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

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

IT(**TP**)A No.292/Bang/2022
Assessment year : 2017-18

Xchanging Solutions Limited, Kalyani Tech Park, Magnolia Building, Survey 1#, 6 & 24, ITPL Main Road, K R Puram Hobli, Bangalore – 560 066. **PAN: AAFCS 9303L**	Vs.	The Assessing Officer, National Faceless Assessment Centre, Delhi [/ DCIT, Circle 7(1)(1), Bangalore].
ASSESSEE		RESPONDENT

Assessee by	:	Shri Padamchand Khincha, CA
Respondent by	:	Shri K. Sankar Ganesh, Jt.CIT(DR)(ITAT), Bengaluru.

Date of hearing	:	05.12.2022
Date of Pronouncement	:	21.12.2022

O R D E R

Per Padmavathy S., Accountant Member

This appeal is against the final order of assessment passed by the AO, National Faceless Assessment Centre, [NFAC], Delhi u/s. 143(3) r.w.s. 144C(13) of the Income-tax Act, 1961 [the Act] dated 24.2.2022 for the assessment year 2017-18.

2. The assessee is a public limited company, engaged in the business of software development services. It filed its original return

of income for AY 2017-18 declaring an income of Rs.3,78,28,990. The case was selected for complete scrutiny and accordingly notice u/s. 143(2) was served on the assessee. The assessee later filed a revised return declaring a loss of Rs.3,99,88,257. Since the assessee had international transaction, a reference was made to the TPO to determine the arm's length price of the international transaction with its AE. The TPO made an adjustment of Rs.12,01,05,614 based on which the AO passed a draft assessment order. Aggrieved, the assessee filed objections before the DRP whereby the TP adjustment was reduced to Rs.11,45,97,470. The assessee is in appeal against the final assessment order passed pursuant to the directions of the DRP.

3. Ground Nos.1 & 2 are general not warranting separate adjudication. Grounds 3 to 17 pertaining to TP adjustment are as extracted below –

"Transfer Pricing grounds

3. The learned DRP/AO/TPO erred in making an addition of INR 4,14,21,224 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 and adjustment on account of the interest income on loan amounting to INR 7,31,76,246 with respect to transactions entered into by the Appellant with its AEs.

4. The learned DRP/AOTTPO 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.

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

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

b) The learned DRP/AO/TPO have erred, in law and in facts, by not applying an upper turnover filter and accordingly accepting companies which are much larger in size and operations as compared to the Appellant

c) The learned DRP/AO/TPO erred in law and in facts by providing employee cost greater than 25% of turnover as a comparability criterion

d) The learned DRP/AO/ TPO erred in law and in facts by rejecting companies by computing related party transactions (greater than 25% ratio) inappropriately.

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

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

i. Great Software Laboratory Private Limited
ii. Mindtree Limited
iii. Tata Elxsi Ltd.
iv. Larsen & Toubro Infotech Ltd.
v. Infobeans Technologies Limited
vi. Persistent Systems Limited
vii. Aptus Software Labs Private Limited

viii. Cygnet Infotech Private Limited
ix. Nihilent Limited
x. Threesixty Logica Testing Services Private Limited
xi. Infosys Limited
xii. Consilient Technologies Private Limited
xiii. Cybage Software Private Limited
xiv. OFS Technologies Limited
xv. R Systems International Limited

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

i. Evoke Technologies Limited
ii. Sankhya Infotech Ltd
iii. Sasken Communication Technologies Limited
iv. RS Software (India) Ltd
v. Jindal Intellicom Pvt Ltd

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

i. Celstream Technologies Limited
ii. Akshay Software Technologies Limited
iii. Sybrant Technologies Pvt Ltd
iv. Isummation Technologies Limited

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

i. Rheal Software Private Limited
ii. Kals Information Systems Limited
iii. Harbinger Systems Private Limited
iv. CG Vak Software & Exports Limited
v. Great Software Laboratory Private Limited
vi. Mindtree Limited
vii. Tata Elxsi Limited
viii. R Systems International Limited

ix. Infobeans Technologies Limited
x. Infosys Limited
xi. Cybage Software Private Limited
xii. Nihilent Limited
xiii. OFS Technologies Limited
xiv. Consilient Technologies Private Limited

8. The learned DRP/AO/TPO erred, in law and on facts, in recomputing the operating margin of the Appellant by considering certain operating items (e.g. Provisions and liabilities written back, etc.) as non-operating in nature and vice-versa.

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

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

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

12. Without prejudice to the ground 4 and 5 above, the learned DRP/AO/TPO erred in law and in facts by not giving due consideration to the Appellant'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 Appellant with its AEs.

13. The learned DRP has erred in not passing a speaking order in relation to the Appellant's contention against adjustment for interest on loan advanced to AE.

14. The learned DRP/AO/TPO has erred in not considering loan advanced to AE as Informal or Quasi-equity.

15. The learned DRP/AO/TPO has erred in not giving due consideration to the fact that advancing loan to the AE was merely a shareholder's activity and it has also resulted in intrinsic benefit for the Appellant.

16. Without prejudice to the ground 13 and 14, the learned DRP/AO/TPO ought to have considered that a part of the loan outstanding from the AE was a mere book entry passed because of an acquisition done by Appellant and did not constitute actual loan advanced to AEs.

17. Without prejudice to our ground of objection 16 above, the learned DRP/TPO/A0 have erred, in law and in facts, by not providing the basis for arriving at the arm's length interest rate of Libor plus 400 basis point for computing notional interest income on loan.

4. The assessee had the following international transactions with its AE.

International Transactions as per TP Report			
Particulars	**Paid/Payable**	**Received/ Receivable**	**Method**
Provision of software development services to AEs		322,496,874	TNMM
Reimbursement of expenses to AEs	38,454,256		Other Method
Trade receivables		108,307,282	Other Method
Trade payables	38,731,604		Other Method
Reimbursement related receivables		7,924,397	Other Method

5. The assessee applied TNM method as the most appropriate method for computing the ALP. Operating Profit/Operating Cost is considered as Profit Level Indicator. The margins computed as per the TP study of the assessee is given below:-

Particulars	**Software Development**
	Services (IN INR)
Income:	
Revenue from operations	343,529,933
Provision for doubtful advances no longer required written back	4,155,821
Miscellaneous income	1,062,406
Total operating income	**348,748,160**
Expenses:	
Direct cost	191,309,625
Other indirect expenses	96,968,126
Foreign Exchange loss	13,015,509
Depreciation	8,153,007
Total operating expenses	**309,446,268**
Operating profit	**39,301,892**
Operating profit/Operating cost	**12.70%**

6. The assessee selected 14 comparables whose 35th percentile is 6.84 and 65th percentile is 10.17 with a median of 8.54 (page 1204 of paper book I). Accordingly, the assessee concluded that the price charged for the international transaction is within arm's length.

