facto lead to upholding their inclusion, as with exclusion of comparables considered herein above, assessee falls into +/- 5% range. However, we grant liberty to assesse to allege other comparables, not considered by us in an appropriate instance.

Tata Elxsi & Bodhtree Consulting Ltd.

This *Tribunal* in the case of *Infinera India (P.) Ltd. v. ITO* reported in *(2016) 72 taxmann.com 68* has considered these comparables under similar FAR like that of present assessee for assessment year AY 2009-10. In the aforesaid decision the issue raised was

against including these companies as comparable companies. The plea of the Assessee was that the aforesaid five companies are not functionally comparable with the Assessee who was engaged in the business of providing SWD services to AE. It is also not in dispute before us that the functional profile of the Assessee in this appeal and the Assessee in the decision rendered in the case of *Infinera India (P.) Ltd. (supra)* are identical.

In the case of *Infinera India (P.) Ltd. (supra)* this *Tribunal* held these companies are not functionally comparable with a company rendering captive SWD services.

The Ld.DR could not point out any difference in facts. Hence, we hold these companies be excluded from the list of comparable companies as functionally not comparable with the Assessee company. The Ld.DR could not point out any difference in facts.

We therefore hold these companies to be excluded from the list of comparable companies as functionally not comparable with the assessee.

Bodhtree Consulting Ltd.

We find that exclusion of aforesaid companies was sought by the assessee in the case of *John Deere India Pvt. Ltd. Vs. ACIT in ITA No. 2236/PN/2012 decided on 18-11-2015 for assessment year 2008-09*. The *Tribunal* after considering the submissions of assessee and various decisions held that these companies are not good comparables and directed to exclude the same from the list of comparable entities. The findings of *Tribunal* in respect of aforesaid company is as under:

"20.1 Bodhtree Consulting Ltd. :

The assessee had initially selected Bodhtree Consulting Ltd. in its list of comparable. Subsequently, the same was taken out from the list of comparable as the said company is not exclusively engaged in software development services. The TPO again included the company in the list of comparable entity. The Ld. Counsel in support of his submissions that, Bodhtree Consulting Ltd. is not a good comparable placed reliance on the decision in the case of Barclays Technology Centre India (P) Ltd. Vs. ACIT (supra). The Co-ordinate Bench of the Tribunal in the case of Barclays Technology Centre India (P) Ltd. Vs. ACIT (supra) rejected Bodhtree Consulting Ltd. as comparable by placing reliance on the decision of Bangalore Bench of the Tribunal in the case of M/s. Mindteck (India) Ltd. in I.T.(TP).A.No.70/Bang/2014 decided on 21-08-2014 in the case of NetHawk Networks India Pvt. Ltd. in ITA No. 7633/M/2012 decided on 06-11-2013 for the assessment year 2008-09. The relevant extract of the order of Tribunal is as under: "20. The next point raised by the assessee is for exclusion of Bodhtree Consulting Ltd., from the final set of comparables. The main plea of the assessee is that the said concern is engaged in development and sale of software products and therefore it is not functionally comparable to the assessee. It is also pointed out that the said concern is engaged in product engineering and content engineering services which are in the nature of ITES services, and are not comparable with the assessee's activities. At the time of hearing, it was also pointed out that the said concern operates under a different pricing model, i.e. fixed price

project method, whereby revenues from software development is recognized based on software developed and billed to the clients. It has been explained that in such a situation, expenditure for developing software would be billed in an earlier year but the income would be recognized in a subsequent year. This business model results in fluctuation in margins over the years……..”

The Ld.AR submitted that *Hon’ble Pune Bench of the Tribunal* in the case of *QLogic (India) Private Limited vs. DCIT (ITA No.227/PN/2014) for assessment year 2009-10 dated 21.10.2014* excluded the said concern from the list of comparables in a similar situation by following the decision of the *Coordinate Bench of the Tribunal in the case of M/s. Mindteck (India) Ltd., vide I.T.(TP).A.No.70/Bang/2014 dated 21-08-2014.* Further it is submitted that decision of *Hon’ble Mumbai Bench of the Tribunal in NetHawk Networks India Pvt. Ltd. vide ITA No.7633/M/2012 dated 06-11-2013 for assessment year 2008-09* also been relied upon the above decisions for excluding the said concern from the final set of comparables.

On the other hand the Ld.DR defended inclusion of Bodhtree Consulting Ltd.

We have Perused the submissions advanced by both sides in light of records placed before us. The plea of the assessee is that the said concern is engaged in the sale of software products, apart from considering software services, and that no segmental data is available in this context; thus, it is functionally not comparable with the assessee’s activities. In this regard, we have perused the discussion made by our *Coordinate Bench in the case of NetHawk*

Networks India Pvt. Ltd. (supra) wherein the said concern has been found to be not exclusively engaged in rendering software development services. The relevant discussion in the case of *NetHawk Networks India Pvt. Ltd. (supra)* is as under :

There is no material placed before us which would require us to deviate from the above view. Thus, in view of the detailed discussion in the aforesaid order, we are of the view that Bodhtree Consulting Ltd. is not functionally comparable to the services rendered by the assessee.

