

IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCH ' A '

BEFORE SHRI VIJAY PAL RAO, JUDICIAL MEMBER AND
SHRI INTURI RAMA RAO, ACCOUNTANT MEMBER

I.T. (T.P.) A. No.33/Bang/2013
(Assessment Year : 2008-09)

M/s. Trilogy E-Business Software India Pvt. Ltd.,
No.1/2, Lalitha Nilaya, 4th Cross, RMV 2nd Stage,
Bhopsandra, Bangalore-560 094.

.... Appellant.

Vs.

Dy. Commissioner of Income Tax,
Circle 12(4), Bangalore-560 001.

..... Respondent.

I.T. (T.P.) A. No.115/Bang/2013
(Assessment Year : 2008-09)
(By Revenue)

Assessee By : Shri Padam Chand Khincha, C.A.
Respondent By : Dr.P.K. Srihari, Addl. CIT (D.R.)

Date of Hearing : 18.5.2016.
Date of Pronouncement : 08.06.2016.

O R D E R

Per Shri Vijay Pal Rao, J.M. :

These Cross Appeals are directed against the order dated 6.11.2012
of Commissioner of Income Tax (Appeals)-IV, Bangalore for the
Assessment Year 2008-09.

2. The assessee-company was incorporated in June 2000 and is wholly owned subsidiary of Versata International Inc., (previously known as Trilogy Inc.). During the financial year relevant to the assessment year under consideration, the assessee has provided software development services as well as call centre services to its Associated Enterprises (in short 'AEs'). The assessee is compensated on cost +10% basis by its AEs for the services provided by the assessee. The financial results of the assessee for the assessment year under consideration are recorded by the Transfer Pricing Officer (in short 'TPO') in paragraph 2.1 as under :

	ITES Rs.	Software Rs.	Total Rs.
Total operating income	55,50,639	43,78,31,848	44,33,82,487
Total operating cost	49,12,070	39,80,28,956	40,29,41,023
Operating Profit	6,38,569	3,98,02,895	4,04,41,464
PBIT / Cost	13%	10%	10.04%
PBIT / Sales	11.50%	9.09%	9.12%

3. The assessee has reported international transactions in **92 CE report** which are reproduced by the TPO in paragraph 2.2 as under :

Sl.No.	Type of Transaction	Amount Received Rs.	Amount Paid Rs.
1	SWD Services	43,78,31,849	
2	ITES	55,50,639	
3	Reimbursement of expenses		1,60,05,330

Thus the assessee operates in two segments i.e. software development services and call centre services to its AEs. The services in call centre services are accepted by the TPO at arm's length. The TPO has not accepted the international transactions in software development services segment at arm's length and accordingly proceeded to determine the Arm's Length Price ('ALP'). To bench mark its international transactions regarding software development services, the assessee has selected 21 comparable companies as under :

Sl.No.	Name of the Company	Weighted Avg. Operating Margin on cost. %
1.	Akshay Software Technologies Ltd.	6.60
2	Aztecsoft Ltd.	18.16
3	Goldstone Technologies Ltd.	11.50
4	Helios & Matheson Information Technology Ltd.	38.40
5	Indium Software (India) Ltd.	11.09
6	KPIT Cummins Infosystems Ltd.	13.20
7	Lanco Global Systems Ltd.	13.28
8	Larsen & Toubro Infotech Ltd.	11.35
9	Maars Software Intl. Ltd.	15.58
10	Melstar Information Technolgoeis Ltd.	3.46
11	Mindtree Ltd.	16.98
12	Persistent Systems Pvt. Ltd.	24.34
13	Quintegra Solutions Ltd.	15.18
14	R S Software (India) Ltd.	14.11
15	SIP Technologies and Exports Ltd.	18.37
16	Sasken CommunicationTechnologies Ltd.	17.88
17	TVS Infotech Ltd.	- 21.27

18	VJIL Consulting Ltd.	5.85
19	VMF Softech Ltd.	4.32
20	Visualsoft Technologies Ltd.	16.76
21	Zylog Systems Ltd.	16.87
	Arithmetic Mean	12.95