7. The TPO arrived at the final list of comparables as given below:-

SI. No.	**Company Name**	**F.Year wise OP/OC (%)**			**Wt Average**
		2016-17	**2015-16**	**2014-15**	
1	Rheal Software Pvt. Ltd.	-12.27	3.29	3.02	-1.85
2	Kals Information Systems Ltd	1.37	3.97	5.77	3.62
3	Infomile Technologies Ltd.	11.12	9.91	10.22	10.43
4	Harbinger Systems Pvt Ltd	12.8	12.69	17.18	14.1

5	C G-V A K Software & Exports Ltd.	11.65	16.95	17.3	15.09
6	Tech Mahindra Ltd.	16.51	17.08	15.85	16.51
7	X S Cad India Pvt. Ltd.	18.93	27.57	11.36	19.78
8	Exilant Technologies Pvt. Ltd.	17.19	25.9	16.75	20.03
9	Larsen & Toubro Infotech Ltd.	20.78	19.21	23.98	21.14
10	Great Software Laboratory Pvt. Ltd.	27.18	20.24	10.67	21.24
11	Mindtree Ltd.	20.12	26.11	27.51	24.17
12	R Systems International Ltd.	16.74	31.05	26.44	24.40
13	Persistent Systems Ltd.	25.05	23.95	30.4	26.17
14	Tata Elxsi Ltd.	24.9	29.13	24.45	26.19
15	Aptus Software Labs Pvt. Ltd.	24.84	27.68	26.73	26.32
16	Cygnet Infotech Pvt. Ltd.	25.48	27.76	32.41	28.55
17	Infobeans Technologies Ltd.	23.34	41.21	22.21	28.92
18	Nihilent Ltd.	30.8	24.46	34.26	29.84
19	Cadsys (India) Ltd.	18.59	31.58	45.7	30.22
20	OFS Technologies Ltd.	19.95	28.64	67.11	30.80
21	Threesixty Logica Testing Services Pvt. Ltd.	36.64	48.46	42.03	36.64
22	Pagetraffic Web-Tech Pvt. Ltd.	43.96	45.69	24.19	38.31
23	Infosys Ltd.	39.24	38.51	41.46	39.74
24	Cybage Software Pvt. Ltd.	63.3	61.97	69.1	64.79
25	Consilient Technologies Pvt. Ltd.	54.85	71.83	69.51	65.14
26	Dun & Bradstreet Technologies & Data Services Pvt. Ltd.	110.36	83.42	76.69	90.18
27	E-Infochips Pvt. Ltd.	106.61	95.12	76.42	92.03
	35th Percentile				**21.24**
	Median				**26.19**
	65th Percentile				**29.84**

8. The TPO also recomputed the margin of the assessee at 11.01% and accordingly arrived at the TP adjustment with respect to Software Development services as given below:-

SWD SEGMENT		
Particulars	**Formula**	**Amount (in Rs.)**
Taxpayers Operating Revenue	OR	343,529,933
Taxpayers Operating Cost	OC	309,446,268
Taxpayers Operating Profit	OP	34,083,665
Taxpayers PLI	PLI=OP/OC	11.01%
35th Percentile Margin of comparable set		21.24%
Adjustment Required (if PLI< 35th Percentile)		Yes
Median Margin of comparable set	M	26.18%
Arm's Length Price	ALP=(1+M)*OC	390,459,301
Price Received	OR	343,529,933
Shortfall being adjustment	ALP-OR	4,69,29,368

9. The DRP after considering the objections of the assessee gave partial relief whereby the TP adjustment was reduced to Rs.11,45,97,470.

10. During the course of hearing the ld. AR submitted that Larsen & Toubro Infotech Limited., Persistent Systems Limited., Tata Elxsi Limited., Infosys Limited., Cybage Software Private Ltd., Nihilent Technologies Ltd., Mindtree Limited., R system International Limited., should be excluded based on upper turnover filter of Rs.200 crores. The ld. AR submitted that the turnover of the assessee is Rs.34.35

crores. The TPO while applying the turnover filter failed to apply the upper turnover filter of Rs.200 crores and above. Accordingly, the above 8 comparables whose turnover is more than 200 crores should be excluded. In this regard, the ld. AR relied on the decision of the coordinate Bench in the case of *Radisys India Ltd. v.DCIT, IT(TP)A No.190/Bang/2022*.

11. The ld. DR relied on the orders of the lower authorities.

12. We have heard the rival submissions and perused the material on record. The coordinate Bench of the Tribunal in *Radisys India Ltd. (supra)* while considering the turnover filter held as under:-

> "7.3. We have perused the submissions advanced by both the sides in light of record placed before me. We note that the assessee has a turnover under software development service segment at Rs.1,59,43,94,173/-. It is also noted that the Ld.TPO has excluded from the list of comparable companies, chosen by the assessee in the TP study, whose turnover was less than Rs.1 crore. The contention of the assessee is that, as the Ld. TPO excluded companies with a low turnover, he failed to apply the same yardstick to exclude companies with a high turnover. From the submissions of the assessee, we note that the comparables sought for exclusion on turnover filter is more than Rs.200 crores as follows:
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> 1) Larsen & Toubro Infotech Limited – Rs.6,183 Cr.
> 2) Persistent Systems Limited - Rs.1,732 Cr.
> 3) Tata Elxsi Limited - Rs.1,201 Cr.
> 4) Infosys Limited - Rs.59,257Cr.
> 5) Cybage Software Private Ltd. - Rs.759 Cr.
> 6) Nihilent Technologies Ltd. - Rs.259 Cr.

7.4. It is also an admitted position that coordinate bench of this Tribunal in assessee's own case in IT(TP)A No.2482/Bang/2019 dated 22.2.2022 excluded comparables with high turnover and have been consistently following the turnover range of Rs.1 to 200 Crores and Rs.200 to Rs.2000 crores, so on and so forth. The coordinate bench of this Tribunal in assessee's own case cited (supra) has dealt with the applicability of turnover filter by observing as under: 11. As far as comparability of companies listed as (a) to (g) in Grd.No.4 raised by the Assessee is concerned, the admitted factual position is that the turnover of these companies is more than Rs.200 Crores and the Assessee's turnover is only Rs.1,21,34,35,876/-. The TPO excluded from the list of comparable companies chosen by the Assessee in its TP study companies whose turnover was less than Rs.1 Crore. The contention of the Assessee before the DRP was that while the TPO excluded companies with low turnover, he failed to apply the same yardstick to exclude companies with high turnover compared to the Assessee. The reason for excluding companies with low turnover was that such companies do not reflect the industry trend as their low cost to sales ratio made their results less reliable. The contention of the Assessee was that there would be effect on profitability wherever there is high or low turnover and therefore companies with high turnover should also be excluded from the list of comparable companies. The DRP primarily relied on the decision rendered by the Hon'ble Delhi High Court in the case of Chryscapital Investment Advisors India Pvt.Ltd Vs. DCIT 82 Taxmann.com 167(Del), wherein it was held that high turnover ipso facto does not lead to the conclusion that a company which is otherwise comparable on FAR analysis can be excluded and that the effect of such high turnover on the margin should be seen. The DRP therefore held that a company which is otherwise functionally comparable cannot be excluded only on the basis of high

7.4. It is also an admitted position that coordinate bench of this Tribunal in assessee's own case in IT(TP)A No.2482/Bang/2019 dated 22.2.2022 excluded comparables with high turnover and have been consistently following the turnover range of Rs.1 to 200 Crores and Rs.200 to Rs.2000 crores, so on and so forth. The coordinate bench of this Tribunal in assessee's own case cited

