

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

Before Shri George George K, JM & Ms.Padmavathy S, AM

IT(TP)A No.294/Bang/2021 : Asst.Year 2016-2017

M/s.Xchanging Solutions Limited Kalyani Tech Park Magnolia Building, Survey 1#, 6 & 24 ITPL Main Road KR Puram-Hobli Bangalore 560 066 PAN : AAFCS9303L	v.	The Assistant Commissioner of Income-tax, Circle 7(1)(1) Bangalore.
(Appellant)		(Respondent)

Appellant by : Sri.Padamchand Kincha, CA
Respondent by : Dr.Manjunath Karkaihalli, CIT-DR

Date of Hearing : 10.05.2022	Date of Pronouncement : 12.05.2022
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O R D E R

Per George George K, JM :

This appeal at the instance of the assessee is directed against final assessment order dated 30.04.2021 passed u/s 143(3) r.w.s. 144C(13) of the I.T.Act. The relevant assessment year is 2016-2017.

2. The brief facts of the case are as follows:

The assessee is a public limited company, engaged in providing software development services to its Associate Enterprises (AEs) as well as non-AEs. For the assessment year 2016-2017, the assessee filed return of income u/s 139(1) of the I.T.Act on 25.11.2016 declaring income of Rs.17,03,54,780. During the relevant financial year, the assessee had entered into international transaction of provision of software development services to AEs as well as

non-AEs. The assessment was selected for scrutiny and during the course of assessment proceedings, the matter was referred to the Transfer Pricing Officer (TPO) to determine Arm's Length Price (ALP) of the international transaction undertaken by the assessee with its AEs. The TPO passed the transfer pricing order dated 30.10.2019 determining the total TP adjustment of Rs.3,48,49,941 in respect of software development services transaction of the assessee and a sum of Rs.83,55,708 in respect of interest on delayed receipt of trade receivables from its AEs. Pursuant to the TPO's order, a draft assessment order dated 31.12.2019 was passed by the AO in which the aforesaid TP adjustment made by the TPO was incorporated. As regards corporate tax issue is concerned, the A.O. in draft assessment order proposed disallowance of Rs.50,20,109 by invoking the provisions of section 40(a)(i) of the I.T.Act.

3. Aggrieved, the assessee filed objections before the Dispute Resolution Panel (DRP). The DRP vide its directions dated 25.03.2021, partly allowed the objection raised by the assessee. Pursuant to the directions of the DRP, final assessment order was passed dated 30.04.2021 in which the TP adjustment was worked out to Rs.4,30,60,301 and adjustment pertaining to the Corporate Tax remained unchanged at Rs.50,20,109.

4. Aggrieved by the final assessment order, the assessee has filed this appeal before the Tribunal, raising following grounds:-

“Based on the facts and circumstances of the case and in law, Xchanging Solutions Limited (hereinafter referred to as “the Company” or “the Appellant”), respectfully craves leave to prefer an appeal against the order passed by the learned Additional / Joint / Deputy / Assistant Commissioner, Income-tax Officer, National e-Assessment Centre, Delhi [hereinafter referred to as the “learned AO”] dated 30 April 2021 under Section 143(3) read with Section 144C(13) and Section 144B of the Income-tax Act, 1961 (“the Act”) pursuant to the directions issued by the Dispute Resolution Panel (“DRP”) under Section 144C(5) the Act inter-alia on the following grounds which are without prejudice to each other:

On the facts and circumstances of the case and in law:

General grounds

1.The impugned order and directions of the Hon'ble DRP are based on incorrect appreciation of fact and wrong interpretation of law and therefore, are bad in law.

2.The learned DRPI AOI Transfer Pricing Officer (“TPO”) have erred in making adjustments /disallowances aggregating to INR 4,80,80,410 to the returned income and thereby has erred in law and on facts in assessing the total income of the Appellant at INR 21,84,35,190.

Transfer Pricing grounds

3.The learned DRP/AOITPO erred in making an addition of INR 3,47,04,593 to the total income of the Appellant on account of adjustment in the arm's length price (“ALP”) of the provision of software development services transaction entered by the Appellant with its Associated Enterprises (“AEs”).

4.The learned DRP/AO /TPO have erred in law and facts by not accepting the economic analysis undertaken by the Appellant in accordance with the provisions of the Act read with the Income-tax Rules, 1962 (“Rules”) and conducting a fresh economic analysis for the determination of the arm' length price in connection with the impugned international transaction and holding that the Appellant's international transaction is not at arm's length.

5. The learned DRP/AO/TPO erred by applying the following quantitative and qualitative filters:

at” The learned AO/TPO have erred, in law and in facts, by rejecting certain comparable companies having different accounting year / financial year (i.e., companies having accounting year other than March 31 or companies whose financial statements were for a period other than 12 months)

b)The learned AO/TPO have erred, in law and in facts, by using only the lower turnover filter of less than INR 1 crore as a comparability criterion and not applying a higher threshold limit for turnover filter.

6.The learned DRP/AO /TPO erred, in law and in facts, by exercising his powers under Section 133(6) of the Act to obtain information which was not available in public domain and relying on the same for comparability purposes.

7.Without prejudice to the above grounds, the learned DRP/AO/TPO have erred in law and in facts, by accepting/rejecting companies based on unreasonable comparability criteria:

a)The learned DRP/AO /TPO erred, in law and in facts, by accepting the following companies that cannot be considered as comparable to the Appellant in law and fact on one or more grounds:

- i. Larsen & Toubro Infotech Ltd.*
- ii. Infobeans Technologies Limited*
- iii. Persistent Systems Limited*
- iv. Nihilent Technologies private Limited*
- v. Inteq Software Private Limited*
- vi. Infosys Limited*
- vii. Thirdware Solution Limited*
- viii.Cybage Software Private Limited*
- ix. Aspire Systems (India) Private Limited*

b)The learned AO/ TPO / DRP erred, in law and in facts, in rejecting the following comparable companies selected by the Appellant in its TP documentation even though the companies are functionally comparable to the Appellant:

- i. Akshay Software Technologies Limited*
- ii. R Systems International Limited*
- iii. Mudunuru Limited*
- iv. Sasken Communication Technologies Limited*
- v. Maveric Systems Limited*
- vi. Infomile Technologies Limited*

c)The learned AO/ TPO / DRP erred, in law and in facts, in rejecting the following comparable companies selected by the Appellant as additional comparables even though the companies are functionally comparable to the Appellant:

- i. Evoke Technologies Limited*
- ii. Celstream Technologies Limited*
- iii. Isummation Technologies Limited*

8.The learned DRP/AO/TPO erred, in law and in facts, by incorrectly computing the operating margin of certain comparable companies considered in the TP order:

- i. Kals Information Systems Limited
- ii. CG Vak Software & Exports Limited
- iii. Infobeans Technologies Limited
- iv. Infosys Limited
- v. Thirdware Solution Limited
- vi. Cybage Software Private Limited
- vii. Persistent Systems Limited
- viii. Aspire Systems (India) Limited
- ix. Nihilent Analytics Limited
- x. Larsen & Toubro Infotech Limited

9.The learned DRP/AO/TPO erred, in law and on facts, in recomputing the operating margin as earned and disclosed by the Appellant in its Transfer Pricing Study in respect of the provision of software development services to its AEs.

10.The learned AO / TPO /DRP have erred, in law and in facts, by not making suitable adjustment to account for differences in working capital position of the Appellant vis-a-vis the comparables.

11.The learned DRP/AO /TPO erred, in law and in facts, by not making suitable adjustments on account of differences in the risk profile of the Appellant vis-a-vis the comparables, while conducting comparability analysis.

12.Without prejudice to the ground 5 above, the learned DRP/AO/TPO erred in law and in facts by not giving due consideration to the Assessee's request to consider the internal comparable data for the purpose of application of TNMM in order to determine the ALP of the international transaction entered into by the Assessee with its AEs.