Accordingly, Bodhtree Consulting Ltd. has to be excluded from the final set of comparables.

Thirdware Solutions Ltd.

This company was proposed for inclusion in the list of comparables by the Ld.TPO. Before the Ld.TPO, the assessee objected to its inclusion due its high turnover. Before us, the assessee objected to the inclusion of this company as a comparable for the reason that apart from software development services, it is in the business of product development and trading in software and giving licenses for use of software.

In this regard, the Ld.AR submitted that :-

(i) This company is engaged in product development and earns revenue from sale of licences and subscription. It has been pointed out from the Annual Report that the company has not provided any separate segmental profit and loss account for software development services and product development services.

(ii) In the case of *E-Gain communications Pvt. Ltd.* reported in *2008-TII-04-ITAT-PUNE-TP*, *Hon'ble Pune Tribunal* directed that this company be excluded for software service providers, as its

income includes income from sale of licences which has increased the margins of the company.

The Ld.AR prayed that in the light of the above facts and in view of the aforecited decision of the *Tribunal (supra)*, this company ought to be omitted from the list of comparables.

Per contra, the Ld.DR supported the view of the Ld.TPO in including this company in the list of comparables.

We have heard the rival submissions and perused and carefully considered the material on record.

It is seen from the material on record that the company is engaged in product development and earns revenue from sale of licenses and subscription. However, the segmental profit and loss accounts for software development services and product development are not given separately. Further, as pointed out by the Ld.AR, *Hon'ble Pune Bench of the Tribunal* in the case of *E-Gain Communications Pvt. Ltd. (supra)* directed that since the income of this company includes income from sale of licenses, it ought to be rejected as a comparable for software development services. In the case on hand, the assessee is rendering software development services.

We therefore direct this comparable to be excluded from the list of comparables.

Accordingly, Ground No.1.2 -1.2.16 along with Additional Ground no.1.2.17 stands allowed as indicated herein above.

Additional Ground No.1.2.18:

This ground has been raised seeking the grant of working Capital Adjustment.

We direct the LD.AO/TPO to grant WCA to even out the differences between the assessee and comparables is any as per law.

Accordingly this additional ground raised by assessee stands allowed.

Ground No.2.1 to 2.7: Both sides submitted that identical issue has been considered by Co-ordinate Bench of this *Tribunal* in assessee's own case for *Schneider Electric IT Business for assessment year 2009-10 reported in (2019) 106 taxmann.com 70*, wherein this issue has been set aside to Ld.TPO. It has been submitted that the same view has been followed in assessee's own case for AY 2007-08. For sake of convenience the relevant para from AY2007-08 is reproduced as under:

> *35. We have perused the order passed by this Tribunal in assessee's own case for assessment year 2009-10 (supra) and observed that the issue has been decided by observing as under:*
>
> > *RESEARCH AND DEVELOPMENT SERVICES SEGMENT:*
> > *14. As far as determination of ALP in this segment is concerned, the disputes raised by the Assessee are that the nature of services rendered by the Assessee to its AE was SWD services and it is not correct to characterize the same as R& D Services. Though this was the basis on which the TP study was undertaken by the Assessee, the Assessee submits that there is no estoppels in the matter of determination of ALP. The learned counsel in this regard has also pointed out that the TPO in AY 10-11 & 2011-12 accepted the claim of the Assessee in this regard and the relevant order's of TPO was also placed before us. The other grievance projected by the Assessee is that even assuming that the Assessee is to be regarded as rendering R & D services to its AE, the comparable companies chosen by the TPO and retained by the DRP are not comparable functionally and otherwise. The other grievance projected by the Assessee is regarding not granting working capital adjustment to the profit margins of comparable companies and the profit margins of the Assessee before comparing the profit margins with comparable companies to arrive at ALP.*
> > *15. The learned DR on the other hand while pointing out that the Assessee in his TP Study has chosen to characterize the transaction with AE as R & D Services cannot now be permitted to say that the nature of services is akin to SWD services. In this regard he also drew our attention to the Agreement between the Assessee and its AE under which the services in question were rendered by drawing our attention to Page 4997 of the Assessee's paper book.*