(supra) has dealt with the applicability of turnover filter by observing as under:

11. As far as comparability of companies listed as (a) to (g) in Grd.No.4 raised by the Assessee is concerned, the admitted factual position is that the turnover of these companies is more than Rs.200 Crores and the Assessee's turnover is only Rs.1,21,34,35,876/-. The TPO excluded from the list of comparable companies chosen by the Assessee in its TP study companies whose turnover was less than Rs.1 Crore. The contention of the Assessee before the DRP was that while the TPO excluded companies with low turnover, he failed to apply the same yardstick to exclude companies with high turnover compared to the Assessee. The reason for excluding companies with low turnover was that such companies do not reflect the industry trend as their low cost to sales ratio made their results less reliable. The contention of the Assessee was that there would be effect on profitability wherever there is high or low turnover and therefore companies with high turnover should also be excluded from the list of comparable companies. The DRP primarily relied on the decision rendered by the Hon'ble Delhi High Court in the case of Chryscapital Investment Advisors India Pvt.Ltd Vs. DCIT 82 Taxmann.com 167(Del), wherein it was held that high turnover ipso facto does not lead to the conclusion that a company which is otherwise comparable on FAR analysis can be excluded and that the effect of such high turnover on the margin should be seen. The DRP therefore held that a company which is otherwise functionally comparable cannot be excluded only on the basis of high turnover. The Assessee has raised Grd.No.4 before the Tribunal challenging the aforesaid view of the DRP.

12. On the issue of application of turnover filter, we have heard the rival submissions. The parties relied on several decisions rendered on the above issue by the various decisions of the ITAT Bangalore Benches in favour of the Assessee and in favour of the Revenue, respectively. The ITAT Bangalore Bench in the case of Dell International Services India (P) Ltd. Vs. DCIT (2018) 89 Taxmann.com 44 (Bang-Trib) order dated 13.10.2017, took note of the decision of the ITAT Bangalore Bench in the case of Sysarris Software Pvt.Ltd. Vs. DCIT (2016) 67 Taxmann.com

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

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

"9. Having heard both the parties and having considered the rival contentions and also the judicial precedents on the issue, we find that the TPO himself has rejected the companies which are (sic) making losses as comparables. This shows that there is a limit for the lower end for identifying the comparables. In such a situation, we are unable to understand as to why there should not be an upper limit also. What should be upper limit is another factor to be considered. We agree with the contention of the learned counsel for the assessee that the size matters in business. A big company would be in a position to bargain the price and also attract more customers. It would also have a broad base of skilled employees who are able to give better output. A small company may not have these benefits and therefore, the turnover also would come down reducing profit margin. Thus, as held by the various benches of the Tribunal, when companies which arc loss making are excluded from comparables, then the super profit making companies should also be excluded. For the purpose of classification of companies on the basis of net sales or turnover, we find that a reasonable classification has to be made. Dun &

Bradstreet & Bradstreet and NASSCOM have given different ranges.

Taking the Indian scenario into consideration, we feel that the classification made by Dun & Bradstreet is more suitable and reasonable. In view of the same, we hold that the turnover filter is very important and the companies having a turnover of Rs.1.00 crore to 200 crores have to be taken as a particular range and the assessee being in that range having turnover of 8.15 crores, the companies which also have turnover of 1.00 to 200.00 crores only should be taken into consideration for the purpose of making TP study."

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

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

17.7. We have considered the rival submissions. The substantial question of law (Question No.1 to 3) which was framed by the Hon'ble Delhi High Court in the case of Chryscapital Investment Advisors (India) Pvt.Ltd., (supra) was as to whether comparable can be rejected on the ground that they have exceptionally high profit margins or fluctuation profit margins, as compared to the Assessee in transfer pricing analysis. Therefore as rightly submitted by the learned counsel for the Assessee the

observations of the Hon'ble High Court, in so far as it refers to turnover, were in the nature of obiter dictum. Judicial discipline requires that the Tribunal should follow the decision of a non-jurisdiction High Court, even though the said decision is of a non-jurisdictional High Court. We however find that the Hon'ble Bombay High Court in the case of CIT Vs. Pentair Water India Pvt.Ltd. Tax Appeal No.18 of 2015 judgment dated 16.9.2015 has taken the view that turnover is a relevant criterion for choosing companies as comparable companies in determination of ALP in transfer pricing cases. There is no decision of the jurisdictional High Court on this issue. In the circumstances, following the principle that where two views are available on an issue, the view favourable to the Assessee has to be adopted, we respectfully follow the view of the Hon'ble Bombay High Court on the issue. Respectfully following the aforesaid decision, we uphold the order of the DRP excluding 5 companies from the list of comparable companies chosen by the TPO on the basis that the 5 companies turnover was much higher compared to that the Assessee.

17.8. In view of the above conclusion, there may not be any necessity to examine as to whether the decision rendered in the case of Genisys Integrating (supra) by the ITAT Bangalore Bench should continue to be followed. Since arguments were advanced on the correctness of the decisions rendered by the ITAT Mumbai and Bangalore Benches taking a view contrary to that taken in the case of Genisys Integrating (supra), we proceed to examine the said issue also. On this issue, the first aspect which we notice is that the decision rendered in the case of Genisys Integrating (supra) was the earliest decision rendered on the issue of comparability of companies on the basis of turnover in Transfer Pricing cases. The decision was rendered as early as 5.8.2011. The decisions rendered by the ITAT Mumbai Benches cited by the learned DR before us in the case of Willis Processing Services (supra) and Capegemini India Pvt.Ltd. (supra) are to be regarded as per incurium as these decisions ignore a binding co-ordinate bench decision. In this regard the decisions referred to by the learned counsel for the Assessee supports the plea of the learned counsel for the Assessee. The decisions rendered in the case of M/S.NTT Data (supra), Societe Generale Global Solutions (supra) and LSI Technologies (supra) were rendered

> later in point of time. Those decisions follow the ratio laid down in Willis Processing Services (supra) and have to be regarded as per incurium. These three decisions also place reliance on the decision of the Hon'ble Delhi High Court in the case of Chriscapital Investment (supra). We have already held that the decision rendered in the case of Chriscapital Investment (supra) is obiter dicta and that the ratio decidendi laid down by the Hon'ble Bombay High Court in the case of Pentair (supra) which is favourable to the Assessee has to be followed. Therefore, the decisions cited by the learned DR before us cannot be the basis to hold that high turnover is not relevant criteria for deciding on comparability of companies in determination of ALP under the Transfer Pricing regulations under the Act. For the reasons given above, we uphold the order of the CIT(A) on the issue of application of turnover filter and his action in excluding companies by following the ratio laid down in the case of Genisys Integrating (supra).
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> 14. In view of the aforesaid decision, we hold that 7 companies listed in Sl.No.1,2,4,6,7, 10 and 11 of Grd.No.1 raised by the Assessee whose turnover in the current year is more than Rs.200 Crores should be excluded from the list of comparable companies."
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> 7.5. In view of the above decision in assessee's own case as well as the consistent approach followed by this Tribunal, we direct the Ld. AO/TPO to exclude the comparables with high Turnover, mentioned herein above."