4. The TPO rejected 15 companies selected by the assessee and accepted 6 companies from the set of comparables selected by the assessee. The companies accepted by the TPO from the list of comparables of the assessee are Sl.Nos.7, 11,12,13,14 & 16 in the above Table. The TPO has carried out a fresh search and added 14 more comparable companies in the final set of comparables as under :

Sl. No.	Name of the Company	Operating Margin on Cost %	W. Cap Adj. Margin %
1	Avani Cimcon Technologies Ltd.	25.62	29.60
2	Bodhtree Ltd.	18.72	20.31
3	Celestial Labs Ltd.	87.94	81.52
4	E-ZestSolutions Ltd.	29.81	30.59
5	Flextronics Software Systems Ltd.	7.86	7.12
6	iGAtE Global Solutions Ltd.	13.99	13.14
7	Infosys Technologies Ltd.	40.37	39.06
8	KALS Information Systems Ltd. (Seg.)	31.29	29.60
9	LGS Global Ltd. (Lanco Global Solutions Ltd.)	27.52	27.28
10	Lucid Software Ltd.	16.50	18.65
11	Mindtree Consulting (Seg.)	16.41	16.26
12	Persistent Systems LTd.	20.31	21.43

13	Quintegra Solutions Ltd.	21.74	19.41
14	R S Software (India) Ltd.	7.41	9.71
15	R Systems International Ltd.	15.30	14.31
16	Sasken Communication Technologies Ltd. (Seg.)	7.58	7.97
17	Soft SolIndia Ltd.	17.89	16.33
18	Tata Elxsi Ltd. (Seg.)	18.97	19.58
19	Thirdware Solutions Ltd	19.35	17.75
20	Wipro Ltd (Seg.)	28.45	30.40
	Arithmetic Mean	23.65%	23.50%

The TPO has determined the arithmetic mean at 26.35% and after granting working capital adjustment the adjusted mean margin was arrived at 23.5%. Accordingly, the TPO proposed an adjustment u/s. 92CA of Rs.8,34,25,710. The assessee challenged the action of the TPO / AO by filing the appeal before the CIT (Appeals). The CIT (Appeals) rejected 9 comparable companies from the set of comparables selected by the TPO. The CIT (Appeals) has applied turnover filter and therefore most of the companies were excluded by the CIT (Appeals) on this ground. The assessee also pleaded for inclusion of two more companies in the set of comparables. However, the CIT(A) accepted one of the companies namely **VGL SoftTech Limited** which was excluded by the TPO on the ground of non-availability of data. Thus after exclusion of 9 comparables

and inclusion of one additional comparable, the CIT (Appeals) directed the TPO/A.O to retain 12 comparable companies as under :

Sl.No.	Name of the Company	Operating Margin on Cost as per OGE to CIT(A) order. %
1	Avani Cincom Technologies Ltd.	25.62
2	Bodhtree Ltd.	18.72
3	E-Zest Solutions Ltd.	29.81
4	Kals InformationSystems Ltd.	31.29
5	LGS Global Ltd. (Lanco Global Solutions Ltd.)	27.52
6	Lucid Software Ltd.	16.50
7	Quintegra Solutions Ltd.	21.74
8	R Systems International Ltd. (Seg.)	15.30
9	RS Software (India) Ltd.	7.41
10	Soft Sol India Ltd.	17.89
11	Thirdware Solutions Ltd.	19.35
12	VGL Softech Ltd.	14.19
	Average	20.45
	Less : Working Capital Adjustment	0.15
	Arm's Length Margin	20.30

5. The assessee is aggrieved by the order of the CIT (Appeals) so far as it has retained 11 comparable companies from the set of TPO whereas the revenue is aggrieved by the impugned order of the CIT (Appeals) whereby CIT (Appeals) has excluded 9 comparable companies selected by the TPO by applying turnover and some other comparable companies on functional dis-similarity.

