

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

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

<b>IT(TP)A No. 2570/Bang/2019</b>
<b>Assessment Year : 2015-16</b>

M/s. Xchanging Solutions Ltd., (A DXC Company), Finance Department, 1 <sup>st</sup> Floor, Times Block, HP Avenue, 39/40, Electronics City, Hosur Road, Bangalore – 560 100. <b>PAN: AAFCS9303L</b>	<b>Vs.</b>	The Deputy Commissioner of Income Tax, Circle – 7(1)(2), Bengaluru.
<b>APPELLANT</b>		<b>RESPONDENT</b>

Assessee by	:	Shri Padam Chand Khincha, CA
Revenue by	:	Shri Sumer Singh Meena, CIT DR-1

Date of Hearing	:	03-08-2022
Date of Pronouncement	:	16-08-2022

**ORDER**

**PER BEENA PILLAI, JUDICIAL MEMBER**

Present appeal is filed by assessee against final assessment order dated 23/10/2019 passed by the Ld.DCIT, Circle – 7(1)(2), Bangalore on following grounds of appeal:

*“Based on the facts and circumstances of the case and in law, Xchanging Solutions Limited (hereinafter referred to as "XSL" or the "Company" or the "Appellant"), respectfully craves leave to prefer an appeal against the order passed by the Deputy Commissioner of Income-tax, Circle - 7(1)(2) (the "learned AO"), dated 23 October 2019 for the*

Assessment Year ("AY") 2015-16. under section 143(3) read with section 144C(13) of the Income-tax Act, 1961 ("the Act") in pursuance of the directions issued by Dispute Resolution Panel ("Hon'ble DRP"), Bangalore dated 09 September 2019 under section 144C(5) of the Act ("impugned order") inter-alia on the following grounds:  
That on the facts and circumstances of the case and in law:

General

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

2. The learned AO has erred in making adjustments/disallowances aggregating to INR 11,94.62,783 to the returned income and thereby has erred in law and on facts in assessing the total income of the Appellant at INR 24,38,80,173.

3. The learned AO has erred in laws and in facts, in determining a sum of INR 6,06,03,330 as the balance tax (including interest) demand payable by the Appellant.

4. Transfer Pricing grounds

4.1 The learned DRP/AO/TPO erred in making an addition of INR 11,03,17,720 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 enterprise.

4.2 The learned DRPIAO/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's length price in connection with the impugned international transaction and holding that the Appellant's international transaction is not at arm's length.

4.3 The learned DRP/AO/TPO have erred in law and facts in computing the operating margin of the Assessee by considering certain operating items as non — operating in nature, thus incorrectly computing the operating margins of the Assessee as 5.12%.

4.4 The learned DRP/ AO/TPO erred in rejecting certain comparable companies by applying the following quantitative and qualitative filters:

a) for having different accounting 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) using employee cost greater than 25% of the total revenues as a comparability criterion;

*c) with export sales less than 75% of total sales vis-a-vis 25% of total sales used by the Appellant in the TP Study;*

*d) applying 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;*

*4.5 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.*

*4.6 The learned DRP/ AO / TPO erred in law and in facts, by rejecting the following companies forming part of TP Study based on unreasonable comparability criteria:*

- Akshay Software Technologies Limited*
- R Systems International Limited*
- TVS Infotech Limited*

*4.7 The learned DRP / AO / TPO erred in law and in facts, by rejecting the following companies identified by the Assessee in the search conducted by the TPO which were wrongly rejected by the TPO based on unreasonable comparability criteria:*

- Celstream Technologies Private Limited*
- Infomile Technologies Limited*
- Mudunuru Limited*

*4.8 The learned DRP / AO / TPO erred in law and in facts, by rejecting the following companies identified by the Assessee in the search conducted by the Assessee itself which were rejected by the Assessee at the time of TP study for the reason that sufficient information was not available at the time of TP Study:*

- Maveric Systems Ltd*
- I2T2 India Ltd*
- Evoke Technologies Ltd*
- Harbinger Systems Pvt Ltd*

