

**IN THE INCOME TAX APPELLATE TRIBUNAL
'B' BENCH : BANGALORE**

**BEFORE SHRI N.V VASUDEVAN, VICE PRESIDENT AND
MS. PADMAVATHY S, ACCOUNTANT MEMBER**

ITA No.2024/Bang/2017
Assessment year : 2010-11

The Dy. Commissioner of Income-tax, Circle-7(1)(1), Bengaluru.	Vs.	M/s Unisys India Pvt. Ltd., 4 th & 5 th Floor, Block 'WARP', SJR 1 Park, Whitefield Area, No.13, 14 & 15, KR Puram, Bengaluru-560 066. PAN – AAACU 1502 G
APPELLANT		RESPONDENT

ITA No.2027/Bang/2017
Assessment year : 2010-11

M/s Unisys India Pvt. Ltd., 4 th & 5 th Floor, Block 'WARP', SJR 1 Park, Whitefield Area, No.13, 14 & 15, KR Puram, Bengaluru-560 066. PAN – AAACU 1502 G	Vs.	The Dy. Commissioner of Income-tax, Circle-7(1)(1), Bengaluru.
APPELLANT		RESPONDENT

Assessee by	:	Shri Dhanesh Bafna, AR & Shri Pratik Shah, C.A
Revenue by	:	Shri Srinivasa T Bidari, CIT(DR)

Date of hearing	:	28.04.2022
Date of Pronouncement	:	17.05.2022

ORDER

Per Padmavathy S, Accountant Member

These cross appeals are filed by the assessee and Revenue against the order of the Commissioner of Income Tax, CIT(A)-7 Bengaluru dated 02/08/2017 for the assessment year 2010-11.

2. The brief facts of the case are that the assessee company was incorporated in India on November 28, 1994. All shares of the Assessee are held by Unisys Mauritius Limited, which is ultimately held by Unisys Corpn., USA. During FY 2010-11, Unisys India was essentially engaged in providing IT enabled services (ITES) and Software Development (IT) to its overseas group companies. In terms of the provisions of Sec.92-A of the Act, the Assessee and its wholly owned holding company were Associated Enterprises ("AEs"). In terms of Sec.92B(1) of the Act, the transaction of providing IT enabled services (ITES) and Software Development (IT) to its overseas group companies were "international transaction" i.e., a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost

or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises. In terms of Sec.92(1) of the Act, the any income arising from an international transaction shall be computed having regard to the arm's length price. In this appeal by the Assessee and the revenue, the dispute is with regard to determination of Arms' Length Price (ALP) in respect of the international transaction of rendering IT enabled services (ITES) and Software Development (IT) to the AE.

3. The international transactions in the Software Development Service (IT segment) & ITES segments with associated enterprises (AE's) relevant to this appeal are as follows:-

Sl. No.	Nature of Transaction	Amount (in INR)	Outcome of the TP Order
1	Business Process Outsourcing/ Information Technology enabled services	164,90,49,799	Adjustment done by the TPO
2	Software Development services	92,59,96,387	Adjustment done by the TPO
3	Interest of overdue outstanding	12,85,650	Accepted to be at Arm's length
4	Recovery of Expenses	14,13,89,127	Accepted to be at Arm's length
5	Reimbursement of expenses	6,61,74,125	Accepted to be at Arm's length

4. The details of segment financials are as follows:-

Description	Software Services (Rs.)	ITES (Rs.)
Operating Revenue	92,52,01,220	165,11,30,616
Operating Cost	84,03,26,419	147,51,13,176
Operating profit	8,48,74,801	17,60,17,440
OP/ OC	10%	12%

Software Development Service (IT Segment)

5. Grounds No. 1 to 6 raised by the revenue relate to the addition made consequent to determination of Transfer Price by the Transfer Pricing Officer (TPO) in the SWD Services segment, which addition was deleted by the CIT(A) on the adjustment to Arm's Length Price (ALP) suggested by the TPO. The CIT(A) deleted the 5 comparable companies included by the TPO viz., (i) Infosys Ltd.; (ii) Tata Elxi Ltd. (seg); (iii) Persistent Systems Ltd.; (iv) KALS Information Systems Ltd. and (v) ICRA Techno Analytics Ltd. in SWD segment against which the revenue is in appeal before the Tribunal. The revenue raised further grounds relating to working capital adjustment (Ground No. 7 to 10) allowed by the CIT(A) and the computation of 10A (Ground No. 11 & 12).

6. The revenue filed revised grounds through which it was submitted that Ground 11 and 12 are not pressed and hence dismissed. The grounds raised by the revenue relating to IT segment will be adjudicated first. The grounds raised for exclusion pertaining to ITES segment will be adjudicated while dealing with the appeal of the assessee in later part of this order

7. In support of the claim of the assessee that the price paid to AE was at arm's length, the assessee filed a transfer pricing (TP) analysis. The assessee adopted TNMM as most appropriate method (MAM).

The profit level indicator (PLI) chosen was operating profit to operating cost (OP/OC). The assessee chose the following 16 comparables the average margin of which was 13%.