6. First we take up the assessee's appeal wherein the assessee has raised the following grounds :

1. *" The Order of the learned Commissioner of Income Tax (Appeals) – IV to the extent prejudicial to the appellant is bad in law.*
2. *The learned Assessing Officer has erred in making a reference to Transfer Pricing Officer for determining arm's length price without demonstrating as to why it was necessary and expedient to do so. The learned Commissioner of Income Tax (Appeals) - IV has erred in confirming the action of the Assessing officer.*
3. *The learned Assessing Officer, learned Transfer Pricing Officer and Commissioner of Income Tax (Appeals) - IV have erred in --*
 - a. *passing the order without demonstrating that appellant had motive of tax evasion.*
 - b. *not appreciating that the charging or computation provision relating to income under the head "Profits & Gains of Business or Profession" do not refer to or include the amounts computed under Chapter X and therefore addition made under Chapter X is bad in law.*
 - c. *adopting a flawed process for issuing notices u/s 133(6) and relying on the same without providing complete information or an opportunity to cross examine the companies concerned.*

GROUND ON COMPARABLES AND REJECTION OF TP ANALYSIS OF THE APPELLANT

4. *The learned Assessing Officer, learned Transfer Pricing Officer and Commissioner of Income Tax (Appeals) - IV have erred in*
 - a. *computing the arm's length price based on the data for the Financial Year 2007-08 of the comparables, which was not available when the appellant undertook transfer pricing documentation and reporting obligations;*
 - b. *rejecting the comparables selected by the appellant on unjustifiable grounds;*
 - c. *rejecting the additional comparables proposed by the appellant on unjustifiable grounds; and*
 - d. *rejecting the transfer pricing analysis undertaken by the appellant on unjustifiable grounds.*

GROUND RELATING TO TP ANALYSIS OF THE TPO:

5. *The learned Assessing Officer, learned Transfer Pricing Officer and Commissioner of Income Tax (Appeals) - IV have erred in:*

- a. *Performing fresh transfer pricing analysis and adopting inappropriate filters in doing fresh transfer pricing analysis.*
- b. *adopting companies as comparables even though they are not comparable to the appellant.*
- c. *Not appreciating that the law does not compel adopting many (or any minimum) companies as comparables and that the appellant could justify the price paid/charged on the basis of any one comparable only.*
- d. *not making proper adjustment for enterprise level and transactional level differences between the appellant and the comparable companies, including the differences in functions performed, assets employed and risks undertaken.*
6. *The learned Assessing Officer, learned Transfer Pricing Officer and Commissioner of Income Tax (Appeals) - IV have erred in:*
 - a. *Not excluding Fringe Benefit Tax (FBT) from the operating cost while computing arm's length price. Even otherwise, FBT has been excluded from operating cost for comparable companies and on parity of reason, the same should also be excluded while computing operating cost of the appellant.*
 - b. *Treating foreign exchange gain or loss as operating in nature while computing arm's length price. In the alternative, in case, foreign exchange gain or loss is treated as non-operating in nature, then the TPO/AO be directed to exclude foreign exchange loss incurred by the appellant from the operating cost while computing arm's length price.*
7. *The learned Commissioner of Income Tax (Appeals) - IV has erred in confirming companies selected by the TPO as comparables ignoring the submissions of the appellant.*
8. *The learned Assessing Officer, learned Transfer Pricing Officer and Commissioner of Income Tax (Appeals) - IV have erred in not giving*
9. *The learned Assessing Officer has erred in disallowing a sum of Rs. 2,99,07,451/- being research and development expenses under section 37 of the Act stating that the said expenses confer an enduring benefit and is not revenue in nature and stating that R&D Expenses was incurred on behalf of parent company without appreciating that same was incurred for domestic operations. The learned Commissioner of Income Tax (Appeals) - IV has erred in confirming the action of the Assessing officer.*
10. *The learned assessing officer has erred in levying interest under section 234B and 234D of the Income tax Act, 1961. On facts and in the circumstances of the case and law applicable, interest under section 234B and 234D is not leviable. The appellant denies its liability to pay interest under section 234B and 234D.*

PRAYER

11. *On an overall consideration of the facts of the case, and the law applicable:*

The ALP as determined by the Transfer Pricing Officer, as adopted by the Assessing Officer and as confirmed by the CIT(A), to the extent prejudicial to the appellant, being not correct is to be quashed and the figures as determined and returned by the appellant being correct are to be accepted.

a. *The disallowance of R&D expenses be deleted.*

12. *Interest under section 234B and 234D be deleted.*

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 appeals according to law.

The appellant prays accordingly.”

