

**IN THE INCOME TAX APPELLATE TRIBUNAL
“A” BENCH : BANGALORE**

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

ITA Nos.555/Bang/2017 & 3279/Bang/2018
Assessment years : 2010-11 & 2011-12

The Deputy Commissioner of Income Tax, Circle 1(1), Pune.	Vs.	M/s. Capgemini Technology Services India Ltd. [formerly AXA Group Solutions Pvt. Ltd.], P.M.T. Building, Swargate, Shankarshet Road, Pune – 411 037. PAN: AABCM 4573E
APPELLANT		RESPONDENT

Appellant by	:	Shri Sankar Ganesh, Jt.CIT(DR)(ITAT), Bengaluru.
Respondent by	:	Smt. Tanmayee Rajkumar, Advocate.

Date of hearing	:	23.05.2022
Date of Pronouncement	:	30.05.2022

ORDER

Per Padmavathy S., Accountant Member

These appeals are at the instance of revenue directed against the order of the CIT(Appeals)-1, Bengaluru dated 08.11.2016 for the AYs 2010-11 & 2011-12. Common issues are involved in these appeals which were heard together and are disposed of by this consolidated order for the sake of convenience and brevity.

2. The assessee is a subsidiary of AXA Group Solutions SA, France (AE). The assessee offers Software Development Services and Admin Support Services. The assessee is remunerated on a time cost or fixed price basis for the works assigned by AXA Group. The details of international transaction as per 3CEB is as given below:-

International Transactions as per 3CEB Report

Sl. No.	Transaction	Amount in Rs.	
		AY 2010-11	2011-12
1.	Receipt from contract software development service	32,19,53,880	34,72,71,221
2.	Payment for administrative support services	1,41,08,690	48,71,308
3.	Management fees paid	2,17,38,508	1,77,93,277
4.	Reimbursement of FBT	2,58,120	-
5.	Reimbursement of expenses received	1,83,28,390	56,86,792
6.	Training expenses paid	-	1,99,177
7.	Other expenses paid	-	60,743

3. As per the TP documentation, for the provision of Software Development Services and Admin Support Services the assessee has applied Transaction Net Margin Method (TNMM) as the most appropriate method for determining the arm's length price for the services rendered and considered the mark-up on total cost i.e. Operating profit / Total cost as the relevant profit level indicator (PLI).

4. The assessee company filed the return of income for the assessment year 2010-11 on 27.09.2010 declaring an income of Rs.2,73,35,297/- after claiming deduction u/s.10A. The assessee has paid the tax based on the deemed total income u/s.115JB. The return was processed u/s.143(1) of the Income Tax Act (the Act) and through

CASS the case was selected for scrutiny. The assessing officer (AO) referred the case to Transfer Pricing Office (TPO) u/s.92CA as the assessing had international transactions. The TPO accepted the ALP towards all transactions but made an adjustment towards ALP of management fees for an amount of Rs.2,17,38,508. The AO passed an assessment order incorporating the TP adjustment and also made other additions / disallowances towards the following:-

- a. Adjustment to export turnover towards telecommunication and travel expenses in foreign currency – Rs.4,97,940
- b. Disallowance u/s.14A r.w.r.8D – Rs.13,19,449
- c. Disallowance of software expenses treating the same as capital expenditure - Rs.7,70,913

5. The assessee preferred an appeal before the CIT(A) against the order of the AO. The CIT(A) gave substantial relief to the assessee by deleting all the additions / disallowances made by the AO except the disallowance u/s.14A r.w.r.8D. The assessee did not prefer any further appeal whereas the revenue is in appeal before the Tribunal against the relief given by the CIT(A)

6. The effective grounds raised by the revenue for AY 2010-11 are reproduced below:-

“ALP Adjustment:

2. The Ld. CIT(A) erred in deciding the facts of the case by following an APA agreement between CBDT and a different taxpayer when such agreements are applicable only to a specific set of facts.

3. The Ld. CIT(A) erred in facts & law in deciding the case without adjudicating on the TPO's arguments that neither supporting documents nor reasonable explanation (or) benefit analysis had been submitted before the TPO, to validate the payment of management fees.

Corporate tax issues:

4. The Ld. CIT(A) erred in directing that the expenditure reduced from the export turnover i.e. expenditure of Rs. 13,63,422/- towards telecommunication and Travel expenses in foreign currency, be also reduced from the Total Turnover for computing the deduction allowable u/s 10A of the Act following the ratio laid down by the Hon'ble High Court of Karnataka in the case of Tata Elxsi Limited in (2012) 349 ITR 98 (Kar), without appreciating the fact that there is no provision in Section 10A that such expenses should be reduced from the 'total turnover' also, as Clause (iv) of the Explanation 2 to Section 10A provides that such expenses are to be reduced only from the 'export turnover'.