> *16. We have heard the rival contentions and the nature of service as set out in the note filed as part of the written submission before us. We are not reproducing the note filed by the parties before us and the contentions put forth therein because it requires examination by the AO/TPO. We are of the view that in the light of the TPO's acceptance in AY 20010-11 & 2011-12 that the nature of services rendered was akin to SWD services, the entire comparability criteria will change and the comparable companies already retained in the SWD segment will hold good for this segment also. We therefore feel that it would be just and appropriate to remand for fresh consideration by the AO/TPO of the nature of services rendered by the Assessee in this segment. This will depend upon the terms of the Agreement between the Assessee and AE for rendering services which are in dispute. The TPO will decide on the character of services rendered by the Assessee whether it is R & D or SWD, after affording opportunity of being heard to the Assessee and after considering all relevant factors. If the TPO comes to the conclusion that the nature of services rendered is SWD services, then the comparable companies chosen in the SWD services segment, which we have already decided in the earlier paragraphs, would be applicable. If he comes to the conclusion that the services rendered were in the nature of R & D and not SWD services, then the issue with regard to comparability of companies already chosen by the TPO/DRP on the basis of assumption that the Assessee is rendering R & D services and working adjustment to be made to the profit margin of comparable companies chosen on that basis are left open for consideration de novo by the TPO in the set aside proceedings.*

Respectfully following the same, we direct Ld.TPO to compute ALP as directed hereinabove.

Accordingly these grounds raised by assessee stands allowed for statistical purposes.

Ground No.3.1- 3.5 is in respect of the treatment of royalty paid by assessee to its AE by the authorities below. Both sides submit submitted that this issue has been considered by coordinate bench of this tribunal in assessee's own case for AY 2006-07 & AY:2007-08. We refer to the decision of this *Tribunal* in assessee's case reported in *(2020)113 taxman.com 215 for assessment year 2007-08*, where this issue has been considered as under:

> ***10.1*** *The contentions raised by assessee is that assessee in its manufacturing activity uses various marketing intangibles, technology intangibles, process manuals and standards, quality standards etc which is owned by its AE-UK. It has been submitted that assessee also has access to subsequent product improvements and development*

through the licensing agreement which is significant benefit received by assessee which enables assessee to update the technological development in the market. He submitted that the license agreement entered into by assessee with its AE for use of these technologies in the manufacturing of products also grants assessee license to sell such manufactured products in India in domestic market. Ld.AR further submitted that on such sale in the domestic market, assessee is to pay 4.5% of the net revenues earned as per the terms and conditions of the exclusive license agreement.

10.2 *He thus submitted that assessee while benchmarking the payment of royalty used CUP as most appropriate method. Referring to page 59 of TP documentation filed before us he demonstrated most appropriate method adopted by assessee. Ld.AR then pointed out that in TP order Ld. TPO wrongly held that assessee applied TNMM as most appropriate method for benchmarking the transaction which is evident from page 9 of TP order. It has been submitted that Ld.TPO while concluding his remark on this issue proceeded on the footing that TNMM has been used as the most appropriate method.*

10.3 *Before DRP, it has been acknowledged that assessee has used CUP as the most appropriate method to determined arm's length rate of royalties paid to AE.*

10.4 *Ld.AR submitted that, both authorities below proceeded on the footing that, no evidence has been provided by assessee to prove any tangible benefit derived from being the royalty for the so- called superior technology.*

10.5 *Referring to pages of small paper book filed by Ld.AR submitted as additional evidences at the time of haring, which includes documents to establishes assessee as a licensed manufacturer, that products manufactured by assessee cannot be carried out without technological and R & D assistance from its AE, details establishing actual receipt of technical knowhow from its AE against which royalty is paid, details to prove that IPRs and know-how received from AE are confidential property of AE being guidelines, directions, screenshots etc, that helps assessee to manufacture the products.*

It has been submitted that these documents were not placed before the authorities below and therefore requires consideration.

10.6 *Ld.CIT DR supported Ld.AR, that based upon these documents, the issue needs to be reconsidered for establishing actual nature of payments made by assessee.*

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

It is observed that assessee has placed substantial evidence which was not before the authorities below. We are therefore inclined to set aside this issue back to Ld.TPO/AO, for determination of this issue in the light of these documents vis-a-vis the agreement entered into by assessee with its AE under which the royalty has been paid. It has been observed that for assessment year 2006-07 in assessee's own case in ITA No. 1415/be a NG/2010 vide order dated 07/06/19, the issue has

been set aside on the basis of additional evidence filed by assessee for verification of the same. Respectfully following the same we are also inclined to set aside this issue back to Ld. TPO to verify the issue on basis of documents filed by assessee and to establish true nature of transaction regarding payment of royalty by assessee to its AE. Ld.TPO is directed to verify details and if necessary called for any further documents in order to establish the true nature of the transaction regarding the payment of royalties by assessee to its AE and consider the claim of assessee as per law.

Respectfully following the above we direct the Ld.AO/TPO to verify details and if necessary called for any further documents in order to establish the true nature of the transaction regarding the payment of royalties by assessee to its AE and consider the claim of assessee as per law.

Accordingly these grounds raised by assessee stands allowed for statistical purposes.