7. **The assessee has also raised additional grounds by filing a petition**

dt.16.6.2016. The additional grounds raised by the assessee are as under :

1. *“ The above referred appeal is in respect of the order passed by the learned Commissioner of Income Tax (Appeals). The Assessing Officer had passed Assessment Order under section 143(3) on 24.01.2012 against which the Appellant had filed an appeal before the CIT (Appeals). The CIT (Appeals) heard the case and passed order under section 250(6) on 06.11.2012.*

2. *In the order passed under section 143(3), transfer pricing additions were made for transactions with associated enterprises along with certain other additions to the total income of the Appellant.*

3. *The additional grounds of appeal (enclosed herewith) relate to rejection of Quintegra Solutions Ltd, Soft Sol India Ltd, E-Zest Solutions Ltd and Persistent Systems Pvt Ltd as comparables for the software development services rendered by the Appellant. In the case of Quintegra Solutions Ltd and Persistent Systems Pvt, both the Appellant and the TPO had selected it as a comparable. In respect of other comparables, the TPO had selected these companies as comparables in the order passed u/s 92CA. The additional ground also relates to inclusion of Indium software as a comparable which is rejected as a comparable by CIT(A) on the ground of losses. With respect to rejection/inclusion of these comparables, the ground pertains to question of facts. All the necessary facts for adjudicating this ground are already on record. The Appellant humbly prays that the additional ground be admitted and adjudicated along with the other grounds of appeal in the course of hearing of the appeal.*

The Appellant prays accordingly.”

8. By way of additional ground, the assessee is seeking exclusion of 3 companies namely Quintegra Solutions Ltd., e-Zest Solutions Ltd. And Persistent Systems Ltd. The assessee is also raised an issue of exclusion of certain comparable companies by applying the RPT filter at 15% as it has been consistently accepted by this Tribunal. Apart from that the assessee has also seeking inclusion of one company i.e. **Indium Software India Pvt. Ltd.** as a comparable.

9. We have heard the learned Authorised Representative as well as learned Departmental Representative and considered the relevant material on record on the issue of admission of additional grounds raised by the assessee.

10. As regards the additional grounds for applying RPT filter at 15% instead of 25% applied by the TPO, we find that the assessee did not raise any objection against 25% RPT filter applied by the TPO either before the TPO or before the CIT (Appeals). Therefore, this issue does not emanate from the impugned orders of the authorities below. Even otherwise the filter is applied for selecting the comparables and applicable to all the comparable companies either selected by the assessee or by the TPO then we do not find any substance in the

additional grounds raised by the assessee so far as applying the RPT filter at 15% instead of 25% applied by the authorities below and accepted by the assessee. As regards the exclusion of 3 companies by raising the additional grounds we note that the comparability of those 3 companies have been examined by this Tribunal in series of cases. The Tribunal has taken a view in case of ITO Vs. M/s. Net Devices India Pvt. Ltd. Vide order dt.25.5.2016 in I.T.(T.P)A.No.1099/Bang/2011 & C.O. No. 19/Bang/2012 in para 15.3 as under :

" 15.3 We have heard the rival submissions as well as considered the relevant material on record on the admissibility of the additional grounds raised by the assessee. We find that there are some decisions of this Tribunal wherein the comparability of these two companies have been considered and decided by this Tribunal. Therefore, once the assessee has brought on record some decisions of the Tribunal wherein these two companies were held to be not good comparables then the facts and circumstances and in the interest of justice, we admit the additional grounds raised by the assessee. Accordingly, we will deal with the comparability of these two companies on merits."

10.1 Accordingly, we concur with the earlier view of the Tribunal and admit the additional grounds raised by the assessee in respect of functional dis-similarity of certain companies.

10.2 The assessee is seeking exclusion of 12 companies from the final set of TPO. At the outset the learned Authorised Representative of the

assessee has submitted that the revenue has objected to the turnover filter applied by the learned CIT (Appeals) for exclusion of certain comparables. However, the assessee would not object against non-application of turnover filter as sought by the revenue in its appeal. The learned Authorised Representative has submitted that those comparables selected by the TPO are otherwise functionally dis-similar to the assessee. He has pointed out that an identical set of 21 comparable companies selected by the TPO has been considered by the co-ordinate bench of this Tribunal in the case of Kodiak Network (India) Pvt. Ltd. Vs. DCIT in IT(TP)A No.1540/Bang/2012 vide order dt.5.5.2015 for the same asst. year 2008-09.