13.The learned DRP/TPO/ AO have erred in not restricting the transfer pricing adjustment only to the value of the international transactions under consideration (i.e. revenue earned from provision of software development services to AEs outside India) and not to the entire operating revenue of the Assessee from domestic AEs as well as foreign AEs.

14.The learned DRP/AO/TPO have erred in law and facts by determining a transfer pricing adjustment on account of interest on outstanding receivables amounting to INR 83,55,708.

15.The learned DRP/AO/TPO have erred, in law and in facts, by not appreciating that the outstanding trade receivables from its AE's is arising from the provision of software development services transaction and is to be considered as closely linked to such transaction and should not be tested separately from arm's length perspective.

16.The learned DRP/AO /TPO have erred, in law and in facts, by re-characterizing the outstanding receivables as on 31 March 2016 as a separate loan transaction.

17.Without prejudice to our grounds above, the learned DRP/AO /TPO have erred, in law and in facts, by adopting the SBI short term deposit interest rate to compute the notional interest on outstanding receivable as on 31 March 2016.

18.Without prejudice to our grounds above, the learned DRP/AO/TPO have erred, in law and in facts, by not considering that working capital adjustment will appropriately take into account the delayed /outstanding receivable and separate TP adjustment thus will be unwarranted.

19.Without prejudice to our grounds above, the learned DRP/AO /TPO have erred, in law and in facts, by making a separate TP adjustment on account of interest on outstanding receivables rather than adjusting the operating margin earned in the software development service segment by the appellant, for testing the arm's length nature of the transaction.

Corporate Tax grounds

20.The learned DRP/AO has erred, in law and on facts, in disallowing the expenses amounting to INR 50,20,109 under Section 40(a)(i) of the Act, on payments made to Xchanging Global Insurance Solutions Ltd. ("XGISL"), UK towards reimbursement of purchase of software licenses.

21.The learned DRP/AO has erred, in law and on facts, in treating the payments towards the use of software licenses to be in the nature of software taxable as royalty under the provisions of Section 9(1)(vi) of the Act read with Article 13 of the India-UK Double Taxation Avoidance Agreement.

22.The learned DRP/AO has failed to appreciate that the payments are towards use of copyrighted article and not towards use of copyright per se. Thus, the lower authorities have erred in concluding that the payments are in the nature of royalty and are subject to deduction of tax at source.

23.The learned DRP/AO has erred, in law and on facts, in not considering the Hon'ble Supreme Court judgement dated 2 March 2021 passed in the case of Engineering Analysis Centre of Excellence (P.) Ltd. v. Commissioner of Income-tax [2021] 125 taxmann.com 42 (SC) wherein it has been held that payments towards use of copyrighted article are not taxable as royalty in India.

24. That on the facts and in the circumstances of the case and in law, the AO be directed to allow deduction for education cess (UEC") and higher and secondary education cess ("SHEC") paid on income-tax for computing the total income as per the provisions of the Act.

Other Grounds

25.The learned AO has erred, in law and on facts, in levying the interest of INR 1,33,536 under Section 234A of the Act without appreciating that the original return of income was filed by the Appellant within the due date as specified under Section 139(1) of the Act.

26.The learned AO has erred, in law and on facts, in levying the interest of INR 40,72,848 under Section 2348 of the Act.

27.The learned AO has erred, in law and on facts, in computing interest under Section 234C of the Act, on the assessed income at INR 3,65,641 as against Nil computed on the returned income by the Appellant while filing its return of income.

28.The learned AO has erred, in law and on facts, by not appreciating that interest under Section 234C of the Act is to be calculated on returned income and not on assessed income.

The Appellant submits that each of the above grounds is independent and without prejudice to one another.

The Appellant craves leave to add, alter, amend, vary, omit or substitute any of the aforesaid grounds of appeal at any time before or at the time of hearing of the appeal, so as to enable the Hon'ble Tribunal to decide on the appeal in accordance with the law."

5. Though the assessee has raised several grounds on TP adjustment and on Corporate Tax issues, broadly, the issues argued by the learned AR are as follows:-

- (i) TP adjustment on provision for software development services (adjustment of Rs.3,47,04,593)
- (ii) Interest on delayed receivables (adjustment amounting to Rs.83,55,708)
- (iii) Corporate Tax Issues – Disallowance of software

expenses due to non-deduction of TDS.

We shall adjudicate the above issues as under:

Provision for software development services (TP Adjustment of Rs.3,47,04,593)

6. The net margin on cost earned by the assessee as per TP study and as computed by the TPO in the TP order are as follows:-

Particulars	TPO order	TP Study
Operating income	42,16,84,581	43,07,89,324
Operating cost	36,33,67,177	36,19,57,633
Operating profit (Op.Income – Op.Cost)	5,83,17,404	6,88,31,691
Operating Net Margin (OP/OC)	16.04%	19.02%

6.1 The comparison of TP analysis undertaken by the assessee and the TPO are as under:-

Particulars	Appellant	TNMM
Methodology adopted	TNMM	TNMM
Profit Level Indicator (PLI)	OP/OC	OP/OC
Database used	PROWESS, CAPITALINE AND ACE-TP	PROWESS
Comparables selected	12	17

6.2 The assessee in the TP study, had adopted various filters and based on the search process, the assessee arrived at 12 comparables with a range of 8.11% to 12.35% and a median of 10.07%. Accordingly, the assessee in its TP study has sought to justify the ALP of the international transaction undertaken by the assessee with its AEs in respect of provision of software development services.

6.3 The TPO, however, rejected the TP study of the assessee. The TPO based on certain filters selected 17 comparable companies. The comparables selected by the TPO and the arms length margin are as follows:-

Sl. No.	Name of comparable company	Weighted average unadjusted margin (%)
1.	Kals Information Systems Pvt. Ltd.	8.60%
2.	E-Zest Solutions Limited	10.87%
3.	Rheal Software Pvt. Ltd.	14.50%
4.	Sybrant Technologies Pvt. Ltd.	14.74%
5.	Harbinger Systems Pvt. Ltd.	15.06%
6.	CG-VAK Software & Exports Ltd.	18.50%
7.	R S Software (India) Ltd.	20.87%
8.	Larsen & Toubro Infotech Ltd.	24.83%
9.	Orion India Systems Pvt. Ltd.	25.64%
10	Nihilient Ltd.	26.36%
11	Inteq Software Pvt. Ltd.	28.20%
12	Persistent Systems Ltd.	30.89%
13	Infobeans Technologies Ltd.	32.42%
14	Thirdware Solutions Ltd.	36.90%
15	Infosys Ltd.	38.61%
16	Aspire Systems (India) Pvt. Ltd.	39.28%
17	Cybage Software Pvt. Ltd.	66.45%
	35 th Percentile	18.50%
	Median	25.64%
	65 th Percentile	30.89%

6.4 The computation of ALP by the TPO and the adjustment made are as follows:-

Particulars	Amount (INR)
Arm's length median margin as per comparable set	25.64%
Operating Cost (OC)	36,33,67,177
Arm's Length Price (ALP) = 125.64% of OC	45,65,34,522
Price Received	42,16,84,581
Shortfall being adjustment u/s 92CA	3,48,49,941

6.5 Aggrieved, the assessee filed objections before the DRP. The DRP accepted the contentions of the assessee that Orion Systems India Private Limited is not comparable company and directed its exclusion along with exclusion of E-Zest Solutions Limited on the same ground. Further, the DRP also accepted the contention of the assessee that Sagarsoft India Limited should be included. On giving effect to the directions of the DRP, the TP adjustment in respect of software development services was reduced to Rs.3,47,04,593. The comparable that remained pursuant to the directions of the DRP are as follows:-