S.No.	Name of Companies — SWD segment	Markup on Total Cost'
1	Akshay Software Technologies Ltd	9%
2	Compulink Systems Ltd	-7%
3	F C S Software Solutions Ltd	39%
4	Goldstone Technologies Ltd	12%
5	L G S Global Ltd	23%
#6	Larsen & Toubro Infotech Ltd	22%
#7	Mindtree Ltd	22%
8	P S I Data Systems Ltd	5%
9	Polaris Software Lab Ltd	11%
10	Reliance Infosolutions Pvt Ltd	1%
#11.	Sasken Communication Technologies Ltd*	13%
12	Synetairos Technologies Ltd	21%
#13	Thinksoft Global Services Ltd*	18%
14	Zensar Obt Technologies Ltd	19%
15	Crazy Infotech Ltd.	1%
i6	Teledata Marine Solutions Ltd	3%
	Average	13%

8. The assessee's margin of IT segment was 15.60% as per Form 3CEB submitted. The assessee therefore claimed that the international transactions with AE is at arm's length.

9. The TPO out of the above 16 comparables accepted the 4 (Highlighted) comparables and rejected the balance 12. The TPO proceeded to apply fresh filters and chose additional comparables as

given in the below table and worked out the revised TP margin post working capital adjustment at 21.19%.

Particulars	Comparables selected by Ld. TPO	
	Pre WC	Post WC
ICR.A. Techno Analytics Ltd. (seg)	24.94%	24.62%
Infosys Ltd.	44.98%	44.43%
Kals Information Systems Ltd. (seg)	34.41%	30.32%
L&T Infotech Ltd.	19.33%	19.43%
Mindtree Ltd. (seg)	14.83%	12.83%
Persistent Systems and Solutions Ltd.	15.38%	15.21%
Persistent Systems Ltd.	30.35%	28%
R S Software (India) Ltd.	10.29%	10.57%
Sasken Communication Technologies Ltd.	17.36%	16.45%
Tata Elxi Ltd. (seg)	20.93%	17.21%
Thinksoft Global Services Ltd.	17.05%	14.04%
Average margin	22.71%	21.19%

10. The TPO therefore computed the TP adjustments as per below computation

Adjusted margin (post working capital adjustment)	21.19%
Taxpayer operating cost (OC)	Rs. 84,03,24,419
Arm's length price (121.19% of OC)	Rs. 101,83,91,597
Price received	Rs. 92,52,01,220
Shortfall being adjustment u/s. 92CA	Rs. 9,31,90,367

11. Aggrieved, assessee field an appeal before the CIT(A). The CIT(A) accepted the contentions of the assessee and upheld the exclusion of these companies on the basis that they are not functionally comparable and followed the decision of coordinate bench in assessee's own case.

12. The Revenue is in appeal before the Tribunal against the order of CIT(A). The Id.DR submitted that the CIT(A) while excluding the 5 comparables did not call for objection from the TPO and hence the matter should go back to CIT(A) with a direction to call for a remand report from the TPO before deciding the case on merits.

13. The Id.AR in a rebuttal submitted that the assessee has raised its objections before the TPO for the inclusions of these companies and TPO has considered all the facts before deciding to include. Hence there is no requirement for this issue to go back to CIT(A) calling for remand report from TPO. The AR also submitted that the coordinate bench of the Tribunal has upheld the exclusion of (i) Infosvs Ltd.; (ii) Tata Elxi Ltd. (seg); (iii) Persistent Systems Ltd.; and (iv) KALS Information Systems Ltd, in assessee's own case (**ITA No. 67/Bang/2015**) for the assessment year 2009-10. The Ld AR also submitted that exclusion of ICRA Techno Analytics Ltd is also covered by the decision of the coordinate bench of the Tribunal in the case of Cisco Systems (India) Pvt. Ltd., vs. ACIT (**IT(TP)A No.505&508/Bang/20015**).

14. We have heard the rival submissions and perused the materials on record. We notice the coordinate bench of the Tribunal in assessee's own has dealt with regard to exclusion of (i) Infosvs Ltd.; (ii) Tata Elxi Ltd. (seg); (iii) Persistent Systems Ltd.; and (iv) KALS Information Systems Ltd as under -

32. **Infosys Ltd.**:- As far as this company is concerned, it is not in dispute before us that this company has been considered to be functionally different from a company providing simple software development services, as this company owns significant intangibles and has huge revenues from software products. In this regard, we find that the Bangalore Bench of the Tribunal in the case of M/s. TDPLM Software Solutions Ltd. v. DCIT, ITA No.1303/Bang/2012, by order dated 28.11.2013 with regard to this comparable has held as follows:-

“11.0 Infosys Technologies Ltd. 11.1 This was a comparable selected by the TPO. Before the TPO, the assessee objected to the inclusion of the company in the set of comparables, on the grounds of turnover and brand attributable profit margin. The TPO, however, rejected these objections raised by the assessee on the grounds that turnover and brand aspects were not materially relevant in the software development segment.

