

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

BEFORE SMT. BEENA PILLAI, JUDICIAL MEMBER
AND
SHRI LAXMI PRASAD SAHU, ACCOUNTANT MEMBER

IT(TP)A No.153/Bang/2022
Assessment year : 2017-18

MetricStream Infotech (India) Private Limited, # 23 & 24, AMR Tech Park 4B, Honagasandra Village, Begur Hobli, Bengaluru – 560 068. PAN : AACCM 4991K	Vs.	The Assistant Commissioner of Income Tax, Circle 4(1)(2), Bangalore.
APPELLANT		RESPONDENT

Appellant by	:	Shri Padam Chand Khincha, CA
Respondent by	:	Shri Jt.CIT(DR)(ITAT), Bengaluru.

Date of hearing	:	03.04.2023
Date of Pronouncement	:	16.06.2023

ORDER

Per Laxmi Prasad Sahu, Accountant Member

This appeal is directed against the final assessment order dated 28.01.2022 passed u/s. 143(3) r.w.s. 144C(13) r.w.s. 144B of the Income-tax Act, 1961 [the Act] by the Assessing Officer, National Faceless Assessment Centre, Delhi [NFAC], Delhi for the assessment year 2017-18.

2. The grounds of appeal raised by the assessee are as follows:-

GENERAL GROUND

1. The Orders passed by learned Assistant Commissioner of Income Tax, Circle — 4(1)(2), Bangalore (hereinafter referred as "AO" for brevity), learned Deputy Commissioner of Income Tax (Transfer Pricing Officer) — 2(1)(1), Bangalore (hereinafter referred as "TPO" for brevity) and the Honourable DRP-2, Bengaluru ("AO", "TPO" and DRP collectively referred as "lower authorities" for brevity) are bad in law and liable to be quashed.

GROUND RELATING TO TRANSFER PRICING — LEGAL ISSUES

2. The learned AO has erred in making a reference for the determination of the Arm's Length Price of " the international transactions to the TPO without demonstrating as to why it was necessary and expedient to do so.
3. The lower authorities have erred in passing the Order without demonstrating that the Appellant had any motive of tax evasion.

GROUND RELATING TO TP ADJUSTMENT IN SOFTWARE DEVELOPMENT SEGMENT

4. The learned AO has erred in making transfer pricing adjustment of Rs. 26,54,86,758/- towards international transactions in software development segment.
5. The lower authorities have erred in:
 - (i) Conducting a fresh TP analysis despite absence of any defects in the transfer pricing analysis submitted by the Appellant;
 - (ii) Adopting inappropriate filters like one sided turnover filter, 25% RPT filter, etc. in the process of selecting comparables and not adopting appropriate filters like onsite revenue filter, etc;

- (iii) Selecting inappropriate comparables and selecting companies as comparables even though they are not comparable in terms of functions performed, assets utilized, risks assumed, size, one sided turnover, unusual business circumstances, high margin, etc. The lower income tax authorities have erred in adopting the following companies as a comparables:

Larsen & Toubro Infotech Ltd
R Systems International Limited
Mindtree Ltd/
Infobeans Technologies Limited
Persistent Systems Ltd
Tata Elxsi Ltd
Aptus Software Labs Private Limited
Nihilent Ltd
OFS Technologies Limited
Cygnet Infotech Pvt. Ltd
Infosys Ltd
Threesixty Logica Testing Services Pvt. Ltd.
Cybage Software Pvt. Ltd
Consilient Technologies Pvt. Ltd.

- (iv) Rejecting the following comparables selected/proposed by the Appellant For unjustified reasons:

Sagarsoft (India) Limited
Evoke Technologies Private Limited
Sasken Communication Technologies Limited
Sankhya Infotech Limited
Athena Global Technologies Limited
Isummation Technologies Private Limited
E-Zest solutions Limited
Nitor Infotech Private Limited

6. The lower authorities have erred in incorrectly computing the operating profit margin of following comparables:

Harbinger Systems Pvt Ltd

7. The lower authorities have erred in:
- (i) Not making proper adjustment for enterprise level and transactional level differences between the Appellant and the comparable companies;
 - (ii) Not recognizing that the Appellant was insulated from risks, as against comparables, which assume these risks and therefore have to be credited with a risk premium on this account;
 - (iii) Not providing working capital adjustment while computing the Arm's length price.

GROUND'S RELATING TO TP ADJUSTMENT IN MARKETING SUPPORT SEGMENT

8. The learned AO has erred in making transfer pricing adjustment of Rs. 3,73,16,901/- towards international transactions for marketing support segment.
9. The learned DRP has erred in confirming the action of the TPO in:
- i) Conducting a fresh transfer pricing analysis despite absence of any defects in the transfer pricing analysis submitted by the Appellant;
 - ii) Adopting inappropriate filters like one sided turnover filter, 25% RPT filter, etc, in the process of selecting comparables and not adopting appropriate filters like onsite revenue filter etc;
 - iii) Incorrectly computing the operating margins of comparables; and
 - iv) Adopting following companies as comparables even though they are not comparable in respect of functions performed, risks assumed, assets utilized, size, turnover, despite having unusual business circumstances or high margins, substantial RPT, etc.