13. Respectfully following the same, we direct the AO/TPO to exclude the comparables with high turnover of more than Rs.200 crores.

14. Out of the final list of comparables, the ld. AR submitted that Infobean Technologies Ltd., needs to be excluded since the company is functionally not comparable with the assessee. It is submitted that the company had launched 2 new segments in 2017 which is automation

engineering and services which are not functionally comparable with the routine software development services. The company is also engaged in high end services such as customer application development, content management system, enterprise mobility and big data analytics. The company has also made huge investments in technology absorption and there has been abnormal growth in the revenue around 76% and in Profit After Tax of 147% [Page 3938 to 3919 of PB]. Accordingly, the ld. AR submitted that the company is not functionally comparable with the assessee. The ld. AR relied on the decisions of Radisys India Ltd. (supra) in this regard.

15. We heard the rival submissions and perused the material on record. The Tribunal on this issue in the case of Radisys India Ltd. (supra) held as under:-

> "8.1. The two comparables that assessee seeks to exclude on functional dissimilarities are:
>
> (i) Infobeans Technologies Ltd. and
> (ii) Cygnet Infotech Pvt. Ltd.
>
> (i) Infobeans Technologies Ltd.
>
> 8.2 The Ld.AR submitted that, this company is engaged in Automation Engineering, Customized Software, Custom Application Development (CAD), Content Management Systems, Enterprise Mobility and Big data Analytics. It is the submission of the Ld.AR that this comparable is functionally not similar to the assessee. He also submitted that, there is no segmental details available in respect of the revenue generated by this company and that the content management, Analytic services are considered to be KPO as per safe harbour rules. This comparable was decided to be excluded from the list of comparables by the coordinate bench of Tribunal vide IT(TP)A

No.210/Bang/2021 in the case of EIT Services India Pvt. Ltd. Vs. Deputy Commissioner of Income-tax for the AY 2016-17, wherein held as under:

"5.7 We have heard the rival submissions and perused the materials available on record. Infobeans Techonologies Ltd. was considered as comparable in the case of ADP Pvt. Ltd. by the coordinate bench of Hyderabad cited (supra) wherein it was held as under:-

"7.3 We have considered the rival submissions and perused the material on record as well as gone through the orders of revenue authorities. The co-ordinate bench of this Tribunal in ADP (P.) Ltd. (supra), directed the AO/TPO to exclude this company from the list of comparables for determining ALP by observing as under:

"21. Having regard to the rival contentions and the material on record, we find that the Co-ordinate Bench of the Tribunal in the following case has considered similar objections of the assessee therein to direct exclusion of this company from the final list of comparables. For the purpose of ready reference, the relevant paragraph is reproduced below: "

18. We have heard the rival contentions and perused the record. The first aspect is the functional comparability of concern which has been finally selected to be comparable. In respect of Infobeans Systems Pvt. Ltd., the financials of said concern clearly reflect that in addition to providing software development services to its associated enterprises, it had also earned foreign exchange from export of goods on FOB basis. The event of export of goods was also mentioned in notes and also in the Profit and Loss Account, where revenue from sale of software was declared. The segmental details of two activities carried on by the said concern were not available and in the absence of the same, the concern could not be equated as functionally comparable to a concern which was providing software development services to its associated enterprises. Applying the same set of reasoning as in the paras hereinabove, we hold that Infobeans Systems Pvt. Ltd. is not comparable to the assessee".

22. Respectfully following the same, we direct that Infobeans be excluded from the final list of comparables in this case also.

7.4 On perusal of the order of the co-ordinate bench of this Tribunal and on perusal of the financial statements of Infobeans Technologies Ltd., we observe that the company is functionally not comparable and no segmental details are available. Therefore, the co-ordinate bench did not consider this company as comparable in assessee's own case for AYs 2014-15 & 2015-16. Respectfully following the decision of the co-ordinate bench, we direct the AO/TPO to exclude this company from the final list of comparables."

5.8. In view of the above decision of the Tribunal, we are inclined to hold that Infobeans Technologies Ltd. cannot be considered as a comparable and to be excluded from the list of comparables."

8.3. On verification of the financials of this company for AY 2017-18, we note that in the Annual Report at page 2343 placed in paper book Volumes 4 of 6, this has been stated to be catering into vide range of segments as under:

"INFOBEANS TECHNOLOGIES LIMITED Founded in 2000, InfoBeans Technologies is a leading player offering Customized Software, Digital, Transformation and Enterprise Mobility solutions for clients across the globe. With two state-of-the-art facilities in India, the CMMI level 3 certified Company caters to Fortune 100 clients in USA, Germany and Middle East markets. The Company caters to a wide range of segments in the industry, including distributed storage systems, multi-format multimodal content and e-commerce web and mobile platforms for diverse sectors. The Company's transparent operations, professional team of over 700 employees and high customer focus has enabled it to grow a blue-chip client base with over 90% repeat business."

8.4. Further, at page 2320 of the paper book, this company is said to be providing computer programming, consultancy and related activities as per NIC code. A combined reading of this

> makes it clear that this company is engaged in not only SWD service but other allied services to various industrial segments. Whereas on perusal of financial statement at page 12367 of the paper book and Note 20 at page 2378 of the paper book, we note the revenue recognition is only under one head being "Expert" amounting to Rs.66,12,31,773/-. We also notice that at page 2408, in Related Party Transaction details this company has earned revenue of Rs.8,00,53,350/- from it's AE. From this it is clear that this company is rendering services to non-AE customers also, whereas the assessee before us is a captive service provider only catering to the requirements of its AE. Under such circumstances we do not deem it fit to be considered in the final set of comparables.
>
> Accordingly, this comparable is directed to be excluded."

16. In assessee's case, the year under consideration i.e. AY 2017-18 is same as in the case of Radisys India Ltd. (supra), therefore respectfully following the above decision, we hold that Infobean Tecnologies Ltd. should be excluded from the list of comparables.

17. The next exclusion sought by the ld. AR is with regard to Aptuse Software Labs P. Ltd. The assessee submitted before the TPO that the company fails employee cost filter for FY 2015-16 and FY 2014-15. It was also submitted that the company fails export turnover filter for FY 2015-16. The assessee further submitted that the company is engaged in providing wide range of services i.e. provisions of infrastructure management, cloud computing, engineering Q&A and as a network operation centre, accordingly the functions are not comparable to the assessee. The DRP while considering the objections of the assessee held that –

“9.5.5 We note that the company has failed the employee cost filter and we are of the view that the software development services as well as IT enabled services are mainly rendered by the employees and hence, the employees cost for rendering such services is generally high, and therefore the application of the employees cost filter is appropriate to eliminate companies which are rendering services through sub-contracts. The Hon'ble Delhi bench of ITAT in the case of Navisite India Pvt. Ltd. in ITA no. ITA No.5329/D/2012, the Hon'ble 1TAT upheld the application of the above filter. The view has also been upheld by the Hon'ble Delhi High Court, in the case of Rampgreen Solutions Pvt. Ltd. (ITA.102/2015) in paragraph 38 of the decision. wherein it is held that "plainly, a business model where services are rendered by own employees and using one's own infrastructure would have a different cost structure as compared to a business model where services are outsourced. There was no material for the Tribunal to conclude that the outsourcing services by would have no bearing on the profitability of the said entity." Hence, we do not find any infirmity in application of above filter.