*4.9 The learned DRP/ AO / TPO erred in law and in facts, by accepting the following companies as comparable company though the same cannot be considered as comparable to the Appellant in law and fact on one or more grounds:*

- Tata Elxsi Ltd*
- Mindtree Ltd*
- Persistent Systems Ltd*
- Nihilent Technologies Pvt Ltd*
- Aspire Systems India Pvt Ltd*
- Inteq Software Pvt Ltd*
- Infosys Ltd*
- Thirdware Solution Ltd*
- Cybage Software Pvt Ltd*

4.10 Without prejudice to the transfer pricing documentation maintained by the Appellant, the Learned DRP/ AO / TPO have failed to appreciate that the following companies are not functionally comparable to the Appellant, and therefore erred in considering the same as comparables:

- Larsen & Toubro Infotech Ltd
- Infobeans Technologies Ltd

4.11 The learned DRP/AO/TPO erred, in law and in facts, by erroneously computing the margins of certain comparable companies.

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

4.13 The learned DRP / AO / TPO erred in law and in facts, by comparing full-fledged risk bearing entities with Assessee's captive operations without making suitable adjustments to account for differences in functional and risk profile of the Appellant vis-a-vis the comparables.

4.14 Without prejudice to the ground of the appeal 4.2 above, the learned DRP/ AO/TPO erred in the law and in the facts by not giving due considerations 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 the AEs.

4.15 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 91,45,063.

4.16 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 which is to be considered as closely linked to such transaction and should not be tested separately from arm's length perspective.

4.17 The learned DRP/AO/TPO have erred, in law and in facts, by re-characterizing the outstanding receivables as on 31 March 2015 as a loan transaction.

4.18 Without prejudice to our ground of appeal 4.15 above, the learned DRP/AO/TPO have erred. In law and in facts, by not considering that once the working capital adjustment is granted, it appropriately takes into account the delayed/ outstanding receivable and separate TP Adjustment is unwarranted.

4.19 Without prejudice to our ground of appeal 4.15 above, the learned DRP / AO / TPO have erred, in law

*and in facts, by considering invoice-wise method as against a more suitable approach of weighted average method (as originally used by the learned TPO) for computation of interest adjustment on account of delayed/ outstanding receivable.*

*4.20 Without prejudice to our ground of appeal 4.15 above, the learned DRP / AO / TPO have erred, in law and in facts, by not considering the average credit period provided to third party customers as the benchmark to calculate the interest adjustment on account of delayed/ outstanding receivable.*

*Consequential grounds:*

*5. The learned AO has erred in levying interest of INR 2,15,04,395 under section 234B of the Act.*

*6. The learned AO has erred, in laws and on facts, in initiating penalty proceedings u/s 271(1)(c) of the Act.*

*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.”*

2. At the outset, the Ld.AR submitted that, if the issue raised by the assessee in Ground no. 4.14 is considered, all other issues would become academic as the matter would have to be remanded for fresh consideration. He submitted that the assessee in Ground no. 4.14 has raised the issue of not considering the application of internal TNMM for the purpose of bench marking the international transaction.

The Ld.AR submitted that assessee raised this issue before the DRP, and the DRP observed as under:

*“17.0 Ground of Objection 19 - Without prejudice to the ground of objection 2 above, the learned 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;*

17.1 Panel: the assessee contended that internal comparable data should be used for the purpose of TNMM. The assessee raised this issue in its reply to the show cause notice. In this regard it is seen from the TP study report of the assessee that such approach is rejected in the said TP study for the reason that the transactions the assessee had with third parties are different in nature when compared to its AE transactions. The assessee adopted external data for TNMM and identified the external comparables. The relevant extract of the TP study report is reproduced as under.

#### 5.1.2.2 Relevant Data

To determine whether any one of the TP methods can be applied, the availability, coverage and reliability of data necessary for application of the method is important. Accordingly, comparable data was identified as follows:

##### Internal Comparable Data

XSL or its AEs do not undertake same or similar transaction(s) with third parties under comparable circumstances. Accordingly, internal comparable data could not be obtained.