Sl. No.	Name of comparable company	Weighted average unadjusted margin (%)
1.	Sagarsoft India Limited	1.52%
2.	Kals Information Systems Pvt. Ltd.	8.60%
3.	Rheal Software Pvt. Ltd.	14.50%
4.	Sybrant Technologies Pvt. Ltd.	14.74%
5.	Harbinger Systems Pvt. Ltd.	15.06%
6.	CG-VAK Software & Exports Ltd.	18.50%
7.	R S Software (India) Ltd.	20.87%
8.	Larsen & Toubro Infotech Ltd.	24.83%
9.	Orion India Systems Pvt. Ltd.	25.64%
10.	Nihilient Ltd.	26.36%
11.	Inteq Software Pvt. Ltd.	28.20%
12.	Persistent Systems Ltd.	30.89%
13.	Infobeans Technologies Ltd.	32.42%
14.	Thirdware Solutions Ltd.	36.90%
15.	Infosys Ltd.	38.61%
16.	Aspire Systems (India) Pvt. Ltd.	39.28%
17.	Cybage Software Pvt. Ltd.	66.45%
	35 th Percentile	18.50%
	Median	25.60%
	65 th Percentile	30.87%

6.6 Aggrieved by the final assessment order, the assessee has filed appeal before the ITAT. The assessee has raised

several grounds with regard to the TP adjustment made on provision for software development services. However, the learned AR candidly admits that if seven comparables are excluded on the basis of turnover filters and margin for R S Software (India) Ltd. is only taken for assessment year 2016-2017, the other grounds / issues raised on TP adjustment may be left open. The list of seven comparable companies sought to be excluded for the reason that they are having turnover exceeding Rs.200 crore, are as follows:-

Sl. No.	Comparable	Turnover in crore
1.	Larsen & Toubro Infotech Limited	5,569.52
2.	Nihilient Technologies Limited	251.22
3.	Persistent Systems Limited	1,447.14
4.	Thirdware Solutions Limited	221.36
5.	Infosys Limited	53,983.00
6.	Aspire Systems (India) Pvt.Ltd.	230.81
7.	Cybage Software Private Limited	722.25

6.7 As regards R S Software (India) Limited is concerned, it was submitted that the assessee should not be considered as a comparable for assessment years 2015-2016 and 2014-2015 since the company's turnover for the said years exceeds Rs.200 crore. Accordingly, it was contended that the margins earned by the company for assessment years 2015-2016 and 2014-2015 should not be considered. It was stated that the operating margin of R S Software (India) Limited for A.Y.2016-2017 is -2.09%. In support of this contention, the learned AR relied on following ITAT orders of Bangalore Benches of the Tribunal:-

- (i) Aurigo Software Technologies Private Limited v. ITO Ward 1(1)(1), Bangalore IT (TP)A No.178/Bang/2021 (AY 2016-17) (order dated 03.02.2022)
- (ii) Barracuda Networks India Private Limited v. DCIT [IT(TP)A No.229/Bang/2021] AY 2016-17 (order dated 25.10.2021).

6.8 The learned Departmental Representative supported the orders of the TPO and the DRP.

6.9 We have heard rival submissions and perused the material on record. Admittedly, in the instant case, the assessee's turnover is only Rs.40.87 crore. The TPO / DRP had excluded companies having turnover of less than Rs.1 crore, however, the TPO / DRP has not put upper limit of the turnover for exclusion of companies having higher turnover. The Bangalore Bench of the Tribunal in Barracuda Networks India Private Limited (supra), on identical facts (the assessment year and the profile of the assessee are identical), had excluded Larsen & Toubro Infotech Limited, Nihilient Technologies Limited, Persistent Systems Limited, Thirdware Solutions Limited, Infosys Limited, Aspire Systems (India) Private Limited and Cybage Software Private Limited, since the turnover of the above companies had exceeded Rs.200 crore. The relevant ground, namely, ground 4 raised in the case of Barracuda Networks India Private Limited (supra), reads as follows:-

“Ground 4

The lower authorities erred in including the following companies, even though they fail the higher threshold limit of INR 200 crores for turnover filter:

(a) Infosys Ltd.

(b) Larsen & Toubro Infotech Ltd

(c) Persistent Systems Ltd

- (d) Aspire Systems (India) Pvt Ltd
- (e) Thirdware Solution Ltd.
- (f) Cybage Software Pvt Ltd.
- (g) Nihilent Ltd.
- (h) R S Software Ltd. (for FY 2013-14, FY 2014-15)

6.9.1 In deciding the above ground, the Tribunal in the case of Barracuda Networks India Private Limited (supra), considered various judicial pronouncements and held that companies whose turnover is exceeding Rs.200 crore has to be excluded. The relevant finding of the ITAT in the case of Barracuda Networks India Private Limited(supra), reads as follows:-

“11. As far as comparability of companies listed as (a) to (g) in Grd.No.4 raised by the Assessee is concerned, the admitted factual position is that the turnover of these companies is more than Rs.200 Crores and the Assessee’s turnover is only Rs. 17,77,11,711/-. The TPO excluded from the list of comparable companies chosen by the Assessee in its TP study companies whose turnover was less than Rs.1 Crore. The contention of the Assessee before the DRP was that while the TPO excluded companies with low turnover, he failed to apply the same yardstick to exclude companies with high turnover compared to the Assessee. The reason for excluding companies with low turnover was that such companies do not reflect the industry trend as their low cost to sales ratio made their results less reliable. The contention of the Assessee was that there would be effect on profitability wherever there is high or low turnover and therefore companies with high turnover should also be excluded from the list of comparable companies. The DRP primarily relied on the decision rendered by the Hon’ble Delhi High Court in the case of Chryscapital Investment Advisors India Pvt.Ltd Vs. DCIT 82 Taxmann.com 167(Del), wherein it was held that high turnover ipso facto does not lead to the conclusion that a company which is otherwise comparable on FAR analysis can be excluded and that the effect of such high turnover on the margin should be seen. The DRP therefore held that a company which is otherwise functionally comparable cannot be excluded only on the basis of high turnover. The Assessee has raised Grd.No.4 before the Tribunal challenging the aforesaid view of the DRP.

12. On the issue of application of turnover filter, we have heard the rival submissions. The parties relied on several decisions rendered on the above issue by the various decisions of the ITAT Bangalore Benches in favour of the Assessee and in favour of the Revenue, respectively. The ITAT Bangalore Bench in the case of Dell International Services India (P) Ltd. Vs. DCIT (2018) 89 Taxmann.com 44 (Bang-Trib) order dated 13.10.2017, took note of the decision of the ITAT Bangalore Bench in the

case of Sysarris Software Pvt.Ltd. Vs. DCIT (2016) 67 Taxmann.com 243 (Bangalore-Trib) wherein the Tribunal after noticing the decision of the Hon'ble Delhi High Court in the case of Chriscapital (supra) and the decision to the contrary in the case of CIT Vs. Pentair Water India Pvt.Ltd., Tax Appeal No.18 of 2015 dated 16.9.2015 wherein it was held that high turnover is a ground to exclude a company from the list of comparable companies in determining ALP, held that there were contrary views on the issue and hence the view favourable to the Assessee laid down in the case of Pentair Water (supra) should be adopted. The following were the conclusions of the Tribunal in the case of Dell International (supra):

“41. We have given a very careful consideration to the rival submissions. ITAT Bangalore Bench in the case of Genesis Integrating Systems (India) Pvt. Ltd. v. DCIT, ITA No.1231/Bang/2010, relying on Dun and Bradstreet's analysis, held grouping of companies having turnover of Rs. 1 crore to Rs.200 crores as comparable with each other was held to be proper. The following relevant observations were brought to our notice:-