10.3 Thus the learned Authorised Representative has submitted that an identical set of comparable companies selected by the TPO has been examined by the co-ordinate bench in the case of Kodiak Network (India) Pvt. Ltd. (supra). The Tribunal has finally concluded that out of 21 comparable companies selected by the TPO, 12 companies cannot be considered good comparables to the software development services provider company.

10.4 On the other hand, the learned Departmental Representative has submitted that the decision of the co-ordinate bench of this Tribunal in the case of Kodiak Network (India) Pvt. Ltd. (supra) cannot be applied directly in the case of the assessee without verifying the similarity of the business profile of the assessee and M/s. Kodiak Network (India) Pvt. Ltd. (supra). The learned Departmental Representative has submitted that the assessee's business activity in this segment is providing/provision of software development services which may be the inclusive of software development product and therefore the Tribunal in the case of Kodiak Network (India) Pvt. Ltd. (supra) has directed the exclusion of certain comparable companies on the ground of having software product. The said finding cannot be applied in the case of the assessee without verifying the fact that the assessee is not engaged in the software product.

10.5 We have considered the rival submissions as well as relevant material on record. It is pertinent to note that the TPO in the case of Kodiak Network (India) Pvt. Ltd. (supra) has selected an identical set of 21 companies as selected in the case of the assessee. Therefore, it is clear that while selecting the comparable companies, the TPO has

considered the assessee as a software development services provider as in the case of Kodiak Network (India) Pvt. Ltd. (supra). Further, the TPO has recorded the functional profile of the assessee in the impugned order which has been reproduced in the foregoing paragraphs of this order and therefore we do not find any substance in the objections raised by the learned Departmental Representative that the business profile of the assessee as far as the software development services segment may not be similar to that of Kodiak Network (India) Pvt. Ltd. (supra). The Tribunal in the case of Kodiak Network (India) Pvt. Ltd. (supra) has dealt with the issue of functional comparability of identical set of comparables in paras 21 to 25 as under :

" 21. We have considered the rival submissions and relevant material available on record. As we have narrated the facts in the foregoing paras that the TPO has determined the ALP by taking into consideration the set of 20 comparables. The assessee has raised objection regarding 13 comparables out of 20 selected by the TPO. The companies against which the assessee raised objections are as under:

S.No.	Name of the Company
1	AvaniCimcon Technologies Ltd
2	Bodhtree Ltd
3	Celestial Biolabs Ltd
4	E-Zest Solutions Ltd
5	Infosys Technologies Ltd
6	KALS Information Systems Ltd (Seg.)

7	Lucid Software Ltd
8	Persistent Systems Ltd
9	Quintegra Solutions Ltd
10	Softsole India Ltd
11	Tata Elxsi Ltd (Seg.)
12	Thirdware Solutions Ltd (Seg
13	Wipro Ltd (Seg.)

22. We note that the comparability of these 13 companies have been examined by this Tribunal in series of decision as referred by the Id. AR. In the case of M/s 3DPLM Software Solutions Ltd (supra), the co-ordinate Bench of this Tribunal has considered the comparability of these companies in paras 7 to 19.3 of the order which have been reproduced below:

“7.0 Avani Cincom Technologies Ltd.

7.1 This company was selected by the TPO as a comparable. The assessee objects to the inclusion of this company as a comparable on the ground that this company is not functionally comparable to the assessee as it is into software products whereas the assessee offers software development services to its AEs. The TPO had rejected the objections of the assessee on the ground that this comparable company has categorized itself as a pure software developer, just like the assessee, and hence selected this company as a comparable. For this purpose, the TPO had relied on information submitted by this company in response to enquiries carried out under section 133(6) of the Act for collecting information about the company directly.