Focus Suites Solutions & Services Ltd

Axience Consulting Pvt. Ltd.
Pressman Advertising Limited
Scarecrow Communications Limited
Red Baron Integrated Services Pvt Ltd
Lintas India Pvt. Ltd.
Majestic Research Services And Solutions Limited
Platinum Advertising Pvt. Ltd
Cheil India Pvt. Ltd.

- v) Rejecting the following comparables selected/proposed by the Appellant for unjustified reasons:

ICRA Management Consulting Services Limited
MCI Management (India) Private Limited
Kestone integrated Marketing Services Pvt Ltd (Seg)
Killick Agencies & Marketing Limited
Cyber Media Research & Services Limited
Priya International Limited (Segmental)
Chaman Lal Lakhmi Dass Plastics Private Limited
BNR Udyog Limited (Seg)
Fusion Events Limited

10. The lower authorities have erred in:

i) Not making proper adjustment for enterprise level and transactional level differences between the Appellant and the comparable companies.

ii) Not recognizing that the Appellant was insulated from risks, as against comparables, which assume these risks and therefore have to be credited with a risk premium on this account; and

iii) Not providing working capital adjustment while computing the Arm's length price.

OTHER GROUND

11. The learned AO has erred in considering total income as Rs.68,55,84,719/- in the computation sheet of the order,

instead of Rs.68,51,84,719/- as mentioned in the order and as returned by the Appellant.

12. The learned AO has erred in charging interest u/s 234A of the Act despite return of income being filed in time.
13. The learned AO has erred in charging excessive interest u/s 234B of the Act.
14. The lower authorities have erred in levying interest of interest u/s 244A, 234A of Rs.11,07,893/-, 234B of Rs.6,45,80,647/- and 234D of Rs.1,262/-. On the facts and circumstances of the case, interest under various sections of the Act is not leviable.

The Appellant submits that each of the above grounds/ sub-grounds are independent and without prejudice to one another.

The Appellant craves leave to add, alter, vary, omit, substitute or amend the above grounds of appeal, at any time before or at, the time of hearing, of the appeal, so as to enable the Income-tax Appellate Tribunal to decide the appeal according to law.

The Appellant prays accordingly.”

3. The assessee is a wholly owned subsidiary of MetricStream , USA. It is engaged in the business of providing software development services and marketing support services to MetricStream , USA. The services are provided on cost plus basis.

4. A reference was made to the TPO for determining ALP of international transactions entered into and the TPO vide order dated 28.01.2021 u/s 92CA of the Act Din & Order No. ITBA/TPO/F/92CA3/2020-21/1030159189(1) proposed the following TP adjustments:-

Name of the Segment	Segmental Revenue of Appellant	Average margin	TP Adjustment
Software development segment	2,54,23,46,120/-	20 comparables with median of 26.18%.	29,65,34,910/-
Marketing support services segment	48,55,98,855/-	11 comparables with median of 19.53%	3,73,16,901/-
Total			33,38,51,811/-

5. The AO passed the draft assessment order under section 143(3) r.w.s. 144C of the Act dated 26.03.2021 incorporating the TP adjustment of Rs. 33,38,51,811/- made by the TPO. Aggrieved, the assessee filed objections before Id. DRP. Pursuant to the directions of the DRP, an order giving effect to DRP directions was passed by TPO dated 22.01.2022 making total TP adjustment of Rs.30,28,03,659/- as under:-

Name of the Segment	Average margin	TP Adjustment
Software development segment	22 comparables with median of 24.80%	26,54,86,758/-
Marketing support services segment	11 comparables with median of 19.53%	3,73,16,901/-

6. Consequently the AO passed the final assessment order dated 28.01.2022 and assessed income at Rs. 68,51,84,719/-, against which the assessee is in appeal before the Tribunal.

7. **Ground No.1, 4 & 5(i)** are general in nature, hence does not require adjudication. In ground No.2 & 3, the assessee raised legal

issue, which was not argued by the assessee. Therefore, it is dismissed as not pressed.

RPT Filter - Ground No.5(ii)

8. The Id. AR did not argue on the turnover filter and onsite revenue filter. He submitted that RPT ratio has to be calculated on aggregate basis taking ratio of RPT incomes plus RPT expenses by sales in the case of Cygnet Infotech Pvt. Ltd. and Three Sixty Logica Testing Services Pvt. Ltd. If the RPT ratio is not applied on aggregate basis, the whole purpose of applying RPT filter would be lost because companies having substantial RPT will be selected. For example, related party purchases may be sold to third parties and thus profits from such transactions may be tainted. Similarly, purchases from third parties may be sold to related parties, and profits from such transactions may be tainted. This would mean that approx. half of profit of such company may come from tainted transactions. He relied on the decision of the Coordinate Bench of the Tribunal in the case of *JCIT, LTU (OSD) Circle-1, Bangalore vs M/s.Toyota Kirloskar Motors Private Limited (ITA No.2016/Bang/2018) for AY 2013-14* wherein the A.O. was directed to calculate RPT ratio on an aggregate basis taking the ratio of RPT income plus RPT expenses by sales across the board for all the comparable companies.