“9. Having heard both the parties and having considered the rival contentions and also the judicial precedents on the issue, we find that the TPO himself has rejected the companies which .ire (sic) making losses as comparables. This shows that there is a limit for the lower end for identifying the comparables. In such a situation, we are unable to understand as to why there should not be an upper limit also. What should be upper limit is another factor to be considered. We agree with the contention of the learned counsel for the assessee that the size matters in business. A big company would be in a position to bargain the price and also attract more customers. It would also have a broad base of skilled employees who are able to give better output. A small company may not have these benefits and therefore, the turnover also would come down reducing profit margin. Thus, as held by the various benches of the Tribunal, when companies which are loss making are excluded from comparables, then the super profit making companies should also be excluded. For the purpose of classification of companies on the basis of net sales or turnover, we find that a reasonable classification has to be made. Dun & Bradstreet & Bradstreet and NASSCOM have given different ranges. Taking the Indian scenario into consideration, we feel that the classification made by Dun & Bradstreet is more suitable and reasonable. In view of the same, we hold that the turnover filter is very important and the companies having a turnover of Rs.1.00 crore to 200 crores have to be taken as a particular range and the assessee being in that range having turnover of 8.15 crores, the companies which also

have turnover of 1.00 to 200.00 crores only should be taken into consideration for the purpose of making TP study.”

42. The Assessee's turnover was around Rs.110 Crores. Therefore the action of the CIT(A) in directing TPO to exclude companies having turnover of more than Rs.200 crores as not comparable with the Assessee was justified. As rightly pointed out by the learned counsel for the Assessee, there are two views expressed by two Hon'ble High Courts of Bombay and Delhi and both are nonjurisdictional High Courts. The view expressed by the Bombay High Court is in favour of the Assessee and therefore following the said view, the action of the CIT(A) excluding companies with turnover of above Rs.200 crores from the list of comparable companies is held to correct and such action does not call for any interference.”

13. The Tribunal in the case of Autodesk India Pvt.Ltd. Vs. DCIT (2018) 96 Taxmann.com 263 (Bangalore-Tribunal), took note of all the conflicting decision on the issue and rendered its decision and in paragraph 17.7. of the decision held as that high turnover is a ground for excluding companies as not comparable with a company that has low turnover. The following were the relevant observations:

17.7. We have considered the rival submissions. The substantial question of law (Question No.1 to 3) which was framed by the Hon'ble Delhi High Court in the case of Chryscapital Investment Advisors (India) Pvt.Ltd., (supra) was as to whether comparable can be rejected on the ground that they have exceptionally high profit margins or fluctuation profit margins, as compared to the Assessee in transfer pricing analysis. Therefore as rightly submitted by the learned counsel for the Assessee the observations of the Hon'ble High Court, in so far as it refers to turnover, were in the nature of obiter dictum. Judicial discipline requires that the Tribunal should follow the decision of a non-jurisdiction High Court, even though the said decision is of a non-jurisdictional High Court. We however find that the Hon'ble Bombay High Court in the case of CIT Vs. Pentair Water India Pvt.Ltd. Tax Appeal No.18 of 2015 judgment dated 16.9.2015 has taken the view that turnover is a relevant criterion for choosing companies as comparable companies in determination of ALP in transfer pricing cases. There is no decision of the jurisdictional High Court on this issue. In the circumstances, following the principle that where two views are available on an issue, the view favourable to the Assessee has to be adopted, we respectfully follow the view of the Hon'ble Bombay High Court on the issue. Respectfully following the aforesaid decision, we uphold the order of the DRP excluding 5 companies from the list of comparable companies chosen by the TPO on the basis that the 5 companies turnover was much higher compared to that the Assessee.

17.8. In view of the above conclusion, there may not be any

necessity to examine as to whether the decision rendered in the case of Genisys Integrating (supra) by the ITAT Bangalore Bench should continue to be followed. Since arguments were advanced on the correctness of the decisions rendered by the ITAT Mumbai and Bangalore Benches taking a view contrary to that taken in the case of Genisys Integrating (supra), we proceed to examine the said issue also. On this issue, the first aspect which we notice is that the decision rendered in the case of Genisys Integrating (supra) was the earliest decision rendered on the issue of comparability of companies on the basis of turnover in Transfer Pricing cases. The decision was rendered as early as 5.8.2011. The decisions rendered by the ITAT Mumbai Benches cited by the learned DR before us in the case of Willis Processing Services (supra) and Capgemini India Pvt.Ltd. (supra) are to be regarded as per incurium as these decisions ignore a binding co-ordinate bench decision. In this regard the decisions referred to by the learned counsel for the Assessee supports the plea of the learned counsel for the Assessee. The decisions rendered in the case of M/S.NTT Data (supra), Societe Generale Global Solutions (supra) and LSI Technologies (supra) were rendered later in point of time. Those decisions follow the ratio laid down in Willis Processing Services (supra) and have to be regarded as per incurium. These three decisions also place reliance on the decision of the Hon'ble Delhi High Court in the case of Chriscapital Investment (supra). We have already held that the decision rendered in the case of Chriscapital Investment (supra) is obiter dicta and that the ratio decidendi laid down by the Hon'ble Bombay High Court in the case of Pentair (supra) which is favourable to the Assessee has to be followed. Therefore, the decisions cited by the learned DR before us cannot be the basis to hold that high turnover is not relevant criteria for deciding on comparability of companies in determination of ALP under the Transfer Pricing regulations under the Act. For the reasons given above, we uphold the order of the CIT(A) on the issue of application of turnover filter and his action in excluding companies by following the ratio laid down in the case of Genisys Integrating (supra).

14. In view of the aforesaid decision, we hold that companies listed in Sl.No.(a) to (g) of Grd.No.4 raised by the Assessee whose turnover in the current year is more than Rs.200 Crores should be excluded from the list of comparable companies."

6.9.2 In this case, the assessee's turnover is Rs.40.87 crore and the assessee cannot be compared to the companies having high turnover exceeding Rs.200 crore. Therefore, in view of the order of the ITAT in the case of Barracuda Networks India Private Limited(supra), we direct the AO /

TPO to exclude Larsen & Toubro Infotech Limited, Nihilient Technologies Limited, Persistent Systems Limited, Thirdware Solutions Limited, Infosys Limited, Aspire Systems (India) Private Limited and Cybage Software Private Limited, from the list of comparables.

6.9.3 As regards R S Software (India) Limited is concerned, the Bangalore Bench of the Tribunal in the case of Barracuda Networks India Private Limited(supra) had held that R S Software (India) Limited, ought to be accepted as comparable for A.Y. 2016-2017, however, should not be considered as comparable for assessment years 2015-2016 and 2014-2015, since the said company's turnover for the period exceeded Rs.200 crore. Accordingly, it was concluded that the margin earned by the company for assessment years 2014-2015 and 2015-2016 was not to be considered. The relevant finding of the Bangalore Bench of the Tribunal in the case of Barracuda Networks India Private Limited(supra), reads as follows:-

“15. As far as company listed at Sl.No.(h) of Grd.No.4 and Grd.No.5 i.e., R.S.Software (India) Ltd., is concerned, the turnover of this company in the current year is less than Rs.200 Crores but in the earlier two years its turnover was more than Rs.200 crores and was liable to be excluded in those earlier two years. The question raised in the aforesaid grounds is as to: whether this company should also be excluded on the application of turnover filter by reason of its turnover in the earlier two years being more than Rs.200 crores in the light of Rule 10CA of the rules which were applicable from AY 2014-15 onwards

or

whether in computing the weighted average profit margin of this company, the earlier two years profit margins have to be ignored because they fail the test of comparability in those two earlier years by reason of the application of the Rs.200 Crore turnover filter.