11.2 Before us, the learned Authorised Representative contended that this company is not functionally comparable to the assessee in the case on hand. The learned Authorised Representative drew our attention to various parts of the Annual Report of this company to submit that this company commands substantial brand value, owns intellectual property rights and is a market leader in software development activities, whereas the assessee is merely a software service provider operating its business in India and does not possess either any brand value or own any intangible or intellectual property rights (IPRs). It was also submitted by the learned Authorised Representative that :-

(i) the co-ordinate bench of this Tribunal in the case of 24/7 Customer.Com Pvt. Ltd. in ITA No.227/Bang/2010 has held

that a company owning intangibles cannot be compared to a low risk captive service provider who does not own any intangible and hence does not have an additional advantage in the market. It is submitted that this decision is applicable to the assessee's case, as the assessee does not own any intangibles and hence Infosys Technologies Ltd. cannot be comparable to the assessee ;

(ii) the observation of the ITAT, Delhi Bench in the case of Agnity India Technologies Pvt. Ltd. in ITA No.3856 (Del)/2010 at para 5.2 thereof, that Infosys Technologies Ltd. being a giant company and market leader assuming all risks leading to higher profits cannot be considered as comparable to captive service providers assuming limited risk ;

(iii) the company has generated several inventions and filed for many patents in India and USA ;

(iv) the company has substantial revenues from software products and the break up of such revenues is not available ;

(v) the company has incurred huge expenditure for research and development;

(vi) the company has made arrangements towards acquisition of IPRs in 'AUTOLAY', a commercial application product used in designing high performance structural systems.

In view of the above reasons, the learned Authorised Representative pleaded that, this company i.e. Infosys Technologies Ltd., be excluded from the list of comparable companies.

11.3 Per contra, opposing the contentions of the assessee, the learned Departmental Representative submitted that comparability cannot be decided merely on the basis of scale of operations and the brand attributable profit margins of this company have not been extraordinary. In view of this, the learned Departmental Representative supported the decision of the TPO to include this company in the list of comparable companies.

11.4 We have heard the rival submissions and perused and carefully considered the material on record. We find that the assessee has brought on record sufficient evidence to establish that this company is functionally dis-similar and different from the assessee and hence is not comparable and the finding rendered in the case of Trilogy E-Business Software India Pvt. Ltd. (supra) for Assessment Year 2007-08 is applicable to this year also. We are inclined to concur with the argument put forth by the assessee that Infosys Technologies Ltd is not functionally comparable since it owns significant intangible and has huge revenues from software products. It is also seen that the breakup of revenue from software services and software products is not available. In this view of the matter, we hold that this company ought to be omitted from the set of comparable companies. It is ordered accordingly.”

The decision rendered as aforesaid pertains to A.Y. 2008-09. It was affirmed by the learned counsel for the Assessee that the facts and circumstances in the present year also remains identical to the facts and circumstances as it prevailed in AY 08-09 as far as this comparable company is concerned. Respectfully following the

decision of the Tribunal referred to above, we hold that Infosys Ltd. be excluded from the list of comparable companies.

33. KALS Information Systems Ltd.:- . As far as this company is concerned, it is not in dispute before us that this company has been considered as not comparable to a pure software development services company by the Bangalore Bench of the Tribunal in the case of M/s. Trilogy e-business Software India Pvt. Ltd. (supra). The following were the relevant observations of the Tribunal:-

“(d) KALS Information Systems Ltd. 46. As far as this company is concerned, the contention of the assessee is that the aforesaid company has revenues from both software development and software products. Besides the above, it was also pointed out that this company is engaged in providing training. It was also submitted that as per the annual report, the salary cost debited under the software development expenditure was Rs. 45,93,351. The same was less than 25% of the software services revenue and therefore the salary cost filter test fails in this case. Reference was made to the Pune Bench Tribunal’s decision of the ITAT in the case of Bindview India Private Limited Vs. DCI, ITA No. ITA No 1386/PN/10 wherein KALS as comparable was rejected for AY 2006-07 on account of it being functionally different from software companies. The relevant extract are as follows:

46. 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.

47. We have given a careful consideration to the submission made on behalf of the Assessee. We find that the TPO has drawn conclusions on the 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 the TPO, when the same is contrary to the annual report of this company as highlighted by the Assessee in its letter dated 21.6.2010 to the TPO. We also find that in the decision referred to by the learned counsel for the Assessee, the Mumbai Bench of ITAT has 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.”

Following the aforesaid decision of the Tribunal, we hold that KALS Information Systems Ltd. should not be regarded as a comparable.

34. Tata Elxsi Ltd.,:- *As far as this company is concerned, it is not in dispute before us that in assessee’s own case for the A.Y. 2007-*

08, this company was not regarded as a comparable in its software development services segment in ITA No.1076/Bang/2011, order dated 29.3.2013. Following were the relevant observations of the Tribunal:-

II. UNREASONABLE COMPARABILITY CRITERIA : 19. The learned Chartered Accountant pleaded that out of the six comparables shortlisted above as comparables based on the turnover filter, the following two companies, namely (i) Tata Elxsi Ltd; and (ii) M/s. Flextronics Software Systems Ltd., deserve to be eliminated for the following reasons :

(i) Tata Elxsi Ltd., : The company operates in the segments of software development services which comprises of embedded product design services, industrial design and engineering services and visual computing labs and system integration services segment. There is no sub-services break up/information provided in the annual report or the databases based on which the margin from software services activity only could be computed. The company has also in its response to the notice u/s.133(6) stated that it cannot be considered as comparable to any other software services company because of its complex nature. Hence, Tata Elxsi Ltd., is to be excluded from the list of comparables.