Ground no.3.1 to 3.5.

This ground has been raised by assessee against disallowance of expenditure towards royalty under section 40(a) which has already been disallowed under section 92CA of the Act.

It has been submitted that Ld.TPO made adjustment towards royalty under section 92CA of the Act holding that entire expenditure is not at arms length. Ld.AR submitted that assessee on its own disallowed the same under section 40(a)(i) for non-deduction of TDS while determining total taxable income. As we have already set aside the issue of royalty back to Ld.TPO for verification, this issue becomes academic in nature at this moment. Ld.AO is directed to verify submission in respect of *suo-moto* disallowance made by assessee under section 40(a)(i) and to consider the claim as per law.

Accordingly, this ground raised by assessee stands allowed for statistical purposes.

Ground no.4.1 to 4.5:

The issue raised by assessee in this ground is on interest imputed by the Ld.TPO on delayed receivables.

The Ld.AR submitted that interest on receivables outstanding as on 31/03 for a period of more than 6 months was imputed by the Ld.TPO in relation to transaction with AE. Ld. AO/TPO characterised the outstanding receivables to be loan transaction on which notional interest to the extent of Rs.24,30,00,000/-was charged.

From TP study, it is observed that payments to assessee are not contingent upon payment received by AEs from their respective customers. Further Ld.AR submitted that working capital adjustment undertaken by assessee includes the adjustment regarding the receivables and thus receivables arising out of such transaction have already been accounted for. Alternatively, he submitted that working capital subsumes sundry creditors and therefore separate addition is not called for.

Ld.TPO computed interest on outstanding receivables at the rate equal to 10% on the receivables that exceeded 6 months. It has been argued by Ld.AR that authorities below disregarded business/commercial arrangement between the assessee and its AE's, by holding outstanding receivables to be an independent international transaction.

The Ld.AR placed reliance on decision of *Delhi Tribunal in Kusum Healthcare Pvt.Ltd vs. ACIT* reported in *(2015) 62 Taxmann.com 79*, deleted addition by considering the above principle, and

subsequently *Hon'ble Delhi High Court in Pr. CIT vs. Kusum Health Care Pvt. Ltd.,* reported in *(2017) 398 ITR 66 (Del)*, held that no interest could have been charged as it cannot be considered as international transaction. He also placed reliance upon decision of *Delhi Tribunal* in case of *Bechtel India vs DCIT* reported in *(2016) 66 taxman.com 6* which subsequently upheld by *Hon'able Delhi High Court* vide *order dated 21/07/16 in ITA No. 379/2016,* also upheld by *Hon'ble Supreme Court vide order dated 21/07/17, in CC No. 4956/2017.*

It has been submitted by Ld.AR that outstanding receivables are closely linked to main transaction and so the same cannot be considered as separate international transaction. He also submitted that into company agreements provides for extending credit period with mutual consent and it does not provide any interest clause in case of delay. He also argued that the working capital adjustment takes into account the factors related to delayed receivables and no separate adjustment is required in such circumstances.

On the contrary Ld.CIT.DR submitted that interest on receivables is an international transaction and Ld.TPO rightly determined its ALP. In support of her contentions, she placed reliance on decision of *Hon'ble Delhi Tribunal* order in *Ameriprise India Pvt. Ltd. vs. ACIT* in *2015- TII-347-ITAT-DEL-TP,* wherein it is held that, interest on receivables is an international transaction and the transfer pricing adjustment is warranted. He stated that Finance Act, 2012 inserted Explanation to Section 92B, with retrospective effect from 1.4.2002 and sub-clause (c) of clause (i) of this Explanation provides that:

(i) the expression "international transaction" shall include-- ..... (c) capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;....' .

Ld.CIT DR submitted that expression 'debt arising during the course of business' refers to trading debt arising from sale of goods or services rendered in course of carrying on business. Once any debt arising during course of business is an international transaction, he submitted that any delay in realization of same needs to be considered within transfer pricing adjustment, on account of interest income short charged or uncharged. It was argued that insertion of Explanation with retrospective effect covers assessment year under consideration and hence under/non- payment of interest by AEs on debt arising during course of business becomes international transactions, calling for computing its ALP. He referred to decision of *Delhi Tribunal in Ameriprise (supra)*, in which this issue has been discussed at length and eventually interest on trade receivables has been held to be an international transaction. Referring to discussion in said order, it was stated that *Hon'ble Delhi Bench* in this case noted a decision of the *Hon'ble Bombay High Court* in the case of *CIT vs. Patni Computer Systems Ltd., (2013) 215 Taxmann 108 (Bom.)*, dealt with question of law:

(c) `Whether on the facts and circumstances of the case and in law, the Tribunal did not err in holding that the loss suffered by the assessee by allowing excess period of credit to the associated enterprises without charging an interest during such credit period would not amount to international

transaction whereas section 92B(1) of the Income-tax Act, 1961 refers to any other transaction having a bearing on the profits, income, losses or assets of such enterprises?'