16. To answer the above question, we need to look at the amendment to the rules that allow for introduction of a “range concept” for

determination of ALP and “use of multiple year data” for undertaking comparability analysis in transfer pricing cases. The provisions of the Income-tax Act were amended through the Finance (No.2) Act, 2014 to facilitate alignment of Indian transfer regime with international best practices. The manner of computation of ALP is laid down under the Income-tax Rules. The Government has notified the amended Rules for determining ALP vide S.O. No. 2860 (E) dated 19/10/2015. The amended regime will be applicable for computation of ALP of international transactions and specified domestic transactions undertaken on or after 1/04/2014 i.e. on and after PY 2014-15. The amended rules allow for introduction of a “range concept” for determination of ALP and “use of multiple year data” for undertaking comparability analysis in transfer pricing cases. The use of range concept being a statistical tool enhances the reliability of analysis undertaken for computation of ALP. The range concept will be applicable in certain cases for determining the price and will begin with the 35th percentile and end with the 65th percentile of the comparable prices. Transaction price shown by the taxpayers falling within the range will be accepted and no adjustment will be made. The use of multiple year data allows for yearly variations to be averaged out and would therefore add value to transfer pricing analysis. The Amended Income tax Rules, 1962 (‘Rules’) via Notification 83 of 2015 which is the 16th amendment to the originally drafted Indian Tax Rules, 1962, are applicable for transactions undertaken on or after 1 April 2014 (i.e. from FY 2014-15 and onwards). These amended provisions are applicable only when the determination of ‘ALP’ is done under the MAM being resale price method (‘RPM’), cost plus method (‘CPM’) or transactional net margin method (‘TNMM’). The relevant provisions of Rule 10CA of the Rules, in so far as it relates to choice of comparable companies, read as follows:

“Computation of arm's length price in certain cases. 10CA.

(1) Where in respect of an international transaction or a specified domestic transaction, the application of the most appropriate method referred to in sub-section (1) of section 92C results in determination of more than one price, then the arm's length price in respect of such international transaction or specified domestic transaction shall be computed in accordance with the provisions of this rule.

(2) A dataset shall be constructed by placing the prices referred to in sub-rule (1) in an ascending order and the arm's length price shall be determined on the basis of the dataset so constructed:

Provided that in a case referred to in clause (i) of sub-rule (5) of rule 10B, where the comparable uncontrolled transaction has been identified on the basis of data relating to the current year and the enterprise undertaking the said uncontrolled transaction, [not being the enterprise undertaking the international transaction or the specified domestic transaction referred to in sub-rule (1)], has in either or both of the two financial years immediately preceding the current year undertaken the same or similar comparable uncontrolled transaction then,—

(i) the most appropriate method used to determine the price of the comparable uncontrolled transaction or transactions undertaken in the aforesaid period and the price in respect of such uncontrolled transactions shall be determined; and

(ii) the weighted average of the prices, computed in accordance with the manner provided in sub-rule (3), of the comparable uncontrolled transactions undertaken in the current year and in the aforesaid period preceding it shall be included in the dataset instead of the price referred to in sub-rule (1):

Provided further that in a case referred to in clause (ii) of sub-rule (5) of rule 10B, where the comparable uncontrolled transaction has been identified on the basis of the data relating to the financial year immediately preceding the current year and the enterprise undertaking the said uncontrolled transaction, [not being the enterprise undertaking the international transaction or the specified domestic transaction referred to in sub-rule (1)], has in the financial year immediately preceding the said financial year undertaken the same or similar comparable uncontrolled transaction then,—

(i) the price in respect of such uncontrolled transaction shall be determined by applying the most appropriate method in a similar manner as it was applied to determine the price of the comparable uncontrolled transaction undertaken in the financial year immediately preceding the current year; and

(ii) the weighted average of the prices, computed in accordance with the manner provided in sub-rule (3), of the comparable uncontrolled transactions undertaken in the aforesaid period of two years shall be included in the dataset instead of the price referred to in sub-rule (1) :

Provided also that where the use of data relating to the current year in terms of the proviso to sub-rule (5) of rule 10B establishes that,—

(i) the enterprise has not undertaken same or similar uncontrolled transaction during the current year; or

(ii) the uncontrolled transaction undertaken by an enterprise in the current year is not a comparable uncontrolled transaction,

then, irrespective of the fact that such an enterprise had undertaken comparable uncontrolled transaction in the financial year immediately preceding the current year or the financial year immediately preceding such financial year, the price of comparable uncontrolled transaction or the weighted average of the prices of the uncontrolled transactions, as the case may be,

undertaken by such enterprise shall not be included in the dataset.

(3) Where an enterprise has undertaken comparable uncontrolled transactions in more than one financial year, then for the purposes of sub-rule (2) the weighted average of the prices of such transactions shall be computed in the following manner, namely:—

(i) where the prices have been determined using the method referred to in clause (b) of subrule (1) of rule 10B, the weighted average of the prices shall be computed with weights being assigned to the quantum of sales which has been considered for arriving at the respective prices;

(ii) where the prices have been determined using the method referred to in clause (c) of subrule (1) of rule 10B, the weighted average of the prices shall be computed with weights being assigned to the quantum of costs which has been considered for arriving at the respective prices;

(iii) where the prices have been determined using the method referred to in clause (e) of subrule (1) of rule 10B, the weighted average of the prices shall be computed with weights being assigned to the quantum of costs incurred or sales effected or assets employed or to be employed, or as the case may be, any other base which has been considered for arriving at the respective prices

17. Let us apply the above rules to the comparable company R.S.Software (India) Ltd. As per Rule 10CA(2), the dataset of comparable companies chosen has to be arranged in ascending order. As per the 1st proviso to Rule 10CA(2), R.S.Software (India) Ltd., was chosen as a comparable company based on the data relating to the current year and in the earlier two financial years immediately preceding the current financial year. In all the financial years the said company has undertaken similar comparable uncontrolled transaction. Clause (i) to 1st proviso to Sec.10CA(2) mandates that the same MAM has to be used to arrive at the price of the comparable uncontrolled transaction undertaken by R.S.Software (India) Ltd., in the financial years 2013-14 and 2014-15. As per clause (ii) of 1st proviso to Sec.10CA(2), weighted average of the prices of the 3 financial years have to be taken in accordance with Rule 10CA(3) and the weighted average so taken shall be included data set instead of the price arrived at by using current year data alone. In the present case, if one sees the chart of comparables of TPO given in paragraph-4 of this order, the profit margins of the Company R.S.Software (India) Ltd., for the three financial years were 2013-14 to 2015-16 were 24.14%, 32.75% and -2.09% respectively and the weighted average margin of 24.83% has been considered by the TPO.

18. The second proviso to Sec.10CA(2) of the Rules provides for a situation where R.S.Software (India) Ltd., has undertaken comparable uncontrolled transaction only in Financial year 2014-15 & 2015-16, then

the weighted average of the two financial year 2014-15 and 2015-16 has to be computed in the manner laid down in Rule 10CA(3) of the Rules and the margin so arrived at has to be included in the dataset.

19. The third proviso to Sec.10CA(2) of the rules provides that if in the current year i.e., financial year 2015-16 if R.S.Software (India) Ltd., has not undertaken any uncontrolled comparable transaction then that company can never be considered for inclusion in the dataset.