(ii) Flextronics Software Systems Ltd. : The learned TPO has considered this company as a comparable based on 133(6) reply wherein this company reflected its software development services revenues to be more than 75% of the "software products and services" segment revenues. Flextronics has a hybrid revenue model and hence should be rejected as functionally different. Based on the information provided under "Revenue

recognition" in its annual report, it can be inferred that the software services revenues are earned on a hybrid revenue model, and the same is not similar to the regular models adopted by other software service providers. The learned representative pleaded that a regular software services provider could not be compared to a company having such a unique revenue model, wherein the revenues of the company from software/product development services depends on the success of the products sold by its clients in the marketplace. Hence, it would be inappropriate to compare the business operations of the assessee with that of a company following hybrid business model comprising of royalty income as well as regular software services income, for which revenue break-up is not available. He finally submitted that this was a good reason to exclude this company also from the list of comparables.

20. On the other hand, the learned DR supported the order of the lower authorities regarding the inclusion of Tata Elxsi and Flextronics Software Systems Ltd., in the list of comparables. He reiterated the contents of para 14.2.25 of the TPO's order. He also read out the following portion from the TPO's order :

"Thus as stated above by the company, the following facts emerge :

1. The company's software development and services segment constitutes three sub-segments i) product design services; ii) engineering design services and iii) visual computing labs.

2. The product design services sub-segment is into embedded software development. Thus this segment is into software development services.

3. *The contribution of the embedded services segment is to the tune of Rs.230 crores in the total segment revenue of Rs.263 crores. Even if we consider the other two sub-segments pertain to IT enabled services, the 87.45% (>75%) of the segment's revenues is from software development services.*

4. *This segment qualifies all the filters applied by the TPO." Regarding Flextronics Software Systems, the following extract from page 143 of TPO's order was read out by him as his submissions :*

"It is very pertinent to mention here that the company was considered by the taxpayer as a comparable for the preceding assessment year i.e., AY 2006-07. When the same was accepted by the TPO as a comparable, the same was not objected to it by the taxpayer. As the facts mentioned by the taxpayer are the same and these were there in the earlier FY 2005-06, there is no reason why the taxpayer is objecting to it. How the company is functionally similar in the earlier FY 2005-06 but the same is not functionally similar for the subsequent FY 2006-07 even when no facts have been changed from the preceding year. Thus the taxpayer is arguing against this comparable as the company was not considered as a comparable by the taxpayer for the present FY 2006-07."

21. *We have heard the rival submissions and considered the facts and materials on record. After considering the submissions, we find that Tata Elxsi and Flextronics are functionally different from that of the assessee and hence they deserve to be deleted from the list of six comparables and hence there remains only four companies as comparables, as listed below:"*

35. *Following the aforesaid decision of the Tribunal, we hold that M/S.Tata Elxsi Lts should not be regarded as a comparable”*

36.As far as **Persistent Systems Ltd.**, a comparable by the Assessee in his TP study but was objected to by the Assessee before TPO as not comparable, this Tribunal in the case of IT(TP) A.No.108(Bang) 2014 order dated 12.12.2014 in the case of Yodlee Infotech Pvt.Ltd. Vs. ITO held as follows:-

“5.12 This Tribunal in the case of 3DPLM Software Solutions Ltd. Vs DCIT [IT(TP)A 1303/Bang/2012 dated 28-11-2013] had also held that Persistent Software Systems Pvt. Ltd., was in product designing services and into software product development. In the same decision it was also held that M/s. Infosys Technologies Ltd, had considerable intangibles like IPR, and was also into software product development. It was also held that M/s. Tata Elxsi Ltd., was developing niche products and into product designing services. Hence, these companies would in any case have to be excluded from the comparables being functionally different.”

37. *Following the said decision we direct that Persistent Systems Ltd., be excluded from the final list of comparable companies chosen by the TPO*

15. We respectfully follow the decision of the coordinate bench of the Tribunal in assessee’s own case and uphold the decision of CIT(A) to exclude (i) Infosvs Ltd.; (ii) Tata Elxi Ltd. (iii) Persistent Systems Ltd.; and (iv) KALS Information Systems Ltd

16. With regard to the exclusion of **ICRA Techno Analytics Ltd.**, we find that the coordinate bench of the Tribunal in the case of Cisco Systems (supra) has held that

ICRA Techno Analytics Limited

7.1 The learned AR submitted that the company is not a pure software development service provider, and based on the observation in the annual report, the company is engaged in providing host of other services such as engineering services, web hosting and also business process outsourcing. According to the AR, no segmental information is available and therefore, the company cannot be retained as comparable. The DRP held that the segmental information is available for two segments i.e., services and sales. However, it is evident from the annual report that the service segment comprises of software development, software consultancy, engineering services, web development, web hosting etc for which no segmental information is available and therefore, the objection of the assessee is found acceptable. Accordingly, the DRP directed the AO to exclude the above company from the comparables.