The Ld.AR submitted that, while answering above question, *Hon'ble Bombay High Court* referred to amendment to section 92B by Finance Act, 2012 with retrospective effect from 1.4.2002. Setting aside view taken by *Tribunal, Hon'ble Bombay High Court* restored the issue to file of Tribunal for fresh decision in light of legislative amendment. It was thus argued that non/under-charging of interest on excess period of credit allowed to AEs for realization of invoices, amounts to an international transaction and ALP of such international transaction has to be determined by Ld.TPO. In so far as charging of rate of interest is concerned, he relied on decision of the *Hon'ble Delhi High Court* in *CIT vs. Cotton Naturals (I) Pvt. Ltd (2015) 276 CTR 445 (Del)* holding that currency in which such amount is to be re-paid, determines rate of interest. He, therefore, concluded by summing up that interest on outstanding trade receivables is an international transaction and its ALP has been correctly determined.

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

This Bench referred to decision of *Special Bench* of *Kolkotta Tribunal* in case of in case of *Instrumentation Corpn. Ltd. v. Asstt. DIT in ITA No. 1548 and 1549 (Kol.) of 2009, dated 15- 7-2016,* held that outstanding sum of invoices is akin to loan advanced by assessee to foreign AE., hence it is an international transaction as per explanation to section 92 B of the Act. We also perused decision relied upon by Ld.AR. In our considered opinion, these

are factually distinguishable and thus, we reject argument advanced by Ld.AR.

Alternatively, it has been argued that working capital adjustment subsumes sundry creditors. In such situation computing interest on outstanding receivables and loan and advances to international transaction would amount to double taxation. *Hon'ble Delhi Tribunal* in case of *Orange Business Services India Solutions Pvt. Ltd. vs. DCIT in ITA No. 6570/Del/2016 vide its order dated 15.2.2018* has observed that:

> *"There may be a delay in collection of monies for supplies made, even beyond the agreed limit, due to a variety of factors which would have to be investigated on a case to case basis. Importantly, the impact this would have on the working capital of the assessee would have to be studied. It went on to hold that, there has to be a proper inquiry by the TPO by analysing the statistics over a period of time to discern a pattern which would indicate that vis-à-vis the receivables for the supplies made to an AE, the arrangement reflected an international transaction intended to benefit the AE in some way. Similar matter once again came up for consideration before the Hon'ble Delhi High Court in Avenue Asia Advisors Pvt. Ltd. vs. DCIT (2017) 398 ITR 120 (Del). Following the earlier decision in Kusum Healthcare (supra), it was observed that there are several factors which need to be considered before holding that every receivable is an international transaction and it requires an assessment on the working capital of the assessee. Applying the decision in Kusum Health Care (supra), the Hon'ble High Court directed the TPO to study the impact of the receivables appearing in the accounts of the assessee; looking into the various factors as to the reasons why the same are shown as receivables and also as to whether the said transactions can be characterized as international transactions."*

In view of the above, we deem it appropriate to set aside the impugned order on this issue and remit the matter to the file of the Ld.AO/TPO for deciding it in conformity with the above referred judgment. Needless to say, the assessee will be allowed a reasonable opportunity of being heard in such fresh proceedings.

Accordingly these ground raised by assessee stands allowed for statistical purposes.

Ground no.6:

This issue has been raised by assessee against the disallowance made by Ld. AO of expenses incurred towards donation amounting Rs.18,52,713/-.

It has been submitted that assessee may donation to KIADB which was for Jigani welfare activities, where all manufacturing units of the company was situated. Assessee had two manufacturing units which claimed deduction under section 10A. It was submitted that if any disallowance was to be made it should have been made in respect of units as per the segmental financial statement filed by assessee. Ld.AR placed reliance upon decision of Hon'ble Bombay High Court in case of *CIT* v. *Gem Plus Jewellery IndiaLtd.* reported in *(2010) 194 Taxman 192,* where it was held that exemption under section 10A had to be granted on enhanced income. The alternative plea thus raised by assessee was that consequential benefit under section 10A should be allowed if such disallowance is to be made.

Ld. DR submitted that the issue requires verification by Ld.AO.

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

It is observed that Ld.AO and DRP upheld disallowance for want of evidence.

Assessee is directed to file all requisite details and Ld.AO is directed to verify the same and consider the claim as per law.

Accordingly this ground raised by assessee stands allowed for statistical purposes.