20. The submission of the learned Counsel for the Assessee was that as per the proviso to Rule 10CA(2) of the Rules, R.S.Software (India) Ltd., cannot be regarded as comparable company for Financial Year 2013-14 and 2014- 15 because in those years, the turnover of this company was more than Rs.200 crores. Therefore as per the first and second proviso to Rule 10CA(2) of the Rules, the profit margin of this company for Financial year 2013-14 & 2014-15 has to be ignored and the profit margin of the financial year 2015-16 alone should be taken. If one looks at Rule 10CA(2) in isolation, we have to reject this argument because the 1st and 2nd proviso to Rule 10CA(2) of the Rules refers to only R.S.Software (India) Ltd., (i.e., “where the comparable uncontrolled transaction has been identified on the basis of data relating to the current year and the enterprise undertaking the said uncontrolled transaction has in either or both of the two financial years immediately preceding the current year undertaken the same or similar comparable uncontrolled transaction”) undertaking uncontrolled transaction during the relevant previous year and if this condition is satisfied then the profit margin of R.S.Software for the 2 financial years immediately prior to the current financial year has to be taken. A plain reading of the 1st proviso would show that the question of comparability is not to be seen while applying the 1st and 2nd proviso to Rule 10CA(2) of the Rules. The provisions of Rule 10CA(2) have to be read harmoniously with the other provisions of Rule 10B

Determination of arm's length price under section 92C .

10B . (1) For the purposes of sub-section (2) of section 92C, the arm's length price in relation to an international transaction [or a specified domestic transaction] shall be determined by any of the following methods, being the most appropriate method, in the following manner, namely :—

(a) to (d).....

(e) transactional net margin method, by which,—

(i) the net profit margin realised by the enterprise from an international transaction [or a specified domestic transaction] entered into with an associated enterprise is computed in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise or having regard to any other relevant base;

(ii) the net profit margin realised by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction or a number of such transactions is computed having regard to the same base;

(iii) the net profit margin referred to in sub-clause (ii) arising in comparable uncontrolled transactions is adjusted to take into account the differences, if any, between the international transaction [or the specified domestic transaction] and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of net profit margin in the open market;

(iv) the net profit margin realised by the enterprise and referred to in sub-clause (i) is established to be the same as the net profit margin referred to in sub-clause (iii);

(v) the net profit margin thus established is then taken into account to arrive at an arm's length price in relation to the international transaction [or the specified domestic transaction];

(2) For the purposes of sub-rule (1), the comparability of an international transaction [or a specified domestic transaction] with an uncontrolled transaction shall be judged with reference to the following, namely:—

(a) the specific characteristics of the property transferred or services provided in either transaction;

(b) the functions performed, taking into account assets employed or to be employed and the risks assumed, by the respective parties to the transactions;

(c) the contractual terms (whether or not such terms are formal or in writing) of the transactions which lay down explicitly or implicitly how the responsibilities, risks and benefits are to be divided between the respective parties to the transactions;

(d) conditions prevailing in the markets in which the respective parties to the transactions operate, including the geographical location and size of the markets, the laws and Government orders in force, costs of labour and capital in the markets, overall economic development and level of competition and whether the markets are wholesale or retail.

(3) An uncontrolled transaction shall be comparable to an international transaction [or a specified domestic transaction] if—

(i) none of the differences, if any, between the transactions being compared, or between the enterprises entering into such transactions are likely to materially affect the price or cost charged or paid in, or the profit arising from, such transactions in the open market; or

(ii) reasonably accurate adjustments can be made to eliminate the material effects of such differences.

(4) The data to be used in analysing the comparability of an uncontrolled transaction with an international transaction [or a specified domestic

transaction] shall be the data relating to the financial year [(hereafter in this rule and in rule 10CA referred to as the 'current year')]] in which the international transaction [or the specified domestic transaction] has been entered into :

Provided that data relating to a period not being more than two years prior to [the current year] may also be considered if such data reveals facts which could have an influence on the determination of transfer prices in relation to the transactions being compared:

A reading of Rule 10B(3) shows that comparison of an uncontrolled transaction to an international transaction can be done only if differences, if any, between the transactions that are compared or between the enterprises entering into such transactions are likely to materially affect the price or cost charged or paid in, or the profit arising from, such transactions in the open market or reasonably accurate adjustments can be made to eliminate the material effects of such differences. A reading of Proviso to Rule 10B(4) would show that use of data relating to a period of two years prior to the current year may also be considered but with a rider that "if such data reveals facts which could have an influence on the determination of transfer prices in relation to the transactions being compared". If by application of any filter an enterprise undertaking uncontrolled transaction similar to an international transaction is regarded as not being comparable in the earlier two years immediately preceding the current year and thereby attracting the provisions of Rule 10B(2) or 10B(3) then the data for those years will not have any influence on the determination of transfer prices in relation to the transactions being compared for the current year and hence have to be ignored. On a harmonious reading of the provisions of Rule 10CA, 10B(3) (4) of the Rules, we agree with the stand taken by the learned counsel for the Assessee. Therefore, if at all R.S.Software Ltd., is to be regarded as a comparable company, then the margins for AY 2014-15 and 2015-16 of the company have to be ignored because in those years they are to be regarded as not comparable. We hold accordingly."

6.9.4 In the light of the ITAT order in the case of Barracuda Networks India Private Limited(supra), we direct the AO / TPO to include R S Software (India) Limited as a comparable company. However, the margins of the said company for assessment years 2014-2015 and 2015-2016 have to be ignored since the turnover exceeded Rs.200 crore for the said period. It is ordered accordingly.

6.9.5 By excluding the seven companies from the comparable list and by taking the margin of R S Software (India) Limited only for assessment year 2016-2017, prima facie, the margin of comparable company is below the assessee's margin. Therefore, the other grounds raised by the assessee as regards TP adjustment for provision for software development services are left open.

Interest on delayed receivables (Grounds 14 to 19) (TP Adjustment amounting to Rs.83,55,708)

7. The TPO did not accept the assessee's contention that trade receivables are not separate international transaction and impact if any, gets subsumed by way of working capital adjustment. The TPO has proceeded to re-characterize the trade receivable from AEs as loan to AEs and imputed interest on trade receivables (invoice-wise) during the year for a period of 335 days (i.e. allowing a credit period of 75 days), at 6 month LIBOR plus 450 bps (resulting in 4.985%). The same resulted in an adjustment amounting to Rs.83,55,708. The assessee filed objections before the DRP. However, the objections were rejected and adjustment remained unchanged at Rs.83,55,708.

7.1 Aggrieved by the DRP's directions / final assessment order, the assessee has raised this issue before the Tribunal.

7.2 We have heard rival submissions and perused the material on record. The assessee has undertaken working capital adjustment to consider the impact of extended credit period. The working capital adjustments are made to analyse

the operational performance of the companies, therefore, the receivables amount gets adjusted in working capital adjustments and another separate addition is not required under the TP provisions. This principle has been upheld by the Tribunal in assessee's own case for assessment year 2014-2015 in IT(TP)A No.3358/Bang/2011 (order dated 01.11.2021). The relevant finding of the Tribunal in assessee's own case for assessment year 2014-2015 reads as follows:-

“7.4 We have heard rival submissions and perused the material on record. The Tribunal in assessee's own case for assessment year 2008-2009 (supra) had directed AO / TPO to determine afresh the ALP in respect of providing SWD services by considering the proper working capital adjustment in comparable prices. It was held by the Tribunal that in case after giving necessary adjustment, the international transaction of the assessee is found to be at arm's length, then there is no question of separate adjustment on account of allowing credit period from receivables from AE. The relevant finding of the Tribunal in assessee's own case for assessment year 2008-2009 reads as follows:-

“23. We have heard the learned Counsel for the assessee as well as learned Departmental Representative and considered the relevant material on record. At the outset we note that this issue has been considered and decided by this Tribunal in a series of decisions including the decision in the case of M/s. Dell International Services India Pvt. Ltd. Vs. JCIT in ITA No.308/Bang/2015 Dt.17.6.2016 wherein the Tribunal has considered this issue in para 7 as under :