7.1.1 We have heard rival submissions and perused the material on record. We find that this issue was considered by the Co-ordinate Bench of the Tribunal in the case of DCIT v. M/s.Electronics for Imaging India Pvt. Ltd. In IT(TP)A No.212/Bang/ 2015 for assessment year 2010-2011, vide order dated 24.02.2016, wherein the Tribunal held as under:-

“14. At the outset, we note that apart from having the related party revenue at 20.94% of the total revenue, this company was also found to be functionally not comparable with software development services segment of the assessee. The DRP has given its finding at pages 13 to 14 as under:-

“Having heard the contentions, on perusal of the annual report, it is noticed by us that the segmental information is available for two segments i.e., services and sales. However, it is evident from the annual report that the service segment comprises of software development, software development, software consultancy, engineering services, web development, web hosting, etc. for which no segmental information is available and therefore, the objection of the assessee is found acceptable. Accordingly, Assessing Officer is directed to exclude the above company from the comparables.”

15. We find that the facts recorded by the DRP in respect of business activity of this company are not in dispute. Therefore, when this company is engaged in diversified activities of software development and consultancy, engineering services, web development & hosuign and substantially diversified itself into domain of business analysis and business process outsourcing, then the same cannot be regarded as functionally comparable with that of the assessee who is rendering software development services to its AE.

16. In view of the above facts, we do not find any error or illegality in the findings of the DRP that this company is functionally not comparable with that of a pure software development service provider.”

7.1.2 In view of the decision of the Co-ordinate Bench, cited supra, we direct the AO/TPO to exclude the comparable on similar reasons.”

17. Respectfully following the decision of the coordinate bench we confirm the decision of the CIT(A) to exclude ICRA Techno Analytics Ltd from the list of comparables.

18. The next issue contended by the revenue is with regard to the working capital adjustment which the CIT(A) directed the TPO to allow on actual basis. The TPO during the TP proceedings restricted the WCA to 0.55% for IT segment stating that '*in a related party scenario the entire payable/advances cannot be considered as in any business there is an optimum working capital that can be found out only on the basis of comparison with third parties as third parties alone represent the optimum working capital requirement*'. The CIT(A) on appeal, held that the working capital adjustment should be allowed on actual basis following the decision of the coordinated bench of the Tribunal in assessee's own case supra. The revenue is appeal before the Tribunal contending that the working capital adjustment should not be granted on actual and there should be an upper limit.

19. We heard both the parties and perused the materials on record. We notice that the coordinate bench of the Tribunal in assessee's own case for the assessment year 2009-10 has allowed the working capital adjustment on actual basis where the Tribunal held that

40. *The TPO had restricted the cost of capital to 1.71%. Rationality for such an upper limit being placed on working capital adjustment was an issue which had come up before this Tribunal in the case of M/s. Rambus Chip Technologies (India) P. Ltd v. DCIT [IT(TP)A.23/Ban/2015, dt.22.07.2015. Coordinate bench had held as under at para 13 and 14 of its order:*

“13. As regards ground No.3(f), learned counsel for the assessee submitted that the AO/TPO while considering the working capital adjustment, has arrived at the working capital adjustment in the case of the assessee at 5.97%, but while giving effect to the working capital adjustment, has restricted the said adjustment to 1.71% in case of uncontrolled comparables selected by the TPO. The learned counsel for the assessee submitted that the TPO has not given any basis for such restriction of the working capital adjustment. He submitted that the CIT(A) also has not applied his mind to this issue but has summarily confirmed the order of the AO and therefore it has to be set aside.

14. on going through the TPO’s order as well as annexure D referred to in the transfer pricing order on working capital adjustment, we find that the AO has not given any basis for restricting the adjustment to 1.71%. In all the cases relating to transfer pricing adjustment, this Tribunal has been directing to give working capital adjustment on actual basis and the TPO having arrived at 5.97% ought to have adopted the same instead of restricting it to 1.71%. In view of the same, we deem it proper to remand this issue to the file of the AO/TPO for working out the ALP after giving adjustment of working capital as per the calculation of the AO in annexure D annexed to the transfer pricing order. This ground of appeal is accordingly allowed.”

41. Accordingly we direct the AO/TPO to correctly work out the PLI of the final comparables after giving due adjustment for the working capital on actual basis. Related ground of the assessee is therefore allowed.

20. Respectfully following the coordinate bench of the Tribunal we direct the AO / TPO to consider the working capital adjustment on actual basis while working out the PLI of the final comparables. This ground of the revenue is rejected for statistical purposes.