5. The Ld. CIT(A) erred in not appreciating the fact that the jurisdictional High Court's decision in the case of Tata Elxsi Limited in (2012) 349 ITR 98 (Kar) has not been accepted by the department and an appeal has been filed before the Hon'ble Supreme Court, hence not reached finality.

6. The Ld. CIT(A) erred in directing the AO to work out the relevant depreciation with regard to software expenses and allow the same thereby allowing the alternative claim of the assessee, as the AO has brought out in the assessment order that from the details furnished by the assessee the software were purchased on the last day of the FY 2009-10 and the assessee had not produced necessary bills/vouchers for the said purchase and documents to prove that the software were put to use on the same day, also due to the AO's observation in the assessment order that the said

expense is to be disallowed u/s 40(a)(ia) of the I T Act for failure to deduct TDS.”

ALP adjustment of management fees

5. The assessee has made a payment of management fees of Rs.2,17,38,508 for the AYs 2010-11 respectively. This was aggregated with the primary transaction of software development and administrative support services for bench marking purposes. The assessee submitted before the TPO stating that management fee is paid to the AE towards the charges for AE’s employees time spent on providing services in the nature of advise, technical and other assistance in terms of technical operations in terms of agreement entered into by the assessee with its AE and furnished invoices and agreements in support of its claim. The TPO, however, was of the view that international transaction for payment of management fees is a class of its own and the ALP of the transaction cannot be determined using TNMM and proceeded to calculate the ALP in respect of this transaction separately using CUP method. The TPO concluded that the assessee’s submissions are nothing more than a description of certain alleged services received by it from its AE and the documents filed do no prove that the services have been rendered and the assessee has derived tangible substantial and commercial benefit out of such services from its AE. Therefore, the TPO computed the ALP at NIL and made TP adjustment of Rs.2,17,38,508 & Rs.1,77,93,277 for these years.

6. Aggrieved, the assessee preferred appeal before the CIT(A) with the submission that –

- a. The assessee had merged with AXA Technologies Shared Services Pvt. Ltd. [AXA-TSSPL] w.e.f. 1.4.2012. and the merged entity AXA-TSSPL that has entered into APA with the CBDT according to which the payment of management fees is part of the operating cost.
- b. This payment of management fees which was part of the APA continued thereafter.
- c. As per the APA, the CBDT has accepted that the payment of management fees by AXA-TSSPL to its group entity is closely linked with the primary transaction of provision of services and hence the same should be tested using the combined approach at the entity level for arriving at the arm's length conclusion.
- d. This principle has also been accepted by the Bangalore ITAT in the case of AXA-TSSPL in *IT(TP)A No.659/Bang/2012 for the AY 2007-08*
- e. The transfer pricing methodology in the APA is to be applied to treat the transaction as at arm's length.

7. The CIT(A) directed the TPO/AO to recalculate the TP adjustment in terms of TP agreement with the CBDT for AYs 2010-11 & 2011-12 in favour of the assessee by observing as under:-

“4.2 Considering the Advance Pricing Agreement dated 28.3.2016 and the observations of the Hon'ble ITAT, Bangalore directing the TPO/AO to reconsider the same in terms of the above observations and it would be in fitness of

things that the TPO/AO has to recalculate the Transfer Pricing Adjustments in terms of the Transfer Pricing agreement by the Hon'ble CBDT for the AYs 2010-11 and 2011-12. To this extent this ground of appeal is allowed.”

8. The revenue is in appeals before us, aggrieved by the order of the CIT(A). The Id. DR submitted that the main reason for adjustment by the TPO is that the assessee has not proved the services have actually been rendered by the AE and the assessee has derived tangible commercial benefit out of the services from the AE. The Id. DR also submitted that the TPO is justified in treating the payment of management fees as a separate transaction as the APA entered into CBDT is with the AXA Shared Services Private Limited which is the merged entity and that as per the terms of clause (2) of the APA entered into by the assessee, the roll back provision is not applicable to the assessee. The Id. DR further submitted that the assessee has not submitted anything to the contrary to show that it is an integral part of the overall software services rendered by the assessee.