Ground No.7

Both sides submit submitted that this issue has been considered by coordinate bench of this *Tribunal* in assessee's own case for AY 2009-10. We refer to the decision of this *Tribunal* in assessee's case reported in *(2019)106 taxman.com 70* for assessment year 2009-10, where this issue has been considered as under:

> ***"80.*** *As far as deduction on account of provision for warrant expenses of Rs.15,97,71,045/- is concerned, we have heard the rival submissions. The conditions for allowing provision on account of provision for warranty expenses has been laid down by the Hon'ble Supreme Court in the case of Rotork Controls India (P.) Ltd. v. CIT [2009] 180 Taxman 422/314 ITR 62 wherein the Honorable Apex Court has stated that provision for warranty shall be allowed if it is made on scientific basis. The Assessee has filed a chart explaining as to how the Principles laid down by the Hon'ble Supreme Court in the case of Rotork Controls (supra) has been satisfied in its case.*

Principles laid down for provision for warranty to be treated scientific	*Applicability to the Assessee*
1. Present obligation out of obligating events which involves outflow of resources	*There is present obligation on the Company to meet cost for warranty in event of defects in products which would involve outflow of resources*
2. A reliable estimate can be made	*Repair cost and MLO cost incurred is multiplied by actual FFR rate and number of products sold to compute provision.* *Thus, estimate made by Company can be considered reliable*
3. Warranty cost was an integral part of that sale price	*Warranty provided for domestic sales at time of sale.* *Thus, warranty cost is an integral part of sales*
4. A historical trend used as a basis for creation of provision	*Provision created is based on the field failure rate of the products in past. Thus, a historical trend of actual failure of products has been used as a basis for creating the provision*
5. Reversal of unutilized provisions	*In case of Company the entire provision is reversed in next year and actual expense is booked in profit and loss A/C. Thus, there is no question of unutilized provision*

> ***81.*** *The method of creation of provision for warranty by the Assessee is scientific. A perusal of the detailed workings for the provision for warranty were furnished before the learned AO vide submissions dated 4th March 2013 (page number 4154 to 4162 - file 18 of the paper book, relevant pages 4160-4164). The workings annexed to the*

said submission are available in Files 5 and 6 of the paper books with complete listing of the sales. Also, the same were even explained in detail in the submissions dated 13th December 2012 (Page no 685 to 688 File 3), where the accounting entries were also explained. The Assessee submits that the determination of provision is an elaborate exercise covering all products sold and involves of around 35,000 line items. The AO held that provision for warranty made by the Assessee is not scientific because details of the utilization of the warranty have not been provided. In none of the years the unutilized warranty provision was reversed and credited into the P&L account; Utilization can be verified only if the name of the customer and the sales invoice are provided to verify the period of warranty and name of the customer against whom the warranty provision was utilized out of the existing provision, etc.

82. *These conclusions of the AO are unsustainable because the entire provision created by the Assessee is reversed in the next year and actual warranty expense incurred is charged to the Profit and Loss Account. Thus, in the case of the Assessee there is no requirement for maintaining the details of utilization as mentioned by the learned AO as there is no unutilized provision. The trend of provision for warranty i.e., the actual expense vis-à-vis the closing provision for warranty and also reversal of warranty have all been furnished by the Assessee before the AO. (Submission at page 4747 of File 20 of the paperbook (relevant pages 4786-4793). The Ledger extracts for the provision a/c for the year ended 31st March 2008 and 31st March 2009 were also made available at pages 4793-4794. The utilization in the case of Assessee is in the form of evidence for actual expense incurred, which was furnished before the learned AO vide submissions dated 4th March 2013 (page number 4154 to 4162 - file 18 of the paper book). The method of creation of provision for warranty is a robust method of determination of provision for warranty. The same is as follows:*

(i) Provisions for the previous year is reversed completely at the beginning of the current year.

(ii) At the year end, the Company reviews the amount required to be provided as warranty based on the warranty policy of the Company.

(iii) The sales register for the past 3 years are taken as basis for creation of the provisions for warranty.

(iv) The provision is created on the basis of Field Failure Rate (FFR) identified per product for the past one year (i.e. 2008 for 2009 expenses). Further adjustments are made to either increase or decrease this provision based on the assessment of risk exposure.

(v) The provision is created as under :

*FFR * Cost per product* Number of products sold.*
Cost refers to following:

- *Material, Labor and Overhead (MLO) cost for products fully replaced;*
- *Repairs and freight costs for the products repaired.*

83. *It is also clear that the methodology followed by the Assessee was held to be scientific for AY 2008-09. AO's order dated 6th July 2012 clearly states the method of creation of warranty is scientific- page 5 para 2.7 (Page of 4959- file 20):*
" On going through the assessee submissions, it is seen that assessee has created the provisions on a scientific basis based on empirical data, trends, projections, etc"

> ***84.*** *The method of providing and claim deduction on account of warranty expenses is the same in the present AY as it was in AY 2008-09. In the given facts and circumstances of the case, we are of the view that the deduction on account of provision for warranty expenses deserves to be allowed as claimed by the Assessee as the requirements for claiming deduction on account of provision for warranty liability has been satisfied. Gr.No.18 raised by the Assessee is accordingly allowed."*

It is submitted that for year under consideration method of computing the warranty claimed as deduction on account is the same in the present AY as it was in AY 2008-09. There is nothing distinguishing fact brought on record brought on record by the revenue. Respectfully following the above, we are of the view that provision for warranty expenses deserves to be allowed as claimed by the Assessee as the requirements for claiming deduction on account of provision for warranty liability has been satisfied.