7.2 Before us, the learned Authorised Representative reiterated the assessee's objections for the inclusion of this company from the list of comparable companies on the ground that this company is not functionally comparable to the assessee as it is into software products. It is also submitted that the segmental details of this company are not available and the Annual Report available in the public domain is not complete. It was further contended that the information obtained by the TPO under section 133(6) of the Act, on the basis of which the TPO included this company in the final list of comparable companies, has not been shared with the assessee. In support of this contention, the learned Authorised Representative placed reliance on the following judicial decisions:

- i) Trilogy E-Business Software India Pvt. Ltd. V DCIT (ITA No.1054/Bang/2011)

- ii) Telecordia Technologies India Pvt Ltd V ACIT (ITA No.7821/Mum/2011)

It was also submitted that this company has been held to be functionally not comparable to the assessee by a co-ordinate bench of this Tribunal in the assessee's own case for Assessment Year 2007-08 in ITA No.845/Bang/2011 dt.22.2.2013.

7.3 The learned Authorised Representative further submitted that the facts pertaining to this company has not changed from the earlier year (i.e. Assessment Year 2007-08) to the period under consideration (i.e. Assessment Year 2008-09). In support of this contention, it was submitted that :-

(i) The extract from the Website of the company clearly indicates that it is primarily engaged in development of software products. The extract mentions that this company offers customised solutions and services in different areas;

(ii) The Website of this company evidences that this company develops and sells customizable software solutions like "DX Change, CARMA, etc.

7.4 The learned Authorised Representative submitted that a co-ordinate bench of the Tribunal in its order in Curram Software International Pvt. Ltd., in its order in ITA No.1280/Bang/2012 dt.31.7.2013 has remanded the matter back to the file of the Assessing Officer / TPO to examine the comparability of this company afresh, by making the following observations at paras 9.5.2 and 9.5.3 thereof :-

" 9.5.2 As regards the submission of the learned Authorised Representative, we are unable to agree that this company has to be deleted from the list of comparables only because it has been deleted from the set of comparables in the case of Trilogy E-Business Software India Pvt. Ltd. (supra). No doubt this company has been deleted as a comparable in the case of Trilogy E-Business Software India Pvt. Ltd. (supra) and this can be a good guidance to decide on

the comparability in the case on hand also. This alone, however, will not suffice for the following reasons :-

(i) The assessee needs to demonstrate that the FAR analysis and other relevant facts of the Triology case are equally applicable to the facts of the assessee's case also. Unless the facts and the FAR analysis of Triology case is comparable to that of the assessee in the case on hand, comparison between the two is not tenable. (ii) After demonstrating the similarity and the comparability between the assessee and the Triology case, the assessee also needs to demonstrate that the facts applicable to the Assessment Year 2007-08, the year for which the decision in case of Triology E-Business Software India Pvt. Ltd. (supra) was rendered are also applicable to the year under consideration i.e. Assessment Year 2008-09.

9.5.3 It is a well settled principle that the assessee is required to perform FAR analysis for each year and it is quite possible that the FAR analysis can be different for each of the years. That being so, the principle applicable to one particular year cannot be extrapolated automatically and made applicable to subsequent years. To do that, it is necessary to first establish that the facts and attendant factors have remained the same so that the factors of comparability are the same. Viewed in that context, the assessee has not discharged the onus upon it to establish that the decision rendered in the case of Triology E-Business Software India Pvt. Ltd. (supra) can be applied to the facts of the case and that too of an earlier year i.e. Assessment Year 2007-08. The assessee, in our view, has not demonstrated that the facts of Triology E-Business Software India Pvt. Ltd. (supra) are identical to the facts of the case on hand and that the profile of the assessee for the year under consideration is similar to that of the earlier Assessment Year 2007-08. In view of facts as discussed above, we deem it fit to remand the matter back to the file of the Assessing Officer / TPO to examine the comparability of this company afresh by considering the above observations. The TPO is directed to make available to the assessee information obtained under section 133(6) of the Act and to afford the assessee adequate opportunity of being heard and to make its submissions in the matter, which shall be duly considered before passing orders thereon. It is ordered accordingly."