9.5.6 Also, the Hon'ble ITAT Bangalore Bench in the case of DCIT v. Misys Software Solutions (I) P. Ltd. (2017) 87 taxmann.com 170 (Bang.)/IT(TP)A No. 1086/Bang/2013 & CO No.159/Bang/2015 Trib.) took the view that companies having less than 25% employee cost cannot be considered as a good comparable to software development service provider.

9.5.7 The rationale for this filter is that companies that are engaged in providing similar services will require a minimum level of expenditure as personnel expense. Employees cost constitutes the major component of cost in any service sector. Very low employee cost, viz., less than 25% of total cost, indicates that company is either engaged in some other business or it has outsourced the service functions to a third party, i.e., it is not rendering services on its own. Such companies cannot be treated as functionally comparable to the assessee. Hence, we do not find any infirmity in application of above filter. The objection is accordingly rejected.

> In view of the above discussion, the selection of this company is upheld."

18. The ld. AR therefore submitted that the DRP has accepted the contentions of the assessee, however, has erroneously concluded that the objections are rejected.

19. After hearing both the parties, we notice that the DRP has agreed with the various contentions of the assessee which is supported by the relevant extract given above. We notice that the DRP while concluding has stated that the objection of the assessee with regard to exclusion is rejected. Since there seems to be a disconnect between the justification given by the DRP and the final conclusion, we are of the considered view that this issue should be remitted back to the DRP for reconsideration of the conclusion. Accordingly, we direct the DRP to examine the issue in the light of its own observations and decide the issue accordingly after giving reasonable opportunity of being heard to the assessee.

20. The next prayer of the ld. AR is for the inclusion of the following comparables.

1. Akshay Software Technologies Ltd.
2. Evoke Technologies Ltd.
3. Insummation Technologies Pvt. Ltd.

Akshay Software Technologies Ltd.

21. The DRP upheld the exclusion of the company by stating that the exclusion cannot be decided by relying on any judicial precedent. It

was also held that comparabliltiy is an exercise which has to be carried on every year based on the facts of the specific year. The inclusion and exclusion of a comparable has to be necessarily justified on the basis of facts available on record, the FAR analysis and the information in the annual report for each year and not on the basis of judicial precedent. The ld. AR submitted that the company is providing professional services, procurement, implementation support and maintenance of ERP products and services which is a category of business management software and therefore would come under the purview of software related services . It is also submitted that 97.54% of the revenue is from these services which are comparable to that of the assessee (page 4768 of PB). The ld. AR further submitted that the company passes all filters applied by the TPO. The ld. AR relied on the decision of Radisys IndiaLtd. (supra) in this regard.

Evoke Technologies

22. The DRP upheld the exclusion of this company on the ground that the export revenue constitutes only 18.19%of the total revenue. The DRP considered Note No.2.16 which shows an export revenue of Rs.87.58 crores and domestic sales ofRs.61.93 lakhs which is contradictory to the geographical segment information given in Note 2.26. The DRP therefore concluded that the company should be excluded in view of the unreliable data provided in the annual report with regard to export turnover. The ld. AR submitted that the company derives income from software development services and therefore

functionally comparable to the assessee (page 4793 of PB). It is also submitted that it passes all filters applied by the TPO and accordingly needs to be included. The ld. AR relied on the decision of Radisys India Ltd (supra) in this regard.

23. We have heard the rival submissions and perused the material on record. We notice that the above two comparables are considered in the decision of the coordinate Bench in the case of Radisys India Ltd. (supra) where it is held that –

> "6. Ground No.6 is raised by assessee seeking inclusion of following comparables under SWD segment:
>
> (i) Akshay Software Technologies Ltd
> (ii) Batchmaster Software Private Ltd
> (iii) DCIS DOT COM Solutions India Pvt Ltd
> (iv) Evoke Technologies Private Ltd
> (v) Sagarsoft (India) td
> (vi) Sasken Technologies Limited
> (vii) E-Zest Solutions Limited
>
> 6.1 ***
>
> It is submitted that the remaining 5 comparables sought for inclusion, were not considered by the Ld.TPO/AO. We therefore deem it appropriate to remit them to the Ld. AO/TPO. The Ld. AO/TPO shall look into the functional profile of these comparables and verify the same with that of the assessee. If they are functionally found to be similar with that of assessee, the same may be considered in accordance with law, considering the turnover limit of Rs.1 to 200 Crores.
>
> Accordingly, this ground raised by the assessee stands partly allowed."

24. Respectfully following the above decision, we remit the issue of inclusion of Akshay Software and Evoke Technologies back to the AO/TPO with similar directions.

Insummation Technologies Ltd.

25. The DRP did not accept the inclusion of this company on the ground that the company do not appear in the TPO's search matrix and accordingly held that the assessee is cherry picking to reject the inclusion. The ld. AR submitted that the company is not appearing in search matrix of the TPO cannot be the only ground of rejection. At the time of preparation of TP study, the data was not available and therefore the assessee prayed for inclusion of the company during the proceedings since the company is functionally comparable. The company is engaged in the provision of software development services and 100% of its revenue is from rendering of such services [pg 5332 and 5342 of PB]. In this regard, the ld. AR relied on the decision of the coordinate Bench in the case of EIT Services India P. Ltd v. PCIT, IT(TP)A No.210/Bang/2021 dated 22.8.2022.

26. We heard the ld. DR. We notice that the coordinate Bench in the case of EIT Services India P. Ltd (supra) has considered the issue of inclusion of Insummation Technologies and held that –

> "7.6. We have heard the rival submissions and perused the materials available on record. It has been submitted by Ld. A.R. that this comparable has been accepted by the Ld. DRP in assessment year 2017-18 in assessee's own case. As seen from

the direction in para 2.11.7.1 of the order, wherein observed as under:-

"2.11.7.1 Having considered the submissions, and on perusal of the annual report, it is seen that the TPO has rejected the comparable for the reason that it fails export revenue filter. However, on examination of the financials of the company as per Note 13 forming part of financial statements the company has reported Rs.2,20,11,325/- of revenue from export sales as against total sales of Rs.220,84,825/- constituting 99.67% of the total revenue. Thus, the company satisfies the export turnover filter adopted by the TPO. In addition, the company as per the information in the annual report especially the segmental reporting the business activity of the company falls within the single primary business segment viz. Software development. As it is functionally similar and satisfies the export turnover filter, the TPO is directed to consider the company as comparable for the determination of ALP in the software development services."

7.7 In view of the above, we do not find any reason to exclude this company viz. Isummation Technologies Ltd. from the list of comparables in the assessment year 2016-17. Directed accordingly."

27. We notice that in the above decision, the Tribunal has allowed the inclusion of the company in the AY 2016-17 based on the fact that the DRP in AY 2017-18 has accepted the inclusion of the company. Accordingly, respectfully following the decision of the coordinate Bench, we hold that the company be included for AY 2017-18 in assessee's case.