Accordingly this ground raised by assessee stands allowed.

Ground No.8-9: Stock Obsolescence and reversal of provision:

The Ld.AR submitted that the provision for stock obsolescence is a part of closing stock valuation and there is no separate debit made in the P& L account.

The Ld.AO disallowed such provision for stock obsolescence on the ground that there is no such deduction available under the Income Tax Act, 1961.

It is submitted that section 145A of the Act provides that inventory is to be valued as per the accounting method regularly followed by the assessee. The Ld.AR submitted that the method of accounting regularly employed by the assessee is to value the inventory net of provision for stock obsolescence and this method is in accordance with the accounting standard 2-Valuation of inventory. It is thus submitted that the provision for stock

obsolescence is part of inventory valuation and not as a separate charge to the profit and loss account. He placed reliance on the following decisions.

- *CIT vs. IBM India Private Limited ITA No 445 of 2008 (Kar HC)*
- *CIT vs Tupperware India Pvt. Ltd (2015) 53 taxmann.com 232 (Delhi HC)*
- *CIT vs. Wolkem India Private Limited (315 ITR 211) (Raj HC)*
- *Commissioner of Income-tax vs. Carborandum Universal Ltd [1984] 16 Taxman 25 (Mads HC)*
- *Emersons Process Management India (P.) Ltd. v. Additional Commissioner of Income-tax (Mumbai ITAT) (47 SOT 157)*

On the contrary, the Ld.DR relied on the orders passed by the Ld.AO.

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

We find that this issue needs to be revisited by the Ld.AO in order to verify the details filed having regards to the principles laid down by *Hon'ble Karnataka High Court* in case of *CIT vs.IBM India Pvt.Ltd (supra), Hon'ble Delhi High Court in case of CIT vs.Tupperware India Pvt.Ltd(supra)* and *Hon'ble Madras High Court in case of CIT vs. Carborandum Universal Ltd(supra)* and to consider the claim of assessee in accordance with law.

Accordingly this ground raised by assessee stands allowed for statistical purposes.

Ground No.10: Disallowances of advances written off.

The Ld.AR submitted that the Ld.AO allowed the claim of advances written off where ever details were filed. In some of the cases, assessee filed details/evidences before the DRP. The DRP directed the Ld.AO to examine the evidences. It is submitted that the Ld.AO ignored the evidences and disallowed the entire claim of assessee.

At this position, the Ld.DR suggested that the issue may be remanded to the Ld.AO.

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

The assessee has filed a paperbook containing additional evidences which were also filed before the DRP. The Ld.AO failed to follow the directions of DRP and therefore, in the interest of justice we remit the issue back to the file of the Ld.AO.

The Ld.AO shall verify the details/evidences and consider the claim of assessee in accordance with law.

Accordingly this ground raised by assessee stands allowed for statistical purposes.

Ground No.11

These grounds has been raised by assessee, is in respect of exclusion of telecommunication expenses while computing deduction under section 10 A of the act upheld by Ld. CIT (A).

Ld.AR placed reliance upon the decision of *Hon'ble Karnataka High Court* in case of *CIT* v. *Tata Elxsi Ltd.* reported in *(2012) 17 taxmann.com 100* submitted that this issue stands covered in favour of assessee.

On the contrary, Ld.CIT.DR placed reliance upon the order passed by Ld.AO.

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

It is observed that, *Hon'ble Karnataka High Court* in case of *Tata Elxsi Ltd.* (*supra*) on identical issue held that telecommunication expenses is to be included while computing deduction under section 10A of the Act as it is directly linked with earning of

income. Ld.CIT.DR has not brought before us any contradictory/distinguishable facts in respect of present case before us.

Respectfully following *Hon'ble Karnataka High Court* in case of *Tata Elxsi Ltd.* (*supra*), we direct Ld.AO to include telecommunication expenses while computing exempt income u/s10A of the Act.

Accordingly the grounds raised by assessee stands allowed.

Ground No.12-13 are consequential in nature and therefore do not require any adjudication

Additional Ground vide application dated 21/08/2019:

Alternate claim of 10A deduction on unbilled revenue:

It is submitted that assessee during year accounted as export turnover being unbilled revenue, which was yet to be billed and also claimed deduction under section 10A.