ITES segment

21. In the ITES segment the assessee had selected below listed 15 comparables.

S.No.	Name of Companies — ITeS Segment	Markup on Total Cost ²
1	A O K In-House BPO Services Ltd	13%
2	Aditva Birla Minacs Worldwide Ltd	8%
3	Cameo Corporate Services Ltd	10%
#4	Cosmic Global Ltd	34%
5	Delta Services (I) Pvt Ltd	7%
#6	Informed Technologies India Ltd	12%
#7	Infosys B P O Ltd	24%
8	K N M Services Pvt Ltd	14%
9	Optimus Global Services Ltd	-2%
10	Sparsh B P O Services Ltd	6%
11	Crossdomain Solutions Pvt Ltd	28%
12	Omega Healthcare Management services Pvt Ltd	9%
13	B N R Udyog Ltd — Medical Transcription	38%
14	In House Productions Ltd	4%
15	Timex Group India Pvt. Ltd	8%
	Average	14%

22. The average net margin of the reflected comparables was at 14% and the OP/TC of to the assessee upon ITES segment was 17.53%. Hence the assessee concluded that the transactions with AE with regard to ITES segment is within the arm's length price.

23. The TPO out of the 15 comparables selected by the assessee accepted only 3 (highlighted) and rejected the balance 12. The TPO applied fresh filters and selected the following comparables the average margin of which worked out to 26.67%.

Particulars	Comparables selected by Ld. TPO		
	Pre WC		Post WC
Accentia Technologies Ltd.	43.06%		39.69%
Acropetal Technologies Ltd. (seg)	22.27%		17.67%
e-clerx Services Ltd.	55.97%		52.98%
Fortune Infotech Ltd.	22.80%		20.05%
ICRA Online Ltd. (seg)	43.39%		40.72%
Informed Technologies India Ltd.	26.15%		25.94%
Infosys BPO Ltd.	31.23%		28.68%
Cosmic Global Ltd.	14.97%		16.20%
Sundaram Business Services Ltd.	-12.31%		-13.28%
Jeevan Scientific Technology Ltd. (seg)	21.05%		37.99%
Average margin	26.86%		26.67%

24. Thus the AO computed the TP adjustment as per below workings:-

Adjusted margin (post working capital adjustment)	26.67%
Taxpayer operating cost ('OC')	Rs. 147,51,13,176
Arm's length price (126.66% of OC)	Rs. 186,85,25,860
Price received	Rs. 165,11,30,616
Shortfall being adjustment u/s. 92CA	Rs. 21,73,95,244

25. On appeal before the CIT(A) the assessee contended the inclusion by the TPO. The CIT(A) partly allowed the contentions of the assessee whereby he deleted the inclusion of (i) Infosys BPO and

(ii) E-Clerx Services Ltd. relying on the decision of the co-ordinate bench of the Tribunal in assessee's own case.

26. The CIT(A) confirmed the inclusion of the below comparables of the TPO.

- a. ICRA Online Ltd.,
- b. Acropetal Technologies Ltd.,
- c. Accentia Technologies Ltd.,
- d. Fortune Infotech Ltd.,

27. The assessee is in appeal before us for the above inclusions **(Ground No. 1 to 4 of Consolidated Grounds of Appeal filed by the assessee on 23.11.2021 vide letter dated 15.07.2021)**

28. The revenue is appeal for the exclusion of (i) Infosys BPO and (ii) E-Clerx Services Ltd **(Ground No. 1 to 6 of Department Grounds of Appeal).**

29. We shall take up for consideration the grounds raised regarding exclusion of comparable companies. In the case of M/s UL India Pvt. Ltd. Vs. DCIT (IT(TP)A No.574/ & 378/Bang/2015 order dated 24.2.2022 exclusion of all these companies was considered by this Tribunal and excluded. The relevant extract from the decision of the Tribunal -

“24.With regard to exclusion of **Acropetal technologies Ltd**, we find that the expenses incurred on on-site provision of ITeS by the Assessee was 64% of the total expenses and therefore the company was to be regarded as one providing onsite ITeS and cannot be compared with a company providing offshore ITeS such as the Assessee. Secondly the employee cost is less than 25% of the total cost of the company. ITeS services essentially involve and predominantly dependent on employees and therefore wherever the employee cost is less than 25% of the total cost, then the company cannot be regarded as providing ITeS. Therefore, we direct the Assessing Officer to apply 25% employees cost filter and accordingly exclude Acropetal Technologies Limited.

25. With regard to exclusion of **ICRA Online Ltd.**, we find that ICRA is engaged in providing services which are in the nature of Knowledge Process Outsourcing (KPO) services. It provides financial and analytical services and support to clients in the area of Data Extraction, Aggregation, Electronic Conversion of Financial statements, Validation and Analysis, Accounting and Finance, Research and Analytics which are dissimilar to the services rendered by the Assessee. The outsourced services segment of the company is engaged in the provision of high end consultancy services which cannot be compared to the assessee who is into provision of low end IT enabled services which are routine in nature. Further, the safe harbour rules clearly distinguish between an ITE service provider and a KPO service provider. This Tribunal has held that a KPO service provider cannot be compared to an ITE service provider. Reliance in this regard is placed on the decision in the case of Arctern Consulting Pvt. Ltd. (supra) IT(TP)A No.195/Bang/2015 & 302/Bang/2015 Order dated 11.08.2017 for AY 2010-11, & in the case of Outsource Partners International (P) Ltd. I.T(TP)A No.337/Bang/2015 Order dated 6.2.2017 for AY

2010-11, wherein on identical circumstances, the exclusion of this company came to be upheld/the company was directed to be excluded. In the case of *Outsources Partners International (P) Ltd.*, (supra), this Tribunal has adjudicated identical issue and held that this company was not functionally comparable to an ITeS company such as the Assessee and for the reason that this company fails the export earning filter. Respectfully following the said decision, we uphold exclusion of this company from the list of comparable companies for the reasons given in this paragraph.