The learned Authorised Representative submits that this company was selected as a comparable by the TPO not by any FAR analysis or as per the search process conducted by the TPO, but only as an additional comparable for the reason that it was selected as a comparable in the earlier year i.e. Assessment Year 2007-08 on the basis of information

obtained under section 133(6) of the Act. In this regard, the learned Authorised Representative took us through the relevant portions of the TP order under section 92CA of the Act and the show cause notices for both the earlier year i.e. Assessment Year 2007-08 and for this year and contended that the selection of this company as a comparable violates the principle enunciated in Curram Software International Pvt. Ltd. (supra) that a company can be selected as a comparable only on the basis of FAR analysis conducted for that year and therefore pleaded for its exclusion. The learned Authorised Representative also submitted that he has brought on record sufficient evidence to show that the functional profile of this company remains unchanged from the earlier year and hence the findings rendered by the co-ordinate benches of the Tribunal in the assessee's own case for Assessment Year 2007-08 (supra) and in other cases like Trilogy E-Business Software India Pvt. Ltd. (supra) are applicable to the year under consideration as well.

7.5 Per contra, the learned Departmental Representative supported the order of the TPO / DRP for inclusion of this company Avani Cincom Technologies Ltd. in the final set of comparables.

7.6.1 We have heard both parties and perused and carefully considered the material on record. It is seen from the record that the TPO has included this company in the final set of comparables only on the basis of information obtained under section 133(6) of the Act. In these circumstances, it was the duty of the TPO to have necessarily furnished the information so gathered to the assessee and taken its submissions thereon into consideration before deciding to include this company in its final list of comparables. Nonfurnishing the information obtained under section 133(6) of the Act to the assessee has vitiated the selection of this company as a comparable.

7.6.2 We also find substantial merit in the contention of the learned Authorised Representative that this company has been selected by the TPO as an additional comparable only on the ground that this company was selected in the earlier year. Even in the earlier year, it is seen that this company was not selected IT(TP)A 1380/Bang/2012 Page 7 of 34 on the basis on any search process carried out by the TPO but only on the basis of information collected under section 133(6) of the Act. Apart from placing reliance on the judicial decision cited above, including the assessee's own case for Assessment Year 2007-08, the assessee has brought on record evidence that this company is functionally dis-similar and different from the assessee and hence is not comparable. Therefore the finding excluding it from the list of comparables rendered in the immediately preceding year is applicable in this year also. Since the functional profile and other parameters by this company

have not undergone any change during the year under consideration which fact has been demonstrated by the assessee, following the decisions of the co-ordinate benches of this Tribunal in the assessee's own case for Assessment Year 2007-08 in ITA No.845/Bang/2011 dt.22.2.2013, and in the case of Triology E-Business Software India Pvt. Ltd. (ITA No.1054/Bang/2011), we direct the A.O./TPO to omit this company from the list of comparables.

8.0 Bodhtree Consulting Ltd.

8.1 This company has been selected as a comparable company to the assessee by the TPO; the inclusion of which was not objected to by the assessee before both the TPO and the DRP. The assessee has not objected to the inclusion of this company in the list of comparables, as can be seen from the grounds of appeal raised in Form 36B before this Tribunal. 8.1 However in the course of proceedings before us, the learned Authorised Representative objected to the inclusion of this company as a comparable for the following reasons :

(i) This company has reported abnormally fluctuating margins in the period from 2005 to 2011, which indicate abnormal business factors and abnormal profit margins and hence should not be considered as comparable to the assessee.

(ii) The abnormally fluctuating margins indicate that this company bears higher risk in contrast to the assessee who has earned consistent margins over the years, indicating difference in the risk profile between this company and the assessee.

(iii) This company has registered exponential growth of 67% in terms of revenue and 41% in terms of profits over the immediately preceding year which can be attributed to the development of a software application, MIDAS (Multi Industry Data Anomaly) which was made available for customers as SaaS (Software as a Service).

8.3 Per contra, the learned Departmental Representative opposed the exclusion of this company from the list of comparable companies. The learned Departmental Representative contended that since the assessee had accepted the TPO's proposal for inclusion of this company in the set of comparables and had not objected to its inclusion even before the DRP, the objections raised by the assessee in this regard, at this stage, ought to be rejected.

8.4.1 We have heard both parties and perused and carefully considered the material on record. Admittedly, there is no disputing the fact that the assessee had never objected to the inclusion of this company in the set of comparables in earlier proceedings before the TPO and the DRP. It is also seen that even in the grounds of appeal raised before us, the assessee has not raised any grounds challenging the inclusion of this company in the list of comparables. In fact in the assessee's own case for Assessment Year 2007-08, this company was selected as a comparable by the assessee itself. We, therefore, find no merit in the contentions raised by the learned Authorised Representative of the assessee in respect of this company at this stage of proceedings.