9.1 It was submitted that the TPO has applied RPT of 25% of sales as threshold limit for related party transactions. In this regard, he submitted that RPT should be 15% of the sales instead of 25% of the

sales. This would result in selection of better uncontrolled comparable transactions as envisaged in the Indian TP regulations and referred to the submissions at Pg 694-695 of PB I. In this regard, reliance was placed on the following decisions, wherein it was held that RPT > 15% of sales is an appropriate filter:-

- ANSR Global Corporation (P.) Ltd vs ACIT [2022] 139 taxmann.com 283 (Bangalore - Trib.) for AY 2016-17 (Para 17 at Pg 2340 of Paper Book III-Case law Compilation)
- Autodesk India (P.) Ltd. [2018] 96 taxmann.com 263 (Bangalore - Trib.)

9.2 In view of the above, the ld. AR submitted that the RPT filter of 15% over sales should be applied on an aggregate basis.

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

9.4 After hearing both the sides, perusing the entire material on record and the orders of the lower authorities, we notice that The coordinate Bench of the Tribunal in the case of *JCIT, LTU (OSD) v. Circle-1, Bangalore vs M/s.Toyota Kirloskar Motors Private Limited (ITA No.2016/Bang/2018) dated 18.8.2021* has held that the RPT ratio has to be consistently calculated on an aggregate basis taking the ratio of RPT income plus RPT expenses by sales. The relevant observations are as follows:-

“7.4 We have heard rival submissions and perused the material on record. There is nothing on record to suggest how RPT ratio has been calculated for all the comparable companies. The learned AR has argued that the TPO in order to retain Tata Motors Ltd. and Maruti Suzuki India Limited has deviated and adopted a new mechanism for computing RPT ratio. On a query from the Bench how RPT ratio has been calculated for other comparables, the learned AR has unable to point out the same.

The RPT ratio has to be consistently calculated on an aggregate basis taking the ratio of RPT income plus RPT expenses by sales. The said position was adopted by the Revenue in the past years. In this regard, the TPOs order in assessee's own case for assessment year 20072008 has been placed on record. A perusal of the same it is clear that RPT ratio has been calculated taking both RPT income transactions plus RPT expenses transactions on aggregate basis. On the facts of this case, it is not clear how RPT ratio has been calculated for Tata Motors Limited vis-à-vis other comparable companies. Therefore, this issue is restored to the files of the A.O. The A.O. is directed to calculate RPT ratio on an aggregate basis taking the ratio of RPT income plus RPT expenses by sales across the board for all the comparable companies (including Tata Motors Ltd. and Maruti Suzuki India Limited).

7.5 Therefore, ground No.2 is allowed for statistical purposes.”

9.5 Following the above decision, we direct the AO to calculate RPT ratio on aggregate basis considering the RPT income plus RPT expenses by sales for all the comparable companies.

9.6 The issue regarding adoption of 15% RPT filter was considered by the coordinate Bench of the Tribunal in the case of Barracuda Networks India Pvt Ltd. in paras 21 to 22 wherein it was noted that the Hon'ble High Court of Karnataka in *PCIT v. Yodlee Infotech P. Ltd. in ITA NO.685/2017 dated 28.6.2018* had upheld the application of 15% RPT filter. Similarly, 15% RPT filter was upheld in the decision cited by the Id. AR in the case of *Autodesk India (P) Ltd. [2018] 96 taxmann.com 263 (Bang. Trib)*. It is ordered accordingly. Ground No.5(ii) is allowed.

9. The assessee vide **ground No.5(iii)** listed above seeks exclusion of companies on different parameters. On going through the order of DRP, we did not find that the ld. DRP has decided on the basis of functionality or not. Further, we note from the objections raised before the ld. DRP at No.6(c) which is as under:-

“Adopting companies as comparables even though they are not comparable in respect of functions performed, risk assumed, assets utilized, size, turnover, despite having unusual business circumstances or high margins, substantial RPT etc.”

10.1 The ld. DRP has decided the issue on the basis of turnover filter and functions performed by the comparable companies have not been decided. The ld AR of the assessee during the course of hearing did not argue on the basis of turnover filter, but he argued on the functions performed and other filters vide its written submissions filed which is placed on record. Since the ld. DRP has not decided on the basis of functional comparability and other filters, therefore, we think it fit to remand the issue to the file of ld. DRP for decision on functional comparability. Ground No.5(iii) is allowed for statistical purposes.

10. The ld. AR submitted that **in ground No.5(iv)** the following companies are requested to be included in the comparables.