Working capital adjustment

28. The TPO did not give working capital adjustment to the assessee. The DRP while upholding the decision of TPO, held that it was not demonstrated with any data or information there exists a

difference in price because of the working capital adjustment. The ld AR relied on the decision of the coordinate bench in the case of *Huawei Technologies India Pvt. Ltd. in IT(TP)A No.1939/Bang/2017 dated 31.10.2018* The ld. DR relied on the decision of lower authorities.

29. We notice that similar issue of working capital adjustment came up for consideration before the coordinate Bench of the Tribunal in the case of *Huawei Technologies India Pvt. Ltd. (supra)* wherein it was held as under:-

> "**15.** In the present case the TPO allowed working capital adjustment accepting the calculation given by the Assessee. The CIT (A) in exercise of his powers of enhancement held that no adjustment should be made to the profit margins on account of working capital differences between the tested party and the comparable companies for the following reasons:

(*i*)	The daily working capital levels of the tested party and the comparables was the only reliable basis of determining adjustment to be made on account of working capital because that would be on the basis of working capital deployed throughout the year.
(*ii*)	Segmental working capital is not disclosed in the annual reports of companies engaged in different segments and therefore proper comparison cannot be made.
(*iii*)	Disclose in the balance sheet does not contain break up of trade and non-trade debtors and creditors and therefore working capital adjustment done without such break up would result in computation being skewed.
(*iv*)	Cost of capital would be different for different companies and therefore working capital adjustment made disregarding this different based on broad approximations, estimations and assumptions may not lead to reliable results.

16. The CIT (A) also placed reliance on a decision of Chennai ITAT in the case of *Mobis India Ltd.* v. *Dy. CIT* [2013] 38 taxmann.com 231/[2014] 61 SOT 40. That decision was based on the factual aspect that the Assessee was not able to demonstrate how working capital adjustment was arrived at by the Assessee. Therefore nothing turns on the decision relied upon by the CIT (A) in the impugned order. In the matter of determination of Arm's Length Price, it cannot be said that the burden is on the Assessee or the Department to show what is the Arm's Length Price. The data available with the Assessee and the Department would be the starting point and depending on the facts and circumstances of a case further details can be called for. As far as the Assessee is concerned, the facts and figures with regard to his business has to be furnished. Regarding comparable companies, one has to fall back upon only on the information available in the public domain. If that information is insufficient, it is beyond the power of the Assessee to produce the correct information about the comparable companies. The Revenue has on the other hand powers to compel production of the required details from the comparable companies. If that power is not exercised to find out the truth then it is no defence to say that the Assessee has not furnished the required details and on that score deny adjustment on account of working capital differences. Regarding applying the daily balances of inventory, receivables and payables for computing working capital adjustment, the Delhi Bench of ITAT in the case of *ITO* v. *E Value Serve.com* [2016] 75 taxmann.com 195 (Delhi - Trib.). has held that insisting on daily balances of working capital requirements to compute working capital adjustment is not proper as it will be impossible to carry out such exercise and that working capital adjustment has to be based on the opening and closing working capital deployed. The Bench has also observed that that in Transfer Pricing Analysis there is always an element of estimation because it is not an exact science. One has to see that reasonable adjustment is being made so as to bring both comparable and test party on same footing. Therefore there is little merit in CIT (A)'s objection on working adjustment based on unavailable daily working capital requirements data. There is also no merit in the objection of the CIT (A) regarding absence of segmental details available of working capital requirements of comparable companies chosen and absence of details of trade and non-trade debtors of comparable companies as these details are beyond the power of the Assessee to obtain, unless these details are available in public domain. Regarding absence of

cost of working capital funds, the OECD guidelines clearly advocates adopting rate(s) of interest applicable to a commercial enterprise operating in the same market as the tested party. Therefore this objection of the CIT (A) is also not sustainable.

17. In the light of the above discussion we are of the view that the CIT (A) was not justified in denying adjustment on account of working capital adjustment. Since, the CIT (A) has not found any error in the TPO's working of working capital adjustment, the working capital adjustment as worked out by the TPO has to be allowed. We may also add that the complete working capital adjustment working has been given by the Assessee and a copy of the same is at pages 173 & 192 of the Assessee's paper book. No defect whatsoever has been pointed out in these working by the CIT (A). We may also further add that in terms of Rule 10B(1)(e) (iii) of the Rules, the net profit margin arising in comparable uncontrolled transactions should be adjusted to take into account the differences, if any, between the international transaction and the comparable uncontrolled transactions which could materially affect the amount of net profit margin in the open market. It is not the case of the CIT (A) that differences in working capital requirements of the international transaction and the uncontrolled comparable transactions is not a difference which will materially affect the amount of net profit margin in the open market. If for reasons given by CIT (A) working capital adjustment cannot be allowed to the profit margins, then the comparable uncontrolled transactions chosen for the purpose of comparison will have to be treated as not comparable in terms of Rule 10B(3) of the Rules, which provides as follows:

> "(3) An uncontrolled transaction shall be comparable to an international transaction if—

(*i*)	none of the differences, if any, between the transactions being compared, or between the enterprises entering into such transactions are likely to materially affect the price or cost charged to paid in, or the profit arising from, such transactions in the open market; or
(*ii*)	reasonably accurate adjustments can be made to eliminate the material effects of such differences."

> **18.** In such a scenario there would remain no comparable uncontrolled transactions for the purpose of comparison. The transfer pricing exercise would therefore fail. Therefore in keeping with the OECD guidelines, endeavor should be made to bring in comparable companies for the purpose of broad comparison. Therefore the working capital adjustment as claimed by the Assessee should be allowed. We hold and direct accordingly."

30. Respectfully following the above decision of the Tribunal, we direct the AO/TPO to allow working capital adjustment claimed by the assessee.

31. Through Ground No.8 the assessee is contending that the TPO while recomputing the operating margin of the assessee has considered certain items such provisions and liabilities written back etc., as non-operating items and vice versa. The ld. AR submitted that these items have been disallowed in the earlier years by assessee while computing the taxable income and have already suffered tax. Therefore the ld. AR prayed that the items should be considered as part of operating cost for the year under consideration. We accordingly remit this issue back to the TPO/AO to examine the claim of the assessee and decide the issue in accordance with law.

32. Ground No.11 pertains to the AO/TPO erred in not restricting TP adjustment to the value of international transaction. In the light of our decision with regard to the TP adjustment, this ground has become academic and accordingly left open.

33. Ground No.13 is with regard to adjustment made by the TPO towards notional interest on loans advanced to AE. The assessee has

reported in the financial statements an amount of Rs.172.83 crores as loans advanced to the AEs which consists of Rs. 74.21 Crore which was inherited by the assessee through merger of SSI Ltd India in the year 2004 and the balance amount of Rs.98.62 advanced by the assessee to its AE Xchanging Solutions Ltd, USA between 2004-07. The assessee had created a provision for the entire amount in the books in earlier years since according to the assessee there was no economic interest / benefit is expected to be realised from these loans in the future years and accordingly in the statement of accounts as of 31.03.2017 the loan amount is reflected net of the provision amount as Rs.NIL. The TPO treated the loan as a separate international transaction by stating that the assessee has provided benefit to its AE by way of advancement of interest free loan and accordingly proposed a TP adjustment by computing a notional interest of Rs.7,31,76,246 at the rate of 6 months LIBOR + 400 basis points. On objections filed the DRP confirmed the adjustment. Aggrieved the assessee is in appeal before us.