##### External Comparable Data

To identify external comparable data, a search was conducted to identify transactions / companies that could be considered as comparable to XSL. The detailed search process has been set out in Section 5.1.3 for software development services below.

Based on such analysis, comparable transaction level data which involved information about uncontrolled transactions, including prices, quantity, and transaction terms, was identified.

#### 5.1.2.3 Conclusion

Based on the nature and characteristics of the transaction analysed, CUP, CPM and TNMM were found applicable.

Out of the above, CUP method cannot be applied in the present case due to non-availability of transaction level data through both internal and external sources of data. Further, RPM/CPM was also not considered due to the following reasons:

Absence of reliable data on functional comparability (same or similar services) of comparable companies, i.e., the degree of comparability existing between the international transaction and the uncontrolled transaction and between the enterprises entering into such transactions; and

Absence of reliable gross margin data of comparable companies necessary for application of the method.

Net margins earned by comparable companies performing activities similar to those of XSL are available in the public domain and can be easily established, thus facilitating a

*more reliable comparability analysis. Further, it is a well accepted principle that net margins are less affected by transactional differences than are prices (as in the case of CUP) and gross margins (as in the case of CPM). In this case, since the functions performed by comparables identified by us were broadly similar to the functions performed by XSL, the TNMM, which involves net margin comparison, was considered as the most appropriate method for testing the above mentioned transaction of XSL.*

#### *5.1.3 Search for comparable uncontrolled data*

*Based on the provision of Rule 10B of the Rules, comparables for the international transaction would have to be companies which are engaged in same or similar activity as XSL, and are comparable in terms of functions performed, risks assumed and assets utilized. Further, such companies should themselves be independent and should not have significant controlled transactions, which could affect the arm's length nature of their operating margins.*

*Accordingly, companies engaged in software services were considered as comparable to the tested party's business activities.*

*Please note that while performing the analysis, factors taken into consideration for judging comparability were characteristics of functions performed and assets employed. While the contractual terms under which XSL India operated were known, the contractual terms of third parties were not available in the public domain and hence this did not become a factor for judging comparability of transactions. Further, the comparables were also Indian companies, akin to XSL and working under similar economic conditions.*

*For the reasons recorded above there is no basis to consider the internal data. Accordingly, the contentions of the assessee are rejected."*

3. In regards to the above observations of the DRP, the Ld.AR submitted in the written submissions that, the assessee's claim cannot be dismissed, simply because, it contradicts the TP study. He placed reliance on following decisions in support of this arguments.

- *Birlasoft (India) Ltd [(ITA No. 200/Del/2015 for AY 2010-11]*
- *Lummus Technology Heat Transfer BV [(ITA No. 1047/De1/2014 for AY 2009-10);*
- *Tecnimont ICB (P) Ltd [ITA No. 4608 & 5085/Mum/2010 for AY 2005-06]*

- *Xchanging Solutions Limited [(IT(TP)A 1385/Bang/2011 for AY 2007-08]*
- *e4e Business Solutions India Pvt Ltd [(IT(TP)A Nos.324 (B)/15 & 220(B)15 for A 2010-11]*
- *Quark Systems (P.) Ltd [ITA No. 100/Chd/2009 for AY 2004-05]*
- *Nvidia Graphics Pvt Ltd [ITA No.1360/Bang/2018 for AY 2013-14]*
- *S.B. & T. International Ltd [(IT(TP)A No. 51/Mum./2017 for AY 2012-13]*
- *In Trading Pvt Ltd [ITA No. 3712/De1/2018 for AY 2011-12]*

4. On the contrary, the Ld.DR vehemently opposed the above submissions of the assessee and relied on the orders passed by the authorities below.

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

6. It is submitted before us that the assessee provides software development service to its AE and the amounts outstanding from the AE was to be settled as on-going basis in the normal course of business having regard to commercial and economic factors. The Ld.AR primarily submitted that, the arms length determination in respect of the trade receivables stands subsumed within the determination of principle transaction, being the software development service segment.