The Ld.AR raised identical submission as raised for AY 2007-08 in assessee's own case. This *Tribunal* considered the issue as under:

> *It has been submitted that invoices were raised in the month of March 2008, and said amount has been realised by assessee during September 2008. The Ld. AO disallowed the claim of assessee by holding that assessee did not raise invoices within time stipulated under Master circular No. 6/2010-11 dated 01/07/10 issued by RBI. The view was held by DRP.*
>
> ***12.1** Ld.AR submits that assessee fulfilled requirement prescribed under RBI circular (supra). He submitted that assessee realised the sum within period of 6 months from the end of financial year or such further period as the competent authority May allow in this behalf. He submitted that 10A being a beneficial provision was introduced for purpose of increasing exports from India and to encourage establishment of export-oriented industrial undertaking in free trade zone*
>
> ***12.2** Ld.AR in support of his argument placed reliance upon decision of Mumbai Tribunal in case of Tech Mahindra R&D Services Ltd. v. Dy. CIT [IT Appeal No. 4462 (M) of 2016, dated 15-5-2018].*

12.3 *On the contrary Ld.DR submitted that, facts in case of assessee is distinguishable with that facts in case of Tech Mahindra R&D Services Ltd. (supra). It has been submitted that Tech Mahindra R&D Services Ltd. (supra) in turn relied upon decision of Madras Tribunal in case of iNautix Technologies India (P.) Ltd. v. Asstt. CIT [IT Appeal No. 541 (Mds.) of 2006, dated 17-1-2006]. It has been submitted that in present case, income has not accrued to assessee of which invoices has been raised in March 2008.*

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

Unbilled revenue means revenue that has been earned but not yet billed to customers as of the end of accounting year. It is very different from unearned revenue. When goods or services has been transferred to customers but customer payment is contingent based on a future event, this amount is generally referred to as an unbilled revenue. In our considered opinion export proceeds received on or brought into India in accordance with RBI guidelines satisfy requirements of section 10 A (3). Further

Section 10A (3) provides that competent authority being RBI can grant extension of time to receive unbilled amounts by assessee pertaining to a particular year.

40.1 Before us assessee has not been able to establish that RBI extended time period to receive income arising out of export of services declared during the year under consideration. In decisions relied upon by Ld.AR in case of Tech Mahindra R&D Services Ltd(supra), assessee therein received income within 6 months of invoice being raised and therefore this Tribunal held that revenue should be included in export turnover and also the total turnover. In the facts of present case, assessee raised invoice in March 2008 that is end of subsequent financial year, for which assessee do not have any permission from RBI regarding extension of time. We are therefore unable to concur with the argument advanced by Ld.AR.

Respectfully following the above this ground raised by assessee stands dismissed.

<u>Additional Ground No.14</u>: Educational Cess:

This issue urged by the assessee related to claim for deduction of Education Cess including secondary & higher education Cess on income tax as deduction while computing the total income.

We notice that identical issue has been dealt with by *Coordinate Bench* of this *Tribunal* in case of *M/s. Infinera India Pvt. Ltd.* in

IT(TP)A No. 2589/Bang/2019 by order dated 23.02.2022 as under:

> *10.1 We notice that the Kolkata Bench of Tribunal in the case of Kanoria Chemicals & Industries Ltd Vs. Addl. CIT (ITA No.2184/Ko1/2018 dated 26.10.2021) has held that the education cess is an additional surcharge levied on income tax and hence it partakes the character of income tax. Accordingly it held that the education cess is not allowable as deduction. The Tribunal also noted the decision rendered by Hon'ble Bombay High Court in the case of Sesagoa Ltd. 117 Taxmann.com 96 and by Hon'ble Rajasthan High Court in the case of Chambal Fertilisers& Chemicals Ltd. Vs. JCIT (ITA No.52/2018 dated 31.7.2018), wherein it was held that the education cess is allowable as deduction. However, the Tribunal observed that the decision rendered by Hon'ble Supreme Court in the case of CIT Vs. K. Srinivasan (1972) 83 ITR 346 was not brought to the notice of the above said Hon'ble High Courts. Accordingly, the Tribunal has expressed the view that the decision rendered by Hon'ble Supreme Court in the case of K. Srinivasan (supra) shall prevail on this issue and accordingly held that the education cess is not allowable as deduction.*
>
> *10.2 Following the above said decision of Kolkata bench of Tribunal in the case of Kanoria Chemicals & Industries Ltd (supra), we hold that payment of education cess including secondary and higher education cess is not allowable as deduction. Accordingly, we reject this ground of the assessee.*

In the result, appeal of the assessee stands partly allowed as indicated herein above.

Order pronounced in the open court on 28th February, 2022.

Sd/-	Sd/-
(CHANDRA POOJARI)	(BEENA PILLAI)
Accountant Member	Judicial Member

Bangalore,
Dated, the 28th February, 2022.
/MS /

Copy to:

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

By order

Assistant Registrar,
ITAT, Bangalore