“ 7. We have considered the rival submissions and relevant material on record. At the outset, we note that allowing a credit period on receivable from AE is not an independent international transaction however, it is part of the main international transaction of providing software development services by the assessee to its AEs. There are series of decisions wherein the Tribunal has considered this transaction as part of the main international transaction between the assessee and its AE and therefore the treatment of the same at the time of determining the arm's length of the international transaction has to be given in the shape of allowing the necessary adjustment in the comparable prices on account of working capital adjustment. We find that the Mumbai Bench of the Tribunal in the case of Goldstar Jewellery Ltd. in ITA No.6570/Mum/2012 vide order dt.14.1.2015 as well as the Delhi Bench of the Tribunal in the case of Kusum Healthcare Pvt. Ltd. Vs. ACIT in ITA No.6814/Del/2014 vide order dt.31.3.2015 has taken this view that allowing the credit period

over and above normal credit period prevailing in the industry is certainly relevant and part of the main international transaction of sale or purchase between the assessee and the AE. However, it was held that it cannot be treated as an independent international transaction de hors the main international transaction between the parties. We further note that an identical issue was considered and decided by the Mumbai Bench of this Tribunal in the case of Information Systems Resource Centre Pvt. Ltd. Vs. ACIT in ITA No.7757/Mum/2012 and C.O. 282/Mum/2013 vide order dt.29.5.2015 in paras 11 to 13 as under :

“ 11. We have considered the rival submissions as well as the relevant material on record. In the present case, the sale transaction of the assessee with its A.E. have been accepted by the Transfer Pricing Officer / Assessing Officer at arm's length and no adjustment has been made in respect of the sale transaction. However, the Transfer Pricing Officer has made the adjustment on account of credit period provided by the assessee to the A.E. on realisation of sale proceeds. At the outset, we note that an identical issue has been considered by the co- ordinate bench of the Tribunal, Mumbai Benches, in Goldstar Jewellery Ltd. (supra), vide Para-8, held as under:-

“8. We have considered the rival submissions and relevant material on record. The assessee has reported international transaction in its TP report regarding sale to its AE from manufacture of jewellery units and diamond trading unit. The TPO accepted the price charged by the assessee from AE at arm's length. However, the TPO has made the adjustment on account of notional interest for the excess period allowed by the assessee to AE for realization of dues. The TPO applied 18.816% per annum as arm's length on the over due amounts of AE and proposed adjustment of Rs. 2,49,95,139/-. The DRP though concurred with the view of the Assessing Officer/TPO on the issue of international transaction, however, the adjustment was reduced by applying the interest rate of 7% instead of 18.816% applied by the TPO. The first issue raised by the assessee is whether the aggregate period extended by the assessee to the AE which is more than the average credit period extended to the nonAE would constitute international transaction. We are of the view that after the insertion of explanation to section 92B(1), the payment or deferred payment or receivable or any debt arising during the course of business fall under the expression international transaction as per explanation. Therefore, in view of the expanded meaning of the international transaction as contemplated under clause (i) (e) of explanation to section 92B(1), the delay in realization of dues from the AE in comparison to non-AE would certainly falls in the ambit of international transaction. However, this transaction of allowing the credit period to AE on realization of sale proceeds is not an independent international transaction but it is a closely linked or continuous transaction along with sale transaction to the AE. The

credit period allowed to the party depends upon various factors which also includes the price charged by the assessee from purchaser. Therefore, the credit period extended by the assessee to the AE cannot be examined independently but has to be considered along with the main international transaction being sale to the AE. As per Rule 10A(d) if a number of transactions are closely linked or continuous in nature and arising from a continuous transactions of supply of amenity or services the transactions is treated as closely linked transactions for the purpose of transfer pricing and, therefore, the aggregate and clubbing of closely linked transaction are permitted under said rule. This concept of aggregation of the transaction which is closely linked is also supported by OECD transfer pricing guidelines. In order to examine whether the number of transactions are closely linked or continuous so as to aggregate for the purpose of evaluation what is to be considered is that one transaction is follow-on of the earlier transaction and then the subsequent transaction is carried out and dependent wholly or substantially on the earlier transaction. In other words, if two transactions are so closely linked that determination of price of one transaction is dependent on the other transaction then for the purpose of determining the ALP, the closely linked transaction should be aggregated and clubbed together. When the transaction are influenced by each other and particularly in determining the price and profit involved in the transactions then those transactions can safely be regarded as closely linked transactions. In the case in hand the credit period extended to the AE is a direct result of sale transaction. Therefore no question of credit period allowed to the AE for realization of sale proceeds without having sale to AE. The credit period extended to the AE cannot be treated as a transaction stand alone without considering the main transaction of sale. The sale price of the product or service determined between the parties is always influenced by the credit period allowed by the seller. Therefore, the transaction of sale to the AE and credit period allowed in realization of sale proceeds are closely linked as they are inter linked and the terms and conditions of sale as well as the price are determined based on the totality of the transaction and not on individual and separate transaction. The approach of the TPO and DRP in analyzing the credit period allowed by the assessee to the AE without considering the main international transaction being sale to the AE will give distorted result by disregarding the price charged by the assessee from AE. Though extra period allowed for realization of sale proceeds from the AE is an international transaction, however, for the purpose of determining the ALP, the same has to be clubbed or aggregated with the sale transactions with the AE. Even by considering it as an independent transaction the same has to be compared with the internal CUP available in the shape of the credit allowed by the assessee to non AE. When the assessee is not making any difference for not charging the interest from AE as well as nonAE then the only difference between the two can be considered is the average period allowed along with outstanding

amount. If the average period multiplied by the outstanding amount of the AE is at arm's length in comparison to the average period of realization and multiplied by the outstanding from non AEs then no adjustment can be made being the transaction is at arm's length. The third aspect of the issue is that the arm's length interest for making the adjustment. Both the TPO and DRP has taken into consideration the lending rates, however, this is not a transaction of loan or advance to the AE but it is only an excess period allowed for realization of sales proceeds from the AE. Therefore, the arm's length interest in any case would be the average cost of the total fund available to the assessee and not the rate at which a loan is available. Accordingly, we direct the Assessing Officer/TPO to re-do the exercise of determination of ALP in terms of above observation." 12. Thus, it is clear that the Tribunal has taken a view that the transaction of allowing the credit period to the A.E. on realisation of sale proceeds has to be considered along with the main international transaction in respect of sale to A.E. A similar view has been taken by the Tribunal, Delhi Bench, in *Kusum Healthcare Pvt. Ltd.* (supra), wherein the Tribunal, vide Para-7 to 10, held as under:-

" 7. We have heard rival submissions and perused the material on record. An uncontrolled entity will expect to earn a market rate of return on its working capital investment independent of the functions it performs or products it provides. However, the amount of capital required to support these functions varies greatly, because the level of inventories, debtors and creditors varies. High levels of working capital create costs either in the form of incurred interest or in the form of opportunity costs. Working capital yields a return resulting from a) higher sales price or b) lower cost of goods sold which would have a positive impact on the operational result. Higher sales prices acts as a return for the longer credit period granted to customers. Similarly in return for longer credit period granted, a firm should be willing to pay higher purchase price which adds to the cost of goods sold. Therefore, high levels accounts receivable and inventory tend to overstate the operating results while high levels of accounts payable tend to understate them thereby necessitating appropriate adjustment. The appropriate adjustments need to be considered to bring parity in the working capital investment of the assessee and the comparables rather than looking at the receivable independently. Such working capital adjustment takes into account the impact of outstanding receivables on the profitability. In this regard, the reliance is placed on the following rulings wherein the need to undertake working capital adjustment has been appreciated by the Hon'ble Tribunals :

- Mercer Consulting India Pvt. Ltd. [TS-170-ITAT-2014(DEL)]
- Mentor Graphics (Noida) Private Limited [109 ITD 101]
- Egain communication (P) Ltd. [ITA No. 1685/PN/2007]
- Sony India (Pvt.) ltd. [2011-TII-43-ITAT-DEL-TP]
- Capgemini India Private Limited [TS-45-ITAT-2013(Mum)-TP]

8. In view of the above, a working adjustment appropriately takes into account the outstanding receivable. Therefore, the assessee has undertaken a working capital adjustment to reflect these differences by adjusting for differences in working capital and thereby, profitability of each comparable company. Accordingly, while calculating the working capital adjusted, operating margin on costs of the comparable companies, the impact of outstanding receivables on the profitability has been taken into account. If the pricing/ profitability of the assessee are more than the working capital adjusted margin of the comparables, then additional imputation of interest on the outstanding receivables is not warranted.