Sagarsoft India Limited

11. The ld. AR submitted that the TPO and DRP held that this company is functionally different as it is into support services which include system administration, Human resource and training and facilities which fall under category of information security

management system. He further submitted that the company has single segment of Software Development Services and is therefore functionally similar and it passes all filters applied by the TPO. The DRP in Appellant's own case for AY 2018-19 has held Sagarsoft to be functionally similar. He also relied on this Tribunal decision in the case of *Quicklogic Software (India) Pvt. Ltd. vs DCIT, Circle-3(1)(1), Bengaluru (IT(TP)A No. 181/Bang/2022)* for AY 2017-18.

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

11.2 We have heard both the parties and perused the material on record. This issue was considered by the coordinate Bench of the Tribunal in the case of *Quicklogic Software (India) Pvt. Ltd. (supra)* where it was held as under:-

“13.4 In respect of Sagarsoft (India) Ltd., the company has been rejected by the Ld.TPO as he found to be engaged in providing system administration, human resources and training and facilities. The Ld.AR submitted that, the company is engaged in the business of software development service segment along with system administration and that this fact has been not considered by the Ld.TPO.

13.5 In respect of Akshay Software Technologies Ltd.,
.....

13.6 On the contrary, the Ld.DR placed reliance on orders passed by authorities below.

13.7 We note that above two comparables has not been verified by the Ld.AO/TPO in detail. We are therefore remanding these comparables also to the Ld.AO/TPO for a denovo verification.

13.8 The principles laid down by this Tribunal in various cases shall be kept in mind while considering the comparability of all these with that of assessee, having regards to the FAR analysis.”

11.3 We note from Note 16 @ page 1391 of PB which is note of the Profit & Loss account that this company has revenue from operations from software development at Rs.162,978,168 for YE 31.3.2017 and Rs.142,412,060 for YE 31.3.30216. We further noted from the page No. 1393 - **Business overview** in which it has been reported as under:-

“Your company is engaged in the business of providing IT services, consultancy, technology and next generation services. It provides business and technology and technology related services to corporations and has made decent progress in the recent years in consolidations its business in all service areas including new service lines and in acquiring new clients in cloud and other new age technologies.....”

11.4 We further noted from significant accounting policies at Sl. No. 17 Segmental reporting :-

“As the company was engaged only in software development and Consultancy during the year, business segment reporting is not applicable.”

11.5 Following the above decision, and our observations from the financial statements we remit this issue to the TPO/AO for fresh verification and decision in accordance with law, after providing assessee opportunity of hearing.

Evoke Technologies Private Limited

12. The TPO excluded this company for the reason that the company is functionally different. Before the DRP the assessee raised objection

& the DRP upheld the same and observed that data provided in annual report with regard to export revenue is unreliable.

12.1 The Id. AR submitted that the company has single segment of Software Development Services and is therefore functionally similar. This company passes all filters applied by the TPO. He relied on the decision of *Quicklogic Software (India) Pvt. Ltd. vs DCIT, Circle-3(1)(1), Bengaluru (IT(TP)A No. 181/Bang/2022) for AY 2017-18* to submit that this company has to be included in the comparables list.

12.2 The Id. DR relied on the orders of lower authorities.

12.3 We have heard the rival submissions and perused the material on record. In the case of *Quicklogic Software (India) Pvt. Ltd. (supra)*, this Tribunal held as under:-

“13.1 It is submitted by Ld.AR that Batchmaster Software Pvt. Ltd. and DCIS DOT COM Solutions India Pvt. Ltd. was ignored by the Ld.TPO as it was reflecting in the search matrix carried out by him. Evoke Technologies Ltd. was rejected by the Ld.TPO for the reason that it supplies end to end services. The Ld.TPO also noted that it may be included in the services other than IT services.

13.2 It is thus submitted by the Ld.AR that in respect of the above three comparables, the Ld.TPO has not considered the functions performed and has cherry picked the comparables without going through the actual functions and annual reports. We are therefore directing these comparables to be reconsidered by the Ld.AO/TPO based on the annual reports.

13.3 The Ld.TPO shall consider these comparables after verifying the FAR of these comparables with that of assessee.

Accordingly, Batchmaster Software Pvt. Ltd., DCIS DOT COM Solutions India Pvt. Ltd. and Evoke Technologies Ltd. for denovo consideration to Ld.AO/TPO.”