7. It is also the submission of the Ld.AR that, the assessee also rendered services to unrelated third parties, and no interest was charged by the assessee in respect of delayed receivables from such unrelated third parties, and therefore, the assessee cannot be charged with any interest in case of the receivables outstanding from the AE.

He thus vehemently argued that no separate adjustment in respect of delayed receivables is required when Working Capital Adjustment is granted when margins of the international transactions are to be computed.

We note that the Ld.TPO computed the interest on outstanding trade receivables using LIBOR of six month + 400 basis points which is computed at an effective rate being 4.3836%.

8. From the records we note that the Ld.TPO records that, realisation of receivables from non-AE was within 112 days, whereas there is a delay of 11 days in realising the receivables from the AE on which the Ld.TPO has computed interest. In our opinion, such imputation of interest is arbitrary and is not in accordance with the principles laid down by the various decisions of *Coordinate Bench of this Tribunal* on this issue as well as various *High Courts*.

9. It is also noted that the Ld.TPO has not considered whether the said receivables are subsumed in the computation of the Working Capital Adjustment. In fact, we note that, the Ld.TPO has not granted any Working Capital Adjustment to the assessee, which in our view is again not in accordance with the transfer pricing principles for computing arms length of the international transaction. It is noted that, the assessee has filed before the Ld.TPO the Working Capital Adjustment computation which is overlooked.

10. Be that as it may, we do not agree with the submission of the Ld.AR that, no separate adjustment for interest on the delayed receivables is to be computed when assessee is not charging interest on delayed receivables from unrelated third parties. This is so because, after the insertion of explanation to section 92B(1), payment or deferred payment or receivables or any debt arising during the course of business falls under the expression "international transaction". Therefore in our view, the expanded

meaning of international transaction as contemplated in clause (i) of explanation to section 92B(1), any delay in realisation of receivables from the associated enterprises would certainly fall within the ambit of international transaction.

11. However, as the receivables are closely associated to the primary rendering of software development services, a credit period has to be granted to the AE and has to be considered along with the main international transaction being the sale of software service development.

12. We therefore are of the view that the adjustment proposed by the Ld.TPO in respect of outstanding trade receivables has to be considered along with the main transaction being the software development service rendered by the assessee to the AE by considering a credit period of 90 days. The Ld.AO shall verify if the same is subsumed in the computation of the Working Capital Adjustment. In the event, the receivables stands subsumed, no adjustments deserves to be made. On the contrary, if any trade payables falls outside the credit period of 90 days, adjustment on such receivables would be restricted to LIBOR + 300 basis points.

13. In support of this above view, we rely on the observations of *Coordinate Bench of this Tribunal* in case of *M/s. Zynga Game Network India Pvt. Ltd. vs. DCIT in ITA No. 2573/Bang/2019 by order dated 23/03/2021* for A.Y. 2015-16 which is placed at page 4436 of the legal paper book.

**Accordingly Ground no. 4.14 raised by assessee stands allowed for statistical purposes.**

14. All other issues in respect of the transfer pricing adjustment alleged in the present appeal is kept open.

15. The assessee has raised the following additional grounds.

*“In addition to the grounds of appeal raised before the Hon'ble Bench, the Petitioner hereby wishes to submit the following additional grounds:*

*Corporate tax matters*

*7. Provision for onerous lease amounting to INR 16,02,473 reversed during the year out of provision created during Assessment Year 2009-10 and added to book profit for that year in view of creation, should be excluded in book profit computation for Assessment Year 2015-16 in terms of clause (i) of Explanation I to Section 115JB(2) of the Act.*

*8. Without prejudice to our contention that provision for onerous lease is an ascertained liability, where an upward adjustment is made on account of provision for onerous lease amounting to INR 1,57,11,187 in the book profit computation for Assessment Year 2010-11 pursuant to Hon'ble Tribunal order for that year, the reversal of such provision during the Assessment Year 2015-16 should be excluded in book profit computation for Assessment Year 2015-16 in terms of clause (i) of Explanation I to Section 115JB(2) of the Act.*