26. As far as **Accentia Technologies Ltd.**, is concerned, we find that this company has been held to be not Functionally not comparable and as a Product development company with Presence of Intellectual Property rights (Approx.57% of the net fixed assets) and with extraordinary events during the year relevant to AY 2010-11 and the segmental data not being available, in the case of & in the case of *Outsource Partners International (P) Ltd. I.T(TP).A No.337/Bang/2015 Order dated 6.2.2017 for AY 2010- 11. Hence, we direct exclusion of the company Accentia Technologies Ltd., from the list of comparable companies.*

27. As far as **Fortune Infotech Ltd.**, is concerned in the case of *Outsource Partners International Pvt. Ltd. (supra)* this company was held to be Functionally not comparable being a Product development company with Presence of Intellectual Property rights (Approx.57% of the net fixed assets) and with related party transactions (RPT) of more than 25%. Hence, we direct exclusion of this company from the list of comparable companies”.

30. We respectfully follow the decision of the coordinate bench of the Tribunal and direct the AO / TPO to exclude (i) ICRA Online

Ltd., (ii) Acropetal Technologies Ltd.,(iii) Accentia Technologies Ltd.,
(iv) Fortune Infotech Ltd.,

31. The CIT(A) gave direction to the TPO to grant working capital adjustments on actual basis in both IT Segment and ITES segment. The TPO while giving effect to the said order provided negative working capital adjustments to the ITES segment. The assessee is in appeal against the negative working capital adjustment before the Tribunal.

32. With regard to the negative working capital adjustment the Ld.AR submitted that the assessee is a captive service provider and does not been any working capital risk. The Ld.AR placed reliance on the decision on the coordinate bench of the Tribunal in the case of Tivo Tech Pvt. Ltd. (2020) 17 Taxxmann.com 259 (Bang ITAT)

33. The Ld.DR supported the decision of the TPO. We heard the rival submissions and perused the materials on record. We notice that the coordinate bench of the Tribunal in the case of Tivo Tech (Supra) has dealt with a similar issue and held that

“15. As far as Gr.No.2.6 is concerned, the Assessee has contended that the TPO and the DRP erred in adding to the average arithmetic profit margin of the comparable companies chosen by the TPO, negative working capital adjustment. It was submitted that Working capital adjustment is made for the time value of money lost

when credit time is given to the customers. The Assessee however is not an entrepreneur but a captive service provider which is entirely funded by the AEs. This being so, the assessee does not stand to lose anything as it is compensated on a total cost plus basis. The assessee is running the business without any working capital risk as compared to the comparables. Therefore, requirement for adjustment of negative working capital does not arise. It was submitted that in the Assessee's own case for assessment year 2012-13, the CIT(A) has reversed the order of the TPO making negative working capital adjustments. Detailed submissions in this regard are placed at pages 154-155 and 333-337 of the paperbook.

16. The Assessee also places reliance on Digital Juice Animation (P.) Ltd. v. Assu. CIT [order dated 6-2-2020 in IT(TP)No. 215/Bang/2017], Lam Research India (P.) Ltd. [IT Appeal No. 1473 & 1385 (Bang.) of 2014, order dated 30-4-2015] and Dy. CIT v. Software AG Bangalore Technologies (P.) Lid. in [IT Appeal No, 1628 (Bang.) of 2014. order dated 31-3-2016] passed by this Hon'ble Tribunal, where it has been held that negative working capital adjustment shall not be made in case of a captive service provider as there is no risk and it is compensated on a total cost plus basis. The Tribunal in the aforesaid decisions have followed decision of ITAT Hyderabad Bench in the case of Adaptec (India) (P.) Lid. v. Assti. CIT 120151 57 taxmann.com 307. The learned DR relied on the order of the TPO/DRP on the issue.

17. On the above ground. it is undisputed that the Hyderabad Bench of the JTAT in case of Adaptec (India) (P.) Ltd. (supra) held that no such addition call made for the following reasons:-

“Ground No. 8 pertains to the issue of negative working capital. As briefly stated above, after arriving at the arithmetic mean of

all comparables at 22.03%, the A.O. worked out negative working capital adjustment of 3.22% thereby, making arms length price at 25.25%. Even though, DRP refused to interfere with the objections of the assessee in its order, we were informed that DRP has directed the TPO/A.O. not to make any negative working capital adjustment in some of the cases in the next assessment year. in the cases of Market Tools Research P. Ltd.. and Mega Systems Worldwide India P. Ltd.. assessee placed on record copies of orders of DRP. In that DRP considered the issue and directed the TPO as under

14. Ground No. 11 Negative Working Capital adjustment - Making a negative working capital adjustment without appreciating the fact that the company does not bear any working capital risks. On this issue, the assessee submitted as under :-

"The learned TPO determined the ALP for the international transactions with A.Es by making a negative working capital adjustment for the differences in working capital between the assessee and the companies considered as comparables. The assessee does not agree with the learned TPO as the company does not bear any working capital risk since it is been fully funded by its A.E. from its inception and has no working capital contingencies. The company has never taken any loans till date from the date of incorporation nor has incurred any expense for meeting the working capital requirement."