12.4 We further observed that the Id. DRP have observed that the figures are wrongly reported in the schedule NO. 2.29 & 2.16 & 2.26 in the financial statement in regard to the Export Turnover but this aspects were not discussed in the above said order as relied by the Id. AR, therefore this decision is not applicable. For the sake of convenience we are reproducing the findings of the Id. DRP as under:-

“Having considered the submissions, and on perusal of the annual report, we note that in the statutory auditor’s report, it is stated in note 2.29 that the financial statements include branch revenue of Rs.1605 lakh and branch net-profit of Rs.2.19 lakh based on audited financial statement of the Branch outside India. Also, as per the geographic segmentation information, the revenue from India was given to be Rs.7214.60 lakhs and that the revenue from US was given to be Rs.160.9 lakh. Thus, the export revenue constitutes only 18.19% of the total revenue. Whereas the Note 2.16 shows export revenue of Rs.87.58 Crores as against total revenue of Rs.88.20 crores which is contradictory to the geographical segment information given at Note 2.26. Therefore, this company cannot be considered as comparable in view of unreliable data provided. In the annual report with regard to export revenue. In the absence of reliable information on export turnover it is not possible to ascertain whether the company satisfies export turnover filter adopted by the TPO. Hence the rejection of the company by TPO is upheld.”

12.5 From the above observation of the Id. DRP we also note from financial statement that the Id. DRP have rightly observed that the figures are wrongly reported. Considering the above findings, in the absence of the correct reporting of the financial data by the

comparable company, even if it satisfies the FAR & filters applied by the TPO, this company cannot be considered as comparable company.

Sasken Communication Technologies Limited

13. The TPO observed that the company is functionally different and fails export revenue filter. The DRP held that the company is not comparable because it is engaged in diversified activities, has R&D activities and owns patents.

13.1 The Id. AR submitted that the company is functionally similar as it is primarily engaged in software consulting and development. The company passes all filters including export revenue filter as applied by the TPO. He referred to pg. 1440, 1446-1450 of PB-II and submission at pg. 711 of PB-I. The DRP in Appellant's own case for AY 2018-19 has held Sasken to be functionally similar. Considering the arguments advanced from both the sides, we remit the issue to the AO/TPO for verification of the facts in AY 2018-19 and present year and for fresh decision in accordance with law.

Sankhya Infotech Limited

14. The TPO & DRP held that the company is functionally different as it is engaged in diversified activities and segmental data is not available. The Id. AR submitted that the company is functionally similar as it provides solutions and services in relation to software development and it passes all filters applied by the TPO. The Id. AR also referred to pg. 1452-1456 of PB-II and submission at pg. 707-708 of PB-I and also referred to pg.1469-1470 of PB-II and submission at

pg. 708-709 of PB-I. Considering the arguments from both the sides and findings recorded by the lower authorities, we remit this issue to the AO/TPO for fresh consideration.

Athena Global Technologies Limited

15. The TPO & DRP rejected the company on the ground that it fails networth filter. The Id. DRP further noted that the negative net worth filter eliminates the intrinsically sick and non-performing companies owing to various internal reasons. The Id. AR submitted that the company is functionally similar as it is primarily engaged in software development. This company passes all filters applied by the TPO. He submitted that Companies having similar FAR cannot be excluded on the basis of negative net worth filter and relied on decision of *Gillette Diversified Operations Pvt Ltd [TS-218-ITAT-2016(DEL)-TP]*. 151/DEL/2013 AY 2005-06, Order dated 01.04.2016

15.1 The Id. DR relied on the orders of lower authorities.

15.2 We have heard both the parties and perused the material on record. We notice from the financial statement that the net worth of the company has been eroded and it is negative net worth company. During the FY 31.3.2016 the negative net worth was Rs. 10.31 crores and in the current year Rs.11.91 crores. Resultantly, the negative net worth is increased by Rs.1.60 crores. However, the revenue from operations has been increased by Rs.2.07 crores, The total net profit before adjusting exceptional item is Rs.0.16 crores and profit from operations before adjusting exceptional item and taxes was decreased

by Rs.0.12 crores. On observation of the financial statement, the negative net worth of the company has increased. Further on perusal of the Note No.18 revenue from operations, the company has shown consulting income of Rs.10.58 crores and as per Note No.36, which is placed at Pg. 1490 of PB, states as under:-

“The company’s operations primarily relate to providing information technology (IT services). Accordingly, the company operates in a single segment which represents the primary segment. Secondly, segmental reporting is performed on the basis of geographical location of the customers as under:-

US	Rs.8.20 crores
UK	Rs.0.63 crores
India	Rs.1.62 crores
Norway	<u>Rs.0.13 crores</u>
Total	<u>Rs.10.58 crores</u>

15.3 Since the lower authorities have rejected this company only on the basis of negative net worth, which leads to intrinsically sick and non-performing companies, but FAR analysis has not been done by both the parties. If the company passes FAR applied by the Id. TPO, the company cannot be excluded only because of the negative net worth. This view is supported in the judgment relied by the AR in the case of *Gillette Diversified Operations Pvt Ltd* (supra) in which it has been held as under:-

24. Ld. TPO rejected two comparables which are discussed as under:-

a. Argus Cosmetic Ltd.