9. The Id. AR submitted that though the roll back provision is not applicable to the assessee as per the APA entered into by the merged entity, the CBDT in the said agreement has considered the management fees as part of the operating cost and the management fees which was continued to be paid in the subsequent assessment years and considered to be an integral part of the primary transaction as per the APA. The Id. AR therefore argued that the same principle should be applied for the assessment year under consideration based on the fact that there is no change to the nature of payment of

management fees. The Id AR submitted that the assessee has submitted all the relevant documents relating to payment of management fees which the TPO did not take into consideration. The Id AR relied on various judicial pronouncements to submit that the TPO ought not to have computed the ALP at NIL and making the TP adjustment for the entire payment made towards management fees.

10. We have considered the rival submissions and perused the material on record. 'Operating Expenses' in the APA has been defined in clause 1(d) as under:-

“(d) "operating expense" means the costs incurred in the previous year by the Applicant in relation to the covered transaction during the course of its normal operations including net foreign exchange difference (if loss) (includes mark to market loss on forward contracts), reimbursement of employee cost, depreciation and amortization expenses relating to the assets used by the Applicant, but does not include the following namely: –

- (i) interest expense;
- (ii) provision for unascertained liabilities;
- (iii) pre-operating expenses;
- (iv) extra-ordinary expenses;
- (v) loss on transfer of assets or investments;
- (vi) expense on account of income-tax; and
- (vii) other expenses not relating to normal operations of the Applicant.

The operating expense includes:

- (i) Expenses and/or depreciation in regard to the assets including third party software licenses provided by the AEs to the Applicant free of cost;

- (ii) Costs in regard to the employee stock option plan (ESOP) or similar scheme granted by the AEs to the employees of the Applicant as and when incurred by the AEs and whether or not recovered from the Applicant;
- (iii) Costs in regard to any stock based compensation/incentive paid to its employees by the Applicant;
- (iv) Any reimbursement of expenses by the Applicant to the AEs(which the AEs have incurred on behalf of the Applicant);
- (v) Inter-company charges as defined in section 3; and
- (vi) Any recovery of expenses by the Applicant from the AEs (which the Applicant has incurred on behalf of the AEs). Recovery of expenses by the Applicant from AEs includes travel, accommodation and any other related expenses of the Applicant's employees travelling overseas to AEs' locations incurred by the Applicant on behalf of the overseas AEs at the request of the AEs.”

9. The assessee has paid management fees amounting to Rs.2,17,38,508 to AXA GS SA during the year under consideration. This management fees is charged by the AE for services rendered towards the following:-

- (i) Technical and operational expertise in the nature of advise and technical assistance for delivery of customer services based on the best practices.
- (ii) Administration, Human Resources and Corporate Communication services regarding the implementation and coordination of general policy and remuneration practices, data processing systems, technological watch on the evolution of remuneration and training methods

- (iii) Advise and technical assistance on development of consistent audit methods
- (iv) Assistance regarding the consolidation of financial results, accounts planning and accounting norms implementation.
- (v) Legal advice regarding contract drafting and negotiation assistance in corporate legal matters.

These are intra-group services and the fee is charged by the AE as per the agreement entered into with the assessee. The contention of the assessee is that these services are rendered with an object to bring consistency of operating policies, standardization of business procedures to bring in efficiency and the assessee is benefitted from both economic and commercial perspective.

11. The assessee has merged with AXA Tech with effect from 1st April 2012 and the merged entity AXA Technologies Shared Services Private Ltd., has entered into an Advance Pricing Agreement (APA) with CBDT commencing from the previous year 2013-14 to previous year 2017-18 (relevant to AY 2014-15 to 2018-19) and also applicable to consecutive four rollback years from previous year 2009-10 to 2012-13. Though as per the term of agreement (page 6 of APA) the international transactions of the assessee is not covered roll back years the previous years beginning from previous year 2013-14, the international transactions of the assessee are covered from the previous year 2013-14 to previous year 2017-18 (relevant to AY 2014-15 to 2018-19).