*9. Provision for litigation amounting to INR 32,00,000 reversed during the year, out of provision created during Assessment Year 2010-11 and added to book profit for that year, should be excluded in book profit computation for Assessment Year 2015-16 in terms of clause (i) of Explanation I to Section 115JB(2) of the Act.*

*10. Provision for litigation amounting to INR 32,00,000 reversed during the year, out of provision created during Assessment Year 2010-11 and disallowed under the normal provisions of the Act, should be excluded from profit while calculating tax under normal provisions.*

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

*In the above circumstances the Petitioner prays that this Hon'ble Tribunal be pleased to;*

*(i) admit and adjudicate the above additional ground(s),*

*(ii) pass any other order that may be required in the circumstances of the case and render justice.”*

15.1 It has been submitted that no new facts needs to be considered in order to dispose of the additional ground raised by the assessee. It is submitted that the additional grounds are issues that does not require investigation of any new facts. The

Ld.AR, thus prayed for the admission of additional grounds so raised by assessee.

15.2 On the contrary, the Ld.CIT.DR though opposed admission of the additional grounds, could not bring anything on record which would challenge such a right available to assessee under the Act.

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

15.4 The Ld.DR did not object for the additional grounds being admitted.

15.5 We note that one of the additional grounds is directly connected with the main issue of disallowance and no new facts needs to be investigated for adjudicating the same. Another issues alleged by the assessee is a legal issue that does not require investigation of any facts.

15.6 Considering the submissions and respectfully following the decisions of *Hon'ble Supreme Court* in case of *National Thermal Power Co. Ltd. Vs. CIT* reported in (1998) 229 ITR 383 and *Jute Corporation of India Ltd. Vs. CIT* reported in 187 ITR 688, we are admitting the additional ground raised by the assessee.

**Accordingly, the additional grounds raised by assessee stands admitted.**

16. The Ld.AR at the outset, submitted that the above issue have been considered by *Coordinate Bench of this Tribunal* in assessee's own case for A.Ys. 2010-11 & 2011-12 in *IT(TP)A No. 492/Bang/2016* wherein it is observed as under:

*"18. Regarding the additional ground No.17, the Id. AR submitted that as per Explanation 2(i) to section 115JB of the Act, any reversal out of provision created in earlier*

*year, if the book profit of such year has been increased by those provisions, be reduced from net profit while computing book profit in the year of reversal, if such amount is credited to Profit & Loss account.*

*19. The Id. DR relied on the orders of the lower authorities.*

*20. We have heard both the parties and perused the material on record.*

*In our opinion, if the book profit is increased by provision created in that year and on reversal of that provision in the present assessment year, net profit of this assessment year to be reduced so as to compute the correct book profit.*

*With these observations, we remit the issue to the AO for fresh consideration.”*

17. Admittedly, both sides submitted that there is no change of facts and the issue needs to be looked into by the Ld.AO afresh.

18. Considering the submissions and respectfully following the view taken by the *Coordinate Bench of this Tribunal* in assessee's own case, we remand the additional grounds raised by assessee to the Ld.AO for fresh consideration based on the directions therein.

**Accordingly the grounds raised by assessee stands allowed for statistical purposes.**

19. **Ground nos. 5 & 6** are consequential in nature and therefore do not require adjudication.

**In the result, the appeal filed by the assessee stands allowed for statistical purposes.**

**Order pronounced in the open court on 16<sup>th</sup> August, 2022.**

Sd/-  
(CHANDRA POOJARI)  
Accountant Member

Sd/-  
(BEENA PILLAI)  
Judicial Member

Bangalore,  
Dated, the 16<sup>th</sup> August, 2022.  
/MS /

Copy to:

1. Appellant
2. Respondent
3. CIT

4. CIT(A)
5. DR, ITAT, Bangalore
6. Guard file

By order

Assistant Registrar,  
ITAT, Bangalore