.....

b. Muller & Phipps India Ltd.

i. The Id TPO has excluded this comparable stating that it has a negative net worth for the year 2005 hence it is not fit comparable to be taken. On appeal before the Id CIT(A) the assessee submitted that the TP regulation and OECD guidelines do not suggest that loss making company should not be taken as comparable. The Id CIT (A) has hold that this company is not simply the loss making company but is also a company having negative net worth and according to him when a company suffers from erosion of its wealth because of continuous loss, same cannot be taken as comparable. The case laws relied upon by the appellant were also rejected as according to him those were relied upon high loss making company and not for a negative net worth comparables.

ii. Before us the Id AR submitted that merely because a company is having negative net worth it cannot be excluded as comparable if the functions performed, Assets deployed and risk assumed are comparable with the business of the company. Against this the Id AR relied on the order of the lower authorities

25. We have carefully considered the rival contentions. According to rule 10(B)(a) of the Income Tax Rules the comparability of international transactions with an uncontrolled transaction shall be judged with respect to the functions performed, taking into account assets employed or to be employed and the risks assumed, by the respective parties to the transactions. According to the Rule 10B(3) a uncontrolled transaction shall be comparable to an international transaction none of the differences, if any, between the transactions being compared, or between the enterprises entering into such transactions are likely to materially affect the price or cost charged or paid in, or the profit arising from, such transactions in the open market. We do not find any such exception provided under the Income Tax Rules 1962. Furthermore neither the Id CIT(A) nor the Id AO had pointed out that how the negative net worth of the comparable make the price of the goods or the profitability arising from such transaction not comparable. Merely because the company is having negative net worth but when the FAR is comparable, it cannot be said to be non comparable unless it is shown that how the negative net worth of

the company has impacted the profitability of the comparable company. We have also noted the issue decided by Special Bench in the case of DCIT V Quark Systems Limited in 2010-TII-02-ITAT-CHD-SB-TP where in the negative net worth company was considered and it was held that business organization with negative net worth cannot be treated at par with a normal business organization. However while considering that issue the comparable was also functionally not comparable in that case. Therefore there was no view expressed in that decision that though comparable has similar FAR still negative net worth company is required to be excluded without showing the impact of negative net worth on the profitability of the company. In view of this we direct the inclusion of this Company i.e. Muller & Phipp India Limited as comparable for the purpose of determining arms length price.

15.4 Accordingly, we remit this issue to the AO/TPO for fresh consideration as per above directions.

E-Zest Solutions Limited

16. The TPO & DRP excluded this company on the ground of functionality as it is engaged in ITeS. The ld. AR submitted that it is functionally similar as it provides software development services and passes all filters applied by the TPO.

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

16.2 We have heard both the parties and perused the material on record. On going through the order of the lower authorities they have excluded this company by holding that the company is engaged in ITeS. We note that in the case of Global E- Business Operations (P.) Ltd. v. Deputy Commissioner of Income Tax in IT (TP) A No. 174/BANG/2022 order dated 16.11.2022 reported in [2023] 147

taxmann.com174 (Bangalore- Trib) for AY 2017-18 it has been held that the company is engaged in ITeS. The relevant part of the order is as under:-

13.1 At the time of hearing, the ld. A.R. pressed only following 4 comparables for inclusion:

- a. Bhilwara Infotechnology Limited;
- b. R Systems International Limited;
- c. ISN Global Solutions Private Limited; and
- d. E-ZestSolutions Limited;

13.2 The other comparables are not pressed. Accordingly, dismissed as not pressed.

Bhilwara Infotechnology Limited & R Systems International Limited:

13.3

13.4

ISN Global Limited:

13.5

13.6

13.7

E-ZestSolutions Limited:

13.8 Now coming to E-ZestSolutions Limited, the ld. DRP observed that on perusal of the annual report it was noted that the company has income from sale of services amounting to Rs. 81.46 crores as per the information statement of profit and loss account given at page nos. 123-125 of the annual report. The company reported that it is exclusively engaged in the business of IT enabled services. This is the context of on segment reporting and is considered to constitute a single primary segment. As it is

part of search matrix of the TPO and functionally similar to the assessee, the TPO is directed to include the comparable for the comparability analysis under ITES segment if it satisfies the filters adopted by the TPO.

13.9 However, the AO/TPO has not included E-ZestSolutions Ltd. in the list of comparables while determining the ALP. However, we direct the AO/TPO to pass the above order in conformity with the order of the Ld. DRP as recorded in para 13.8 above. This ground of appeal of the assessee is allowed.

16.3 In the present case the assessee is engaged in the business of software development services whereas E-Zest Solutions Ltd. is ITeS company. The software development service business company cannot be compared with the ITeS company. Respectfully following the above judgment, we reject the contention of the assessee and uphold the orders of lower authorities.

Isummation Technologies Private Limited

17. The TPO & DRP rejected this company as it functions overlap into both IT & ITeS but has no segmental information. The ld. AR submitted that the company is functionally similar as it is primarily engaged in rendering software development services having single segment and passes all filters applied by the TPO. Further, the DRP in Appellant's own case for AY 2018-19 has held this company to be functionally similar and included in the final list.