9. The assessee had undertaken a working capital adjustment for the comparable companies selected in its transfer pricing report which was also submitted with the Ld. TPO. A snapshot of the result is provided below: Segment Name Appellant's Margin (OP/TC) Working capital adjusted margins of comparables (OP/TC) Manufacturing Activity 46.33% 11.84% Trading Activity 17.44% 8.36% 10. The above analysis empirically demonstrates that the differential impact of working capital of the vis-a-vis its comparables has already been factored in the pricing/profitability of the assessee which is more than that working capital adjusted margin of the comparables. Hence, any further adjustment to the margins of the assessee on the pretext of outstanding receivables is unwarranted and wholly unjustified."

Following the orders of the Tribunal, we set aside this issue to the record of the Assessing Officer / Transfer Pricing Officer and direct to re-do the exercise of determination of arm's length price in the light of the above decisions of the Tribunal. The grounds raised in this cross objection are allowed for statistical purposes." Following the earlier orders of this Tribunal, we set aside this issue to the record of the A.O./TPO with the direction to redo the exercise of determination of ALP by considering the proper working capital adjustment in the comparable prices in respect of transaction of software development services provider to the AE. We make it clear that if after giving the necessary adjustment the international transaction of the assessee is found at arm's length then there is no question of any separate adjustment on account of allowing the credit period on the receivable from AE. We further clarify that the normal credit period allowed for the receivable from the AE shall be the credit period prevailing in the industry and therefore we are of the view that two months credit period should be taken as a normal business practice in the industry. The TPO/A.O shall also consider the benchmark interest rate as LIBOR/PLR in the light of various precedents on this issue."

A similar view has been taken by this Tribunal in a series of other decisions as referred in the earlier decisions as well as relied upon by the ld. AR of the assessee. Accordingly, taking a consistent view we set aside this issue to the record of the A.O./TPO with the direction to redo the

determination of ALP in respect of providing software development services by considering the proper working capital adjustment in comparable price. In case after giving the necessary adjustment the international transaction of the assessee is found at arm's length then there is no question of separate adjustment on account of allowing credit period on receivable from the AE."

7.2.1 Taking a consistent stand, we direct the AO / TPO to redo the transfer pricing analysis in respect of interest on outstanding receivables by taking into account the directions of the Tribunal in assessee's own case for assessment year 2008-2009 (supra). It is ordered accordingly.

7.6 In the result, grounds 9 to 14 are allowed for statistical purposes.

Corporate Tax Issues : Disallowance u/s 40(a)(i) of the I.T.Act amounting to Rs.50,20,109

8. The assessee had made payment to Xchanging Global Insurance Solutions Limited (XGISL) UK amounting to Rs.50,20,109. It is claimed by the assessee that these payments are made towards reimbursement of expenses. It was submitted that charges are towards use of cloud based applications / tools like Leapfrog, Sales force etc. which are procured centrally by XGISL for usage of Xchanging group entities worldwide. It was stated that the cost with respect to these charges are cross charged to the Xchanging group entities on cost to cost basis without any markup. However, the Assessing Officer held that the payments are made for purchase of software license and assessee having failed to deduct TDS, the expenditure claimed cannot be allowed as deduction u/s 40(a)(i) of the I.T.Act. It was further held by the

Assessing Officer that the assessee has paid for the use of software and has clearly gains right to use their patents / copyrights.

8.1 The DRP rejected the objections of the assessee by placing reliance on the judgment of the Hon'ble Karnataka High Court in the case of CIT v Samsung Electronics Ltd. reported in 345 ITR 494 (Kar.). Pursuant to the DRP's directions, the final assessment order was passed, against which the assessee has filed appeal before the Tribunal. The contention of the assessee are summarized as follows:-

- * The payments are towards cloud-based services availed by the Company which does not provide the Company with use or right to use any copyright/process/equipment owned by the service provider and the same are not taxable as "Royalty" under the beneficial provisions of India-UK DTAA in absence of use of or grant of any right to use any copyright/patent etc. Reliance in this regard is placed on the Hon'ble Supreme Court decision in the case of Engineering Analysis Centre of Excellence (P.) Ltd. v. Commissioner of Income-tax (2021)125 taxmann.com 42 (SC).
- * The payment towards leapfrog, Salesforce are towards use of standard applications and does not provide XSL with any right to use, modify, alter, exploit the process/software/IP etc, the payment is not taxable in India under the beneficial provisions of the India-UK DTAA and therefore, the same should not be disallowed under the provisions of Section 40(a)(i) of the Act.
- * The copyright in the software is being used by the service provider and not the Company. All that the Company is doing is availing a standard service for a fee.
- * It is not a case of purchase of software but a case of availing standard services which is available to anyone,

willing to pay, for a fee. The arrangement involves enjoyment of services rather than use of copyright of a software.

- * The Company does not acquire any right in the Intellectual Property ("IP") owned by the service provider in the application tools since there is no transfer or grant of license to use the IP. In this regard, reference is made to Para 9.2 of Schedule 5 of the agreement between the Company and XGISL (placed at Page No. 599 of the Factual Paper book) which states that the Company shall not acquire any right, title or interest in any IP of XGISL.
- * Without prejudice, the Company further submits that the payments to XGISL are in the nature of reimbursements at cost and there is no income element (please do refer to Schedule 1 to the Agreement placed at Page No. 575 of the Factual Paper book). Accordingly, the subject payments by the Company should not attract withholding tax provisions under Section 195 of the Act in absence of element of income embedded therein.

8.2 The learned Departmental Representative supported the orders of the Assessing Officer and the DRP.

8.3 We have heard rival submissions and perused the material on record. The assessee has produced End Users License Agreement (EULA) from pages 572 to 603 of the paper book. The learned AR has taken us through various clauses, especially, clause 9, wherein he emphasized that the assessee does not acquire any right, title or interest in any IPR (refer page 599 of the paper book). The Hon'ble Apex Court in the case of Engineering Analysis Centre of Excellence (P.) Ltd. v. CIT reported in 432 ITR 471 had clearly held that amounts paid by the resident end users to non-resident computer software manufacturer / suppliers for use of computer

software through EULA is not payment of royalty for the use of copyright in computer software and the same does not give rise to any income taxable in India as a result of which the payer is not liable for TDS u/s 195 of the I.T.Act. In light of the judgment of the Hon'ble Apex Court in the case of Engineering Analysis Centre of Excellence (P.) Ltd. v. CIT (supra), we restore the issue to the files of the A.O. The A.O. is directed to examine the EULA entered by the assessee with XGISL and decide the issue afresh. The A.O. shall follow the dictum laid down by the Hon'ble Apex Court in the case of Engineering Analysis Centre of Excellence (P.) Ltd. v. CIT (supra) while taking a decision in the said matter. It is ordered accordingly.

8.4 In the result, grounds 20 to 23 are allowed for statistical purposes.

9. The other grounds raised on the corporate tax issues were not pressed by the learned AR, during the course of hearing.

10. In the result, the appeal filed by the assessee is partly allowed for statistical purposes.

Order pronounced on this 12th day of May, 2022.

Sd/-
(Padmavathy S)
ACCOUNTANT MEMBER

Sd/-
(George George K)
JUDICIAL MEMBER

Bangalore; Dated : 12th May, 2022.
Devadas G*

Copy to :

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

Asst.Registrar/ITAT, Bangalore