

आयकर अपीलीय अधिकरण, हैदराबाद पीठ
IN THE INCOME TAX APPELLATE TRIBUNAL
Hyderabad ' B ' Bench, Hyderabad

Before Shri Laliet Kumar, Judicial Member
And
Shri Manjunatha, G. Accountant Member

आ.अपी.सं / **ITA No.342/Hyd/2016**
(निर्धारण वर्ष / Assessment Year: 2011-12)

Pegasystems Worldwide India (P) Ltd Hyderabad PAN:AAECP3453F	Vs.	Income Tax Officer Ward 16(3) Hyderabad
(Appellant)		(Respondent)
निर्धारित द्वारा/Assessee by:	CAs Kranthi & Mrudulatha	
राजस्व द्वारा/Revenue by:	Shri M Vijay Kumar, CIT(DR)	
सुनवाई की तारीख/Date of hearing:	19/06/2024	
घोषणा की तारीख/Pronouncement:	07/08/2024	

आदेश/ORDER

Per Manjunatha, G. A.M

This appeal filed by the assessee is directed against the final assessment order passed by the Assessing Officer u/s 143(3) r.w.s. 144C(13) of the I.T. Act, 1961, in pursuant to the directions u/s 144C(5) of the I.T. Act, 1961 issued by the learned Dispute Resolution Panel-1, Bengaluru, dated 3.12.2015 and pertains to A.Y 2011-12.

2. The assessee has raised multiple grounds on various issues, including rejection of T.P documentation, rejection of use of multiple year data, negative working capital adjustment, inclusion of certain comparables and exclusion of certain comparables, but restricted its arguments only on the grounds relating to inclusion/exclusion of certain comparables. Therefore, we deem it not necessary to reproduce the grounds of appeal filed by the assessee.

3. The brief facts of the case are that the assessee company, M/s. Pegasystems Worldwide India (P) Ltd is a wholly owned subsidiary of Pegasystems Inc. USA . The company is engaged in providing software development services to Pega US and is remunerated on a cost plus mark-up basis. The assessee has filed its return of income for the A.Y 2011-12 on 7.10.2011 disclosing 'nil' income after claiming deduction of Rs.7,79,30,465/- u/s 10AA of the I.T. Act, 1961 in respect of its exports from SEZ Unit. The case was selected for scrutiny and during the course of assesment proceedings, the Assessing Officer noticed that the assessee has entered into international transactions with its AEs for providing software development services and receivables from AE. During the course of assesment proceedings, the issue of international transaction entered into by the assessee was referred to the TPO to determine the Arms' Length Price (ALP) of international transaction of the assessee with its AE. The TPO vide order u/s 92CA(3) dated 31.10.2014 determined the ALP for the provision of software

development services and arrived at higher value of Rs.2,229,53,557/- being transfer pricing adjustment u/s 92C of the Act. The TPO had also made transfer pricing adjustment of Rs.2,30,25,260/- towards notional interest receivable on outstanding receivable from AE. Against the draft assessment order, the assessee has filed objections before the DRP and contested TP adjustment suggested by the TPO in respect of provision of software development services and notional interest receivable on outstanding receivables from AE. The DRP-1 Bengaluru vide directions issued u/s 144C(5) of the I.T. Act, 1961 dated 3.12.2015 directed the Assessing Officer to recompute the deduction claimed u/s 10A of the Act by excluding communication charges from the total turnover. The DRP had also directed the Assessing Officer to delete TP adjustment made towards receivables and further issued direction to the Assessing Officer/TPO to exclude certain comparables for the reasons stated in their order dated 3.12.2015. In pursuant to the directions issued by the DRP u/s 144C(5) of the Act dated 3.12.2015, the Assessing Officer has passed the final assessment order u/s 143(3) r.w.s. 144C(13) of the I.T. Act, 1961 dated 27.01.2016 and made addition of Rs.3,29,70,250/- towards TP adjustment in respect of provision of software development services.

4. Being aggrieved by the final assessment order, the assessee is in appeal before us.

5. The first issue that came up for our consideration from Ground No.6 of assessee's appeal is inclusion of certain comparable companies like Evoke Technologies Pvt Ltd, Akshay Software Technologies Ltd, Mindtree Ltd and R.S. Software India Ltd. The learned Counsel for the assessee submitted that the learned DRP is erred in excluding Evoke Technologies Pvt Ltd by holding that the margin of the company was abnormally low as compared to other comparable companies and further expenses on consultancy charges is increased by 1,118% which indicated that the low margins during the relevant period was due to peculiar circumstances. However, the fact remains that the learned DRP has not spelt out as to how increase in consultancy charges resulted in peculiar circumstances or low margins. Therefore, he submitted that the reasons given by the DRP to exclude Evoke Technologies Pvt. Ltd is incorrect and thus prayed for inclusion of the said company on the ground that the FAR analysis of the above company is similar to the appellant company.