34. The ld AR submitted separate arguments with regard to loan inherited as a result of merger and with regard to the loan given by the assessee to its AE directly.

35. With respect to the loan amount of INR 74,21,40,000 resulting out of merger scheme, the ld AR submits that this asset is appearing in the books of the company because of adoption of pooling of interest method to give effect to the amalgamation. The assessee had not paid

any consideration to acquire this asset as the same was not expected to be realised even by the erstwhile company. Accordingly, it was accounted in the books at the time of acquisition as asset brought in and the entire amount is provided for. It is further submitted that the loan issued by erstwhile Company not forming part of consideration paid on account of merger and is adjusted from the general reserve and hence the consideration paid was only for the net amount. The ld AR submitted that the loan should not be treated as an asset in the books of the assessee as there is not it is probable that future economic benefits associated with the item that will flow in future. Thus, the ld AR contended the loan is a fictitious asset having no substance, appearing in the books only due to the accounting entry as mandated but in reality, no economic benefit is expected to be realized. The reason for creating the provision reflects the management expectation that this amount is not realizable and the recording of entry was done to an accounting compulsion. It is therefore submitted that where a Company has deemed its loan to be irrecoverable, there should be no notional interest on such loan which should be charged and made taxable in the hands of the Company. Reliance in this regard is placed on the decisions in the case of UCO Bank, Calcutta Vs. Commissioner Of Income-Tax, West Bengal [Civil Appeal No.235 of 1996] and Bombay Dyeing & Mfg Co Limited VS ACIT/DCIT [ITA No.928/M/2020 & ITA Nos.3299 &2779/M/2019]. One more plea of the ld AR is that the loan does not fall under the ambit of the transfer pricing provisions as the net amount of loan outstanding in the books

of accounts is Nil and is not an international transaction occurred during the year.

36. With regard to Loan issued directly by the assessee to its AE amounting to INR 98,61,60,000, the ld AR submitted that the loan was extended to meet the working capital needs and to ensure the survival of AE which was in a fragile financial position because of certain loss-making contracts which it couldn't get out of and thus, at risk of financial breakdown. It is further submitted that subsequently, from the year ended 31 March 2011 onwards, recognizing that there are no future economic benefits expected to arise from the loan, the entity has recorded the provision for the above-mentioned amount of loan advanced to it AEs and consequently, disclosed in the books as set off against the loans and advances balance i.e. net balance of loans advanced to AEs is shown as NIL. The next argument of the ld AR is that the assessee being parent company, the funds provided per se, is an arrangement enabling the subsidiary to avail funding other than shareholder equity and hence the same partakes the character of 'quasi-equity. In this regard reliance is placed on the decisions in the case of Vijay Electricals (ITA 842 / Hyd / 2012) and SGS India Private Limited Vs Addl. Commissioner of Income-tax (ITA No. 2406/Mum/2006). The next line of argument of the ld AR is that the investment by the assessee in the wholly owned subsidiary is a strategic investment for increasing business, sales and profit, and therefore the assessee, has a deep interest in the operations of its subsidiaries. Any support to them is therefore in the business interest

of the assessee and it was obligatory on part of the assessee, being the parent company and the company desirous of expanding its business in US Market, to provide the funds required for the expansion. Thus, it is argued that any support granted to its subsidiary is in the business interest of the assessee and represents a shareholder activity. In addition to the above, the ld AR submitted that the assessee has similar amount outstanding for the previous years as well in relation to which the TPO has consistently accepted the position of the assessee and has not imposed any transfer pricing adjustment, i.e., has not imputed any notional interest in respect of such irrecoverable loan amount.

37. Without prejudice to the above contentions, the ld AR would submit that even if the TPO imputes notional interest income on the aforementioned irrecoverable debt, it also requires corresponding deduction u/s 36(1)(vii) as the loan stands irrecoverable. Further, even the income relating to the aforementioned debt is hypothetical and also irrecoverable. Hence, the hypothetical income is not required to be explicitly accounted for in the books of accounts. In a scenario wherein notional interest is imputed on the loan amount, such interest shall also get accrued and form part of the loan. Even if an adjustment with respect to the notional interest is made, then a corresponding deduction under section 36(1)(vii) of the Act should also be provided in respect of the notional interest forming part of the loan, which would be written off as irrecoverable by the assessee. Accordingly, it is submitted that the net income in any case would be NIL from this transaction.

38. The ld DR presented the following arguments –

Loan Resulting out of Demerger Rs.74.21 Crores

In this regard it is submitted that the loan was never written off. If the statement that the previous company itself considered these loans as irrecoverable is true SSI Ltd could have written it off prior to merger. This didn't happen. The reason was that the hope was still alive for the previous company as well as the appellant. The statement that no future economic benefit was expected must be supported by the action. But the action of the assessee is contrary to the claim. It is not written off.Only provision is made. The reason for making provision without complete write off is that the provision can be reversed at any point on recovery of the debt. This shows that the debt is not mere fictitious asset.

The AR borrowed support from AS 10 which talks about certainty of cost involved to recognise the cost of the asset as an asset (as evident form the AS 10 extract provided by the Ld. AR in page no 5 of his submission). However, in the case of appellant the cost of asset is not in question. The asset was taken over from the erstwhile company without encumbrances and uncertainty through a scheme of merger. Hence there is no substance in the statement of the assessee that the provision was created as per the AS 10.

In addition, the AR relied on the Judgement of Hon'ble SC in the case of UCO Bank, Calcutta Vs. Commissioner of Income Tax, West Bengal [Civil Appeal No 235 of 1996] and decision of Hon'ble Mumbai Tribunal in the case of Bombay Dyeing &Mfg Co Limited Vs. Addl. CIT / DCIT in ITA 928/M/2020 and 3299 & 2779/M/2019.

In this context it is placed that the decision of the Hon'ble SC was rendered in the context of a banking company that too in the context of a domestic transaction which doesn't involve either related party transaction nor international transaction and where there is no scope for profit shifting. Whereas the transaction of appellant in question involves international transaction and related party transaction with scope for profit shifting and the adjustment was made by the TPO with respect to

interest under Chapter X which contains special provisions relating to Avoidance of tax through international transactions with Associated Enterprises.

The Special bench decision in the case of Instrumentarium Corporation Ltd.v.Assistant Director of Income-tax, International Taxation-I, Kolkata reported in **[2016] 71 taxmann.com 193 (Kolkata - Trib.) (SB)** made it clear that the principle of commercial expediency which is applicable in the case of domestic transaction as approved in the case of SA Builders Ltd. v. CIT [2007] 288 ITR 1/158 Taxman 74 is not applicable to international transactions. Applying the same ratio, the decision of Hon'ble SC rendered in the context of unrelated party domestic transaction is not applicable to the international transaction with the AEs.

Moreover, the assessee is not in the banking business.