12. In the APA agreement, the impugned payment i.e., Management fee is considered as part of operating expenses (page 14 of the APA). It was the contention of the assessee that the CBDT has accepted that the payments of management fees by AXA Tech to its group entity as closely

linked with primary transaction of provision of services and to be tested using the combined approach at entity level. Though as per the term of agreement (page 6 of APA) the international transactions of the assessee is not covered roll back years, it is inferred from the APA that the principle of management fees being part of the operating expenses and be tested at entity level. The APA is entered into by CBDT after the thorough verification of the nature of transaction of the assessee and therefore in our considered view, the principle inferred can be applied for the year under consideration also. We also notice that the coordinate bench of the Tribunal in the case of *AXA Technologies Shared Services Private Limited [IT(TP)A/659/Bang/2012]* for the assessment 2007-08 has considered the same issue and has remanded the issue back to AO/TPO for fresh adjudication considering management fees payment to AE to be tested at an entity level using the combined approach. The relevant extract of the decision of Hon'ble Tribunal is reproduced below :-

“9. We have considered the rival submissions as well as the relevant material on record. We find that the assessee bench marked its international transactions by computing the operating margin at entity level which is not as per the provisions of Transfer Pricing because the international transactions has to be tested by comparing with uncontrolled and unrelated price. When the assessee earns the revenue of more than 50% from the non-AE clients then the bench marking of the international transactions by taking the results at entity levels is not appropriate therefore we do not approve such methodology applied by the assessee in bench marking the international transactions. However the TPO has segregated the ITES from management fees and found that the international transactions of ITES exclusive of management fees at arm's length. The action of the TPO in determining the ALP of management fees at NIL is not justified because the assessee has paid the management fees under the agreement wherein the services provided by the AE has been enlisted. Therefore, without giving a finding that the assessee has also incurred expenditure in respect of the same

services over and above the management fees paid to the AE it cannot be said that the assessee has not received the alleged management services. Thus only when it is found that the assessee has also incurred the expenditure on account of the same services and also paid the management fees to the AE then the TPO/A.O may come to the conclusion that the assessee has paid the management fees without availing the services from the AE. Even otherwise when the management fees paid under the agreement and there is no finding by the authorities below that the same services also availed by the assessee separately from 3rd party and booked the expenditure in the profit and loss account then determination of the ALP at NIL is not acceptable. The assessee has filed the agreement under which the management fees was paid to the AE along with the relevant record and the department has accepted the management fees along with ITES under the Advance Pricing Agreement dt.28.3.2016 then making a separate adjustment by the TPO by determining the ALP of management fees at Nil is contrary to the stand of the department itself while agreeing to the advance pricing agreement. We find in the Advance Pricing Agreement dt.28.3.2016, the department has accepted the international transactions recorded in Clause 3 at arm's length as under :

"3. Covered Transaction.

The international transactions of provision of Information Technology Infrastructure and IT support services. Intercompany charges including -

- Payment of management fees
- Payment of business consultancy charges
- Payment of guarantee commission
- Payment of other expenses such as communication expenses, contractor expenses, repairs and maintenance and transversal charges
- Payment towards people soft maintenance
- Payments towards internet charges and software expenses
- Training expenses
- Software expenses
- Payments towards service charges
- Payments towards web hosting and maintenance

- Any other inter-company charge of similar nature

Between the appellant and its AEs, as described in Appendix I, shall be the covered transactions for the Agreement and the Agreement shall apply only to these international transactions."

Though the price accepted by the department under said agreement are not applicable for the year under consideration however, on principle the management fees is accepted along with the other service and the ALP for ITES as well as other services including the payment of management fees has to be determined on composite transaction basis. The TPO has not examined the matter by considering the management fees as part of the operating cost for the purpose of testing the ITES as per provisions of section 92 of the Act. Accordingly, we set aside the matter to the record of the TPO/A.O for reconsideration of the same afresh in terms of the above observations."

13. From the above it becomes clear that the principle laid down by the Tribunal is that though the terms of APA agreement is not applicable for the year under consideration, the payment of management fees has to be determined on composite transaction basis.

14. The other contention of the revenue is that that the assessee has not proved that the services have actually been rendered by the AE and that the assessee had a tangible, substantial and commercial benefit out of the said services. We notice that the assessee during the course proceedings before the TPO and CIT(A) has shared the invoices, agreement copies etc. The TPO has rejected these documents and proceeded to assess the ALP at NIL without calling for any further details from the assessee to substantiate that the assessee has derived substantial and commercial benefit out of the services rendered by the AE.

In view of the above discussion and following the principle laid down by the coordinate bench of the Tribunal in the case of AXA Technologies Shared Services Private Limited (supra) in our considered view for the purpose of ALP the management fees is to be considered on a composite transaction basis. Since the AO/TPO has not considered management fees as part of operating cost for the purpose of testing ALP, it is only appropriate to remand the issue back to the AO/TPO to examine the issue afresh in accordance with the law after giving reasonable opportunity of being heard to the assessee. The assessee is directed to cooperate with the proceedings by producing the relevant documents as and when called for. This issue raised by the revenue is dismissed and allowed in favour of the assessee for statistical purposes for both the year under appeal.