We have gone through the submissions and the order of the TPO. The assessee pleaded that the DRP has acceded such a plea in some other case. On examination, we find that the DRP, Hyderabad in the case of Cordys Software India P. Ltd., for A.Y.

2008-09 in its directions dated 3-8-2012 has given a finding as under:-

"7.7.4 Thus, working capital adjustment is made for the time value of money lost when credit time is provided to the customers. The applicant is not an entrepreneur but a captive service provider. Its entire funding needs are provided by the A.E. This being so, the applicant does not stand to lose anything as it is compensated on a total cost plus basis. The TPO probably was carried away by the large amount of receivables appearing in the books of the applicant. But the applicant is running its business without any working capital risk while comparable companies have such a risk for them. If at all any working capital adjustment is to be made to this situation, only a positive adjustment has to be made to the comparables so that they are brought on par with the applicant. In view of the same, the Panel directs that negative working capital adjustment to the arithmetic mean margin of the comparables shall not be made." In view of the above, the Panel directs that negative working capital adjustment to the arithmetic mean margin of the comparables shall not be made.

18. In view of the above, we are of the opinion that assessee's case being similar, there is no need for making any negative working capital adjustment when assessee does not carry any working capital risk. In fact. TPO should have done necessary working capital adjustment to the profits of the selected comparables so as to make them comparable to the assessee. In view of this, we direct the TPO not to make negative working capital adjustment.

34. In view of the above decision of the coordinate bench of the Tribunal we hold that the negative working capital adjustment shall not be made. The AO is directed accordingly.

35. With regard to the grounds raised by the revenue with regard to exclusion of Infosys BPO Ltd and E-clerx Services Ltd, the coordinate bench of the Tribunal in assessee's own case has confirmed the exclusion and held that –

Infosys BPO Ltd :

47. The comparability of this company with an ITES company was considered by this Tribunal in the case of Symphony Marketing Solutions India P. Ltd v. ITO (IT (TP))a no.1316/Bang/2012 for AY 2008-09 order dt 14.08.2013. This Tribunal in para 24 of its order, on considering this company as a comparable held as follows:-

"This company is listed at sl. 13 in the list of comparable companies chosen by the TPO. As far as this company is concerned, it is the submission of the learned counsel for the assessee that this company has a brand value and therefore there would be significant influence in the pricing policy which will impact the margins. Schedule 13 to the profit and loss account of this company for the F.Y. 2007-08 shows that this company incurred huge selling and marketing expenses. Page 133 of the annual report of this company for the F.Y. 2007-08 shows that this company realizing its brand value has chosen to value the same on the basis of its earnings and that of Infosys. The brand value of the Assessee and Infosys has been valued at Rs.31,863 crores. Infosys BPO, being a subsidiary of Infosys, has an element of brand value associated with it. This is also clear from the presence of brand related expenses incurred by

this company. Presence of a brand commands premium price and the customers would be willing to pay, for the services/products of the company. Infosys BPO is an established player who is not only a market leader but also a company employing sheer breadth in terms of economies of scale and diversity and geographical dispersion of customers. The presence of the aforesaid factors will take this company out of the list of comparables. We therefore accept the contention of the assessee that this company cannot be regarded as a comparable."

48. Following the aforesaid decision of the Tribunal and taking note of the fact that the facts and circumstances in the case of the assessee for the current assessment year are identical, we direct that Infosys BPO be excluded as a comparable.

Eclerx Services Ltd., :

53. The comparability of this company in ITES segment was considered by the Special bench decision of the ITAT in the case of Maerks Global (supra) and the Special Bench in para 82 and 83 of its order came to the conclusion that this company was functionally different and was accordingly engaged in providing high end services involving specialized knowledge and domain expertise in its field. Following the aforesaid decision we are of the view that this company should be excluded from the final list of comparables."

36. We respectfully follow the decision of the coordinate bench of the Tribunal and confirm the decision of the CIT(A)

37. The TPO is accordingly directed to compute the ALP in the IT and ITES segment in the light of the directions given above

38. In the result, the appeal of the assessee is allowed and the appeal of the revenue is dismissed

Order pronounced in court on 17th day of May, 2022

Sd/-

(N.V VASUDEVAN)
Vice President

Sd/-

(PADMAVATHY S)
Accountant Member

Bangalore,
Dated, 17th May, 2022
/ vms /

Copy to:

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

By order

Assessment Registrar, ITAT, Bangalore.