The question involved in the case of Bombay Dyeing (supra) is whether the Outstanding receivables with respect to guarantee fees and technical fee receivables of earlier years are falling within the ambit if international transaction or not (**Please refer para 22 to 23 of the Hon'ble tribunal's order**). It has no relevance to the case of the appellant. The case of the assessee is of loan which is clearly an international transaction covered u/s 92B of the Income Tax Act 1961.

In the case of Instrumentarium Corporation (supra) the question whether computation of income on basis of arm's length price does not require that assessee must report some income first, and only then it could be adjusted for ALP was answered yes. In addition, the question whether therefore, even when no income was reported in respect of an item in nature of income, such as interest, but substitution of transaction price by arm's length price resulted in an income, it could very well be brought to tax under section 92 was also answered yes. In such a circumstance the argument of the assessee that the loan transaction was nil in the books of the appellant holds no water.

Loans issued to XSL USA Rs. 98.61 Crore

In support of the above arguments the assessee relied on the cases of TRF Ltd VCIT 323 ITR 397 (SC) and Vijaya Bank Vs CIT 166 (SC). As stated in the case of Instrumentarium Corporation (supra) the ratio laid down in these cases are not relevant to determination of ALP and taxability of international transaction which is covered under Chapter X of IT Act 1961.

There is no substance in the argument of the assessee that the loan given to its AE is in the nature of informal capital or quasi equity or a shareholder activity. In the following cases the loan given to AEs are clearly made as international transaction and the interest needs to be charged at LIBOR Plus rate.

a. [2014] 50 taxmann.com 272 (Mumbai - Trib.)/[2014] PMP Auto Components (P.) Ltd. v. Deputy Commissioner of Income-tax - 7(1), Mumbai

b. [2018] 91 taxmann.com 357 (Bombay) Tooltech Global Engineering (P.) Ltd. v.Assistant Commissioner of Income-tax, Circle-7, Pune

c. [2015] 56 taxmann.com 358 (Mumbai) Melstar Information Technologies Ltd. v. Assistant Commissioner of Income-tax, Circle-8(2), Mumbai

d. [2015] 55 taxmann.com 523 (Delhi) Commissioner of Income-tax -I v. Cotton Naturals (I) (P.) Ltd

The request of the assessee to write off the interest determined at ALP u/s 36(1)(vii) is without any basis and is against the intention of the Chapter X of the IT Act 1961.

39. We heard the rival submissions and perused the material on record. The loan amount on which the notional interest is imputed consists of two parts. Rs.74.21 crores inherited from a SSI Ltd as part

of merger and an amount of Rs.98.61 crores which the assessee has lent to its AE. As per the financial statements of the assessee a provision is created and adjusted against these loans and the net amount is shown as NIL. The common submission of the ld AR with regard to the amount recoverable being shown as NIL in the books of accounts is that there is no future economic benefit is expected from these loans.

40. With regard to the amount inherited as part of merger, the contention of the TPO was that though the assessee has not given the loan, the assessee is compensated for adjusted during the acquisition process and technically the amount is receivable for the assessee on which interest adjustment is warranted. In this regard we notice on perusal of records that the loan is recorded as an asset since the assessee has adopted pooling of interest method whereby the assets and liabilities of the two companies are summed together and then netted. We also notice that the amount reflected as provision against the loan is adjusted against the reserves and therefore there is merit in the argument of the ld AR that the loan given is not part of the realisable value of the assets and liabilities of the merged entity which is discharged by issue of shares as part of the merger process by the assessee. In other words, through the acquisition process, the assessee in reality has not inherited the loans given as an asset. In our considered view therefore the reflection of the loan inherited as part of merger is only a book entry and does not amount to an international transaction resulting in any benefit to the assessee since there is no

realisable value for the asset. Accordingly we hold that no notional interest is chargeable on the said loan.

41. With regard to the loan lent directly by the assessee to its AE for Rs.98.61 crores, the argument of the ld AR is that loan transaction is in the nature of informal capital or quasi-equity and was merely a shareholder activity and does not fall within the purview of international transaction as defined in section 92 as there is no income arising on account of the transaction. We are unable to agree with this contention of the assessee for the reason that in a quasi equity or in a share holder activity the reward or benefit is not interest but an opportunity to own capital on certain favourable terms and at favourable prices and accordingly such transaction cannot be compared with a simple loan transaction where sole motivation and consideration for the lender is to earn interest on such loans. The fact that the assessee has not charged any interest on the loan does not change the character of the loan and the resultant ALP adjustment towards interest since the point of dispute is whether zero interest, or no interest , is good enough for computing the income where an arm's length interest must substitute this zero interest. Accordingly in our view, the submissions with regard to the loan being quasi equity or being a share holder activity are not tenable.

42. Now, whether an ALP adjustment is warranted with regard to the loan given by the assessee to its AE is the next issue to be considered here. From the perusal of the records, it is clear that the

assessee has created a provision of against the loan on the basis that there is no economic benefit to be derived and there is no possibility of recovery in future. The provision thus created is adjusted against the loan amount and the net figure of NIL is shown in financial statements of the assessee. It should be mentioned here that the provision is created and adjusted against the loan for the year ended 31.03.2011 and the status remains the same till the financial year of the year consideration. The contention of the ld DR is that there is no actual write off since it is only a provision that is created in this case and therefore the interest adjustment towards loan receivable is justified. With regard to the question of whether the provision adjusted against the loan whether amounts to actual write off is settled by the Hon'ble Supreme Court in the case of Vijaya Bank v. CIT, [2010[323 ITR 166 (SC) where in it was held that the provision for doubtful debt debited to the P&L account constitutes an actual write off if the same is simultaneously reduced from the loans & advances/debtors and is shown as net of such provision. Accordingly in the year in which the provision is created by debiting to the P&L account would result in actual write off if the loan amount is shown net of provisions i.e. 31.03.2011. Though it is contended by the ld DR that the ratio laid down in this case is not relevant to determination of ALP and taxability of international transaction which is covered under Chapter X of the Act, in assessee's case there is no amount reflected as loan in the year under consideration and the balance carried is NIL since financial year 31.03.2011. In our considered view therefore there cannot be an

adjustment towards interest on loan when the loan amount itself is NIL during the year under consideration. Accordingly we hold that the notional interest charged on the loan given by the assessee to its AE which is written off and reflected as NIL in financials is to be deleted. Before parting, we would like to make a mention that the provision created towards the loan which is routed through the profit and loss account in the first year of creation i.e. during FY 2010-11 should have been part of the operating cost whereby the same should have been considered for the purpose ALP in that year.

43. The rest of the grounds pertaining to TP adjustment have become academic in the light of our decision given in this order. Ground no 18 is with respect to levy of interest u/s.234A where it is contended that the assessee has filed the return of income within the due date as prescribed u/s.139(1) and therefore the levy of interest is not warranted. In this regard we direct the AO to verify and delete the interest in accordance with law.

44. Ground 19 and 20 are consequential.

45. In the result, the appeal is partly allowed.

Pronounced in the open court on this 21st day of December, 2022.

(N V VASUDEVAN)	(PADMAVATHY S)
VICE PRESIDENT	ACCOUNTANT MEMBER

Bangalore,
Dated, the 21st December, 2022.
/*Desai S Murthy /*

Copy to:

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

By order

Assistant Registrar
ITAT, Bangalore.