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

17.2 Considering the arguments from both the sides, we note that this company has been considered in the case of Xchanging Solutions Ltd.

[2023] 147 TAXMANN.COM 404 (Bangalore Trib) that it is engaged in the business of software development services. The relevant part of the order is as under:-

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

20. The next prayer of the Id. 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.

Evoke Technologies

22.

23.

24.

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 Id. 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 Id. AR relied on the decision of the coordinate Bench in the case of *EIT Services India (P.) Ltd. v. Dy. CIT* [IT (TP) A No. 210 (Bang.) of 2021, dated 22-8-2022].

26. We heard the Id. 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.* Insummation 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.

17.3 Respectfully following the above judgment of the coordinate Bench of the Tribunal, we direct the AO/TPO to include this company in the list of comparables.

Nitor Infotech Private Limited

18. This company was rejected since it did not appear in the search matrix of the TPO. The ld. AR submitted that the financial data relating to this company is available in public domain. It is functionally similar as it provides consultancy and technology services in the area of Business intelligence, collaboration, portals and performance management domain and passes all filters applied by the TPO.

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

18.2 We have heard both the parties and perused the material on record. During the course of hearing, the ld. AR submitted that the data is available in public domain and it is functionally comparable, but during the course of search process by the ld. TPO, it was not appearing in the search process. The ld. AR of the assessee has filed paperbook in which the financial statement of this company is placed at page No.1561 to 1575. We remit this issue to the AO/TPO for examination whether this company passes the FAR and decide the issue afresh as per law.

19. **Ground No.6** is regarding incorrect computation of margin of Harbinger Systems Pvt Ltd. The ld. AR submitted that the TPO has taken margin at 11.16% whereas the correct margin of this company comes to 8.12%. The variation is due to incorrect treatment by the TPO of certain items such as forex gain, bad debts, donation, etc. Therefore, it was submitted to direct the TPO to adopt correct margin after examination of the data. After hearing both the parties and perusing the material on record, we remit this issue to the AO/TPO for verification of the correct margin of Harbinger Systems Pvt Ltd. and accordingly adopt the same for margin computation as per law.

MARKETING SUPPORT SEGMENT

20. The assessee reported international transactions in respect of Marketing Support Segment (MSS). Metricstream US provides enterprises-wide GRC and quality solutions for global corporations. The solutions offered by Metricstream US are used in diverse industries such as pharmaceutical, medical device, high tech manufacturing, energy, financial services, healthcare, manufacturing, food and beverages and automotive to manage quality process, corporate policies, manage regulatory and industry mandate compliance and corporate governance initiatives. Metricstream India is engaged by Metricstream US to provide sales and marketing services for metricstream products. As per the agreement, Metricstream India has been appointed as non-exclusive service provider to provide sales and marketing services in relation to metricstream products. Metricstream India is compensated on a cost plus basis on the services

rendered. The total value of the sales and marketing services transaction undertaken during the year 2016-17 is Rs.48.56 crores. The characterisation of entity is “given the functions, risks and intangible assets of each entity (both related and unrelated parties) how should group entities most accurately be characterised in relation to each controlled transaction.” The assessee has applied TNMM method as the most appropriate method and OP/OC has been taken as PLI in its TP analysis. The TPO noticed that 10 companies were selected for MSS segment and accepted only one comparable viz., Majestic Research Service & Solutions Ltd. and rejected the other companies. The TPO applied certain filters and selected 11 companies including Majestic Research & Solutions Ltd. and calculated Median at 19.53%. The assessee filed objections which was not accepted by the TPO and finally the TPO calculated adjustment of Rs.3,73,16,901. Before the TPO, the assessee also filed additional comparables of 5 companies but it was not accepted. Before the DRP, the assessee filed objections which were also rejected. Accordingly, the AO passed final assessment order.

20.1 The assessee seeks exclusion of certain companies selected by the TPO on the ground of non-comparability in terms of functions performed, assets utilized, risks assumed, etc. as per ground No.9(iv). As per ground No.9(iv), the assessee sought exclusion for the following companies:-

- (i) Focus Suites Solutions & Services Limited
- (ii) Axience Consulting Private Limited

- (iii) Pressman Advertising Limited
- (iv) Scarecrow Communications Limited
- (v) Red Baron Integrated Services Private Limited
- (vi) Lintas India Private Limited
- (vii) Majestic Research Services & Solutions Limited
- (viii) Platinum Advertising Private Limited
- (ix) Cheil India Private Limited

20.2 On going through the order of the Id. DRP, the above named companies sought for exclusion by the assessee has not been dealt by the Id. DRP company wise on FAR basis. Therefore this issue is remitted back to the file of the Id. DRP. The assessee has filed written synopsis before us in which it has challenged on different aspects for exclusion of the abovenamed companies which is placed on record. The assessee is directed to produce the necessary documents in support of its claim for exclusion of the companies before the DRP and the DRP is directed to decide the issue afresh as per law. Ground No.9(iv) is allowed for statistical purposes.