6. The learned Counsel for the assessee further referring to the annual reports of Akshay Software Technologies Ltd submitted that the company earned 99.5% of revenue from software services and it has satisfied all the filters applied by the learned TPO. Therefore, the DRP is erred in exclusion of the above company by Suo motto applying onsite revenue filters without giving any reasons as to how onsite development of software is a reason for exclusion of any company when other criteria are

satisfied or fulfilled. He further submitted that likewise, the learned DRP excluded Mindtree Ltd and R.S. Software India Ltd by applying on site revenue filter only on the ground that it has incurred huge expenditure at foreign branches which indicate substantial activities are undertaken onsite. But fact remains that M/s. Mindtree Ltd has incurred 65% of its expenses domestically and from the above, it is very clear that, substantial services are rendered offshore similar to Pegasystems Worldwide. Further, the learned DRP excluded Mindtree Ltd on the ground that there are extraordinary events of merger and investment in the year. The fact remains that when both the appellant and TPO accepted a particular company after verifying relevant facts, then the learned DRP cannot Suo motto exclude any company by applying fresh filters. Therefore, he submitted that these companies should be included in the list of final comparables.

7. The learned DR, on the other hand, supporting the orders of the DRP submitted that the DRP has given categorical reason as to how these companies are not comparable to the appellant company. Further, these companies are predominantly engaged in providing onsite development services and the TPO has failed to apply onsite revenue filters and therefore, the DRP has rightly applied on site revenue filter and excluded above companies and their order should be upheld.

8. We have heard both the parties, perused the material available on record and gone through the orders of the authorities

below. As regards the reason given by the learned DRP to exclude M/s. Evoke Technologies Ltd on the ground that the margin of the company was abnormally low and reasons for low margin is increase in consultancy charges, we find that the learned Counsel for the assessee has explained relevant financial statement and profit & loss account that the total revenue of the company has increased by 33% and if we compare the percentage of increase in turnover, the total expenditure is also proportionately increased. Further, there is an error in exclusion of the certain expenses including consultancy charges which was shown under the head administrative expenditure and the increase in administrative expenditure is proportionate to increase in turnover. From the above, it is very clear that there is no abnormal increase in consultancy charges as claimed by the learned DRP and further the said increase in expenditure cannot be treated as peculiar economic circumstances which leads to increase or decrease in margins of any company. Further, the FAR analysis of Evoke Technologies Ltd is similar to appellant company which is evident from revenue earned from software development services which is similar to services rendered by the appellant to its AEs. Therefore, we are of the considered view that the learned DRP is erred in excluding Evoke Technologies (P) Ltd by applying new filters which was not at all applied by the appellant and the TPO. This principle is supported by the decision of the ITAT Bangalore Benches in the case of Aspect Technology Center (India) Private Limited in IT(TP)A No.187/Bang/2016 dated 30th July, 2020. We

therefore, direct the TPO/Assessing Officer to include Evoke Technologies (P) Ltd in the list of comparables.

9. In so far as the exclusion of Akshay Software Technologies Ltd, Mindtree Ltd and R.S Software India (P) Ltd, the DRP Suo motto applied on site revenue filters and excluded the above companies on the ground that these companies are engaged in predominantly onsite development and is not comparable to appellant company. First of all, the DRP cannot Suo motto apply new filter which the appellant in their TP study and TPO has not applied the above filters. Further, the DRP is completely erred in observing that above companies are predominantly providing onsite development services only on the basis of expenditure incurred at foreign branches, but fact remains that even if go by the reasons given by the learned DRP that 65% of the expenses are incurred domestically , it can be concluded that substantial services are rendered offshore similar to Pega India. Further onsite development is part of software development activity and nature of services and functions performed remains the same irrespective of whether the service provider undertakes the development activity at a remote location at the offshore or at the clients place onsite except in a case where the services are rendered onsite the cost may be little higher side. Unless the TPO and DRP makes out a case that the appellant has incurred higher cost which is on account of providing onsite development services, in our considered view, onsite revenue filter cannot be applied. Further, when the appellant and the TPO are accepted a

particular company as comparable after analyzing their functions, then the DRP cannot Suo motto exclude the above company by applying new filter and this principle is supported by the decision of the ITAT Bangalore Bench in the case of Aspect Technology Center (India) Private Limited (Supra). Therefore, we set aside the findings of the learned DRP and direct the TPO/Assessing Officer to include Akshay Software Technologies Ltd, Mindtree Ltd and R.S. Software India Ltd in the list of comparables.