15. The next issue is disallowance of deduction u/s.10A of the Act claimed by the assessee. During the FY 2009-10, the assessee incurred telecommunication and travel expenses in foreign currency amounting to Rs.13,63,422 attributable to delivery of software outside India. The AO reduced this expenditure from the export turnover, but did not reduce the same from the total turnover on the ground that normal definition of 'total turnover' has to be adopted and as such the expenses reduced from export turnover cannot be reduced from the total turnover as well.

16. Before the CIT(Appeals), the assessee contended that this issue has been decided by the coordinate Bench of the Tribunal in the case of

AXA-TSSPL for the AY 2006-07 which is confirmed by the Hon'ble High Court of Karnataka. The CIT(Appeals) allowed this ground of the assessee, against which the revenue is in appeal before us.

17. The ld. DR supported the order of the AO.

18. After hearing both the parties, we find that this issue is covered in favour of the assessee by the Hon'ble Supreme Court in the case of *CIT v. HCL Technologies Ltd. 404 ITR 719 (SC)* wherein it was held that when object of formula in section 10A for computation of deduction is to arrive at profit from export business, expenses excluded from export turnover have to be excluded from total turnover also; otherwise, any other interpretation makes formula unworkable and absurd and hence, such deduction shall be allowed from total turnover in same proportion as well. This ground of the revenue is therefore dismissed for both the yeas under appeal.

19. The next issue for consideration is with regard to treatment of software expenditure as capital in nature by the AO. The assessee submitted before the AO that the software expenditure pertains to application software and regular maintenance services which are revenue in nature. However, the AO proceeded to make the disallowance on the ground that the software provides enduring benefit to the assessee and hence to be treated as capital in nature and has also not allowed depreciation stating that the assessee has purchased the assets on the last day of the financial year 2009. The AO further stated in the order that in case the issue is held in assessee's favour by any of

the Higher Appellate Authority, the total expenses of software is to be disallowed u/s.40(a)(ia) of the Act for failure to deduct tax at source.

20. The CIT(A) confirmed the treatment of software expenditure as capital in nature. He, however, directed the AO to work out the depreciation on the software expenses so capitalized and allow the alternative claim of the assessee. The revenue is in appeal aggrieved by the order of the CIT(Appeals).

21. The ld. DR supported the order of the AO.

22. The ld AR submitted that the software expenses are towards purchase of software licenses which are outcome of new technology assist in running the existing business of the assessee and hence is deductible u/s.37(1). Against the non-allowance of depreciation the ld.AR submitted that the software was purchased on April 7, 2009 and March 31 2010 and put to use on the respective dates. Therefore as an alternate plea, the ld. AR submitted that the depreciation should be allowed in accordance with provisions of section 32 of the Act. The ld AR further submitted that in case the disallowance of software expenses is sustained, then the consequential impact on the deduction u/s.10A needs to be given to the assessee.

23. We have heard both the parties and perused the material on record. The AO has not allowed the depreciation on the software expenses treated as capital in nature on the ground that the same is purchased on the last date of the financial year and that the same would

not have been put to use. We see no merit in such argument and even if the assessee has used the asset for one day, the assessee is entitled for 50% of the applicable rate of depreciation as per section 32 of the Act. We therefore direct the AO to allow depreciation on the software purchased as per the provisions of the law and based on the evidences submitted by the assessee in this regard. The assessee may be given a reasonable opportunity of being heard.

24. On the ground raised by the revenue that the said expenses is to be disallowed u/s.40(a)(ia), we notice that the issues covered by the decision of Hon'ble High Court of Karnataka in the case of *PCIT v. Tally Solutions Pvt. Ltd., [2021] 123 taxmann.com 21* and hence we see no reason to interfere with the decision of the CIT(A) to allow depreciation on the Software purchased. This ground of the revenue is dismissed for both the years under appeal.

25. In the result, the appeals of the revenue are dismissed.

Pronounced in the open court on this 30th day of May, 2022..

Sd/-

(N V VASUDEVAN)
VICE PRESIDENT

Sd/-

(PADMAVATHY S)
ACCOUNTANT MEMBER

Bangalore,
Dated, the 30th May, 2022.

/Desai S Murthy /

Copy to:

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

By order

Assistant Registrar
ITAT, Bangalore.