21. By **ground No.9(v)**, the assessee has sought for inclusion of following comparable companies in the marketing support segment:-

- ICRA Management Consulting Services Limited
- MCI Management (India) Private Limited
- Kestone integrated Marketing Services Pvt Ltd (Seg)
- Killick Agencies & Marketing Limited
- Cyber Media Research & Services Limited
- Priya International Limited (Segmental)
- Chaman Lal Lakhmi Dass Plastics Private Limited
- BNR Udyog Limited (Seg)
- Fusion Events Limited

21.1 During the course of hearing, the Id. AR submitted that the lower authorities have not decided the issue on the basis of documents submitted by the assessee, in this regard the Id. AR of the assessee also filed written synopsis in support of its claim which is placed on record. He therefore submitted that the matter may be sent back to the DRP. Considering the submissions from both the sides and going through the material on record, we deem it fit to remit the matter to the Id. DRP for fresh adjudication. The assessee is directed to produce the necessary documents in support of its claim for exclusion of the companies before the DRP and the DRP is directed to decide the issue afresh as per law. Ground No.9(v) is allowed for statistical purposes.

22. **Ground Nos. 7(i) & (ii) and 9 (i) to (iii)** was not argued by the assessee, therefore these are dismissed as not pressed.

23. **Ground Nos. 7(iii) and 10(iii)** by the assessee are with regard to grant of working capital adjustment in the SWD and MSS segments respectively which was rejected by the TPO and the DRP. The Id. AR submitted that that working capital adjustment is an accepted adjustment. The amount of working capital varies greatly, because of credit terms offered to buyer and credit terms available from creditors. Thus, the working capital materially affects the amount of net profit margin in the open market and same should be adjusted for. He relied on *M/s. Yahoo Software Development India Pvt. Ltd. vs JCIT*, Special Range – 7, Bengaluru IT(TP)A No. 178/Bang/2022 for AY 2017-18

and *M/s.Airlinq Technology Pvt. Ltd* vs DCIT, Circle 3(1)(1) Bangalore IT(TP)A No.231/Bang/2021 for AY 2016-17.

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

23.2 We have heard both the parties and perused the material on record. The coordinate Bench of the Tribunal in the case of *Yahoo Software Development India Pvt. Ltd. (supra)* considered this issue and held as under:-

“7. It is submitted that assessee had given working capital adjustment computation before the authorities below, however, the same were ignored by the Ld.AO and DRP. He placed reliance on the decision of the Coordinate Bench of this Tribunal in case of *Mobis India Ltd.* reported in (2013) 38 taxmann.com 231. In *Mobis India Ltd. (supra)*, it was held that, it is necessary to eliminate the difference which is possible only by computing the working capital adjustment in the hands of the comparables. Coordinate Bench relied on the decision of Hon’ble Chennai Tribunal observed that, the OECD guidelines are very clear and advocates adopting the rates of interest applicable to commercial enterprise operating in the same market as that of a tested party.

8. We are therefore of the opinion that the revenue was not justified in denying the working capital adjustment in order to bring the comparable companies for the purposes of broad comparison it is necessary to grant working capital adjustment that would eliminate the differences. The Ld.AO/TPO is directed to allow the working capital adjustment on actuals based on the materials already available on record.

Needless to say that proper opportunity of being heard must be granted to assessee.”

23.3 The coordinate Bench of the Tribunal in the case of *Airlinq Technology Pvt. Ltd (supra)* held that in keeping with the OECD guidelines, endeavour 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.

23.4 Following the above decisions, we direct the AO/TPO to grant working capital adjustment. Grounds No.7(iii) & 10(iii) of the assessee are allowed.

24. The assessee through **ground No.11** has submitted that in the final assessment order, total income was computed at Rs. 68,51,84,719/- after making TP adjustments of Rs.30,28,03,659/-. However, in the computation sheet annexed to the order, the learned AO has inadvertently considered total income at Rs.68,55,84,719/- instead of Rs. 68,51,84,719/-. A rectification application in this regard was filed on 24.02.2022 which is still pending for disposal. Therefore, it is submitted that the AO may be directed to consider the correct total income at Rs. 68,51,84,720/- in the computation sheet and computation of tax liability accordingly. Accordingly, after hearing both the parties, we remit this issue to the AO for verification of the correct total income and tax computation accordingly after giving the assessee opportunity of being heard.

25. **Ground Nos.12, 13 & 14** is consequential in nature.

26. In the result, the appeal of the assessee is partly allowed for statistical purposes.

Pronounced in the open court on this 16th day of June, 2023.

Sd/-

(BEENA PILLAI)
JUDICIAL MEMBER

Sd/-

(LAXMI PRASAD SAHU)
ACCOUNTANT MEMBER

Bangalore,
Dated, the 16th June, 2023.

/Desai S Murthy /

Copy to:

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

By order

Assistant Registrar
ITAT, Bangalore.