10. The next issue that came up for our consideration from Ground No.5 of assessee's appeal is exclusion of Persistent Systems Ltd, E-Zest Solutions Ltd and Sasken Communication Technologies Ltd.

11. The learned Counsel for the assessee, at the time of hearing submitted that the appellant do not wish to press for exclusion of E-Zest Solutions Ltd and therefore, we restrict our adjudication in respect of Ground No.5 relating to exclusion of Persistent Systems Ltd and Sasken Communication Technologies Ltd.

12. The learned Counsel for the assessee submitted that the learned DRP is erred in including Persistent Systems Ltd and Sasken Communication Technologies Ltd only on the ground that there was a general trend among the tax payers to object only the comparables which have high margin without any substantive argument that while examining the comparability of any

company, a fair approach is necessarily to be adopted depending upon the FAR analysis of the company. But the fact remains that M/s. Persistent Systems Ltd is functionally not comparable to the appellant company because it derived revenue from sale of software services and sale of software products, whereas the appellant company is providing software development solution to its parent company on cost plus mark up. Similarly, Sasken Communication Technologies Ltd is also a product company derives revenue from sale of products and product design services. Although the above two companies are not comparable to the appellant company, the learned DRP without any reason included the above company. Therefore, he submitted that the above two companies should be excluded from the final set of comparables.

13. The learned DR, on the other hand, supporting the orders of the DRP submitted that Persistent Systems Ltd is into product development in India like Pega India. The company had long term contract with 297 customers like appellant. Sasken Communication Technologies Ltd is also functionally comparable to the appellant company. Therefore, the DRP has rightly included the above two companies and their order should be upheld.

14. We have heard both the parties, perused the material available on record and gone through the orders of the authorities below. We have also carefully considered the relevant annual reports submitted by the appellant to ascertain the nature of

services rendered by the appellant company and nature of services rendered by Persistent Systems Ltd. On perusal of the details filed by the assessee, we find that Persistent Systems Ltd derives revenue from sale of software products and sale of software services. There is no break up of income/expenses from two segments. The above company is predominantly a product company. Therefore, in our considered view Persistent Systems Ltd cannot be compared with appellant company which is engaged in providing software development services to its AE on cost plus mark up. Further, Persistent Systems Ltd has been held to be not comparable to a software development provider by the ITAT Hyderabad Bench in the case of Conexant Systems (P) Ltd in ITA No.464/Hyd/2016. Therefore, we are of the considered view that the DRP is erred in including Persistent Systems Ltd and thus, we direct the learned TPO/Assessing Officer to exclude Persistent Systems Ltd from the list of comparables.

15. In so far as Sasken Communication Technologies Ltd, from the details available on record, we find that it derives revenue from software development services and product design services. Allocation of actual expenditure between each segment is also not available. It also spent substantial amount for R&D purposes. The company holds inventory. From the above, it is undisputedly clear that it is predominantly a product company which cannot be compared with the appellant company which is engaged in providing software development services to its AE on cost plus mark up. Further, this company has been held to be not

comparable to a software development service provider in the case of Conexant Systems (P) Ltd. Therefore, we direct the learned TPO/Assessing Officer to exclude Sasken Communication Technologies Ltd from the list of comparables.

16. The assessee has raised various grounds relating to other issues including computation of net margin, incorrect selection of filters, selection of multiple year data, negative working capital adjustment and adjustment for risk differences etc., Since the learned Counsel for the assessee restricted his submission with regard to comparables discussed by us in preceding paragraphs, in our considered view, the other grounds taken by the assessee in their grounds of appeal are treated as not pressed and thus remaining grounds are dismissed as not pressed.

17. In the result, appeal filed by the assessee is partly allowed.

Order pronounced in the Open Court on 7th August, 2024.

Sd/- (LALIET KUMAR) JUDICIAL MEMBER	Sd/- (MANJUNATHA, G.) ACCOUNTANT MEMBER
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Hyderabad, dated August, 2024
Vinodan/sps

Copy to:

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3	Pr. CIT -5, Hyderabad
4	Director (IT & TP) Hyderabad
5	DR, ITAT Hyderabad Benches
6	Guard File

By Order