8.4.2 It is also seen from the submissions made before us that the assessee has only pointed out fluctuating margins in the results of this company over the years. This, in itself, cannot be reason enough to establish differences in functional profile or any clinching factual reason warranting the exclusion of this company from the list of comparables. In this view of the matter, the contentions of the assessee are rejected and this company is held to be comparable to the assessee and its inclusion in the list of comparable companies is upheld.

9. Celestial Biolabs Ltd.

9.1 This comparable was selected by the TPO for inclusion in the final list of comparables. Before the TPO, the assessee had objected to the inclusion of this company in the list of comparables for the reasons that it is functionally different from the assessee and that it fails the employee cost filter. The TPO, however, brushed aside the objections raised by the assessee by stating that the objections of functional dissimilarity has been dealt with in detail in the T.P. order for Assessment Year 2007-08. As regards the objection raised in respect of the employee cost filter issue, the TPO rejected the objections by observing that the employee cost filter is only a trigger to know the functionality of the company.

9.2 Before us, the learned Authorised Representative contended that this company is not functionally comparable, as the company is into bio-informatics software product /services and the segmental break up is not provided. It was submitted that :-

(i) This company is engaged in the development of products in the field of bio-technology, pharmaceuticals, etc. and therefore is not functionally comparable to the assessee;

(ii) This company has been held to be functionally incomparable to software service providers by the decision of the co-ordinate bench of this Tribunal in the assessee's own case for Assessment Year 2007-08 (supra);

(iii) The co-ordinate bench of this Tribunal in its order in the case of Triology EBusiness Software India Pvt. Ltd. (supra) at para 43 thereof had observed about this company that –

“ As explained earlier, it is a diversified company and therefore cannot be considered as comparable functionally with the assessee. There has been no attempt to identify, eliminate and make adjustment of the profit margins so that the difference in functional comparability can be eliminated. By not resorting to such a process of making adjustments, the TPO has rendered this company as not qualifying for comparability. We therefore accept the plea of the assessee in this regard.”

(iv) The rejection / exclusion of this company as a comparable for Assessment Year 2007-08 for software service providers has been upheld by the co-ordinate benches of this Tribunal in the cases of LG Soft India Pvt. Ltd. in ITA No.112/Bang/2011, CSR India Pvt. Ltd. in IT(TP)A No.1119/Bang/2011 and by the ITAT, Delhi Bench in the case of Transwitch India Pvt. Ltd. in ITA No.6083/Del/2010.

(v) The facts pertaining to this company has not changed from Assessment Year 2007- 08 to Assessment Year 2008-09 and therefore this company cannot be considered for the purpose of comparability in the instant case and hence ought to be rejected. In support of this contention, the assessee has also referred to and quoted from various parts of the Annual Report of the company.

9.3 Per contra, the learned Departmental Representative supported the inclusion of this company in the list of comparable companies. The learned Departmental Representative submitted that the decisions cited and relied on by the assessee are for Assessment Year 2007-08 and therefore there cannot be an assumption that it would continue to be applicable for the period under consideration i.e. Assessment Year 2008-09.

9.4.1 We have heard both the parties and perused and carefully considered the material on record. While it is true that the decisions cited and relied on by the assessee were with respect to the immediately previous assessment year, and there cannot be an assumption that it would continue to be applicable for this year as well, the same parity of reasoning is applicable to the TPO as well who seems to have selected this company as a comparable

based on the reasoning given in the TPO's order for the earlier year. It is evidently clear from this, that the TPO has not carried out any independent FAR analysis for this company for this year viz. Assessment Year 2008-09. To that extent, in our considered view, the selection process adopted by the TPO for inclusion of this company in the list of comparables is defective and suffers from serious infirmity.

9.4.2 Apart from relying on the afore cited judicial decisions in the matter (supra), the assessee has brought on record IT(TP)A 1380/Bang/2012 Page 8 of 34 substantial factual evidence to establish that this company is functionally dis-similar and different from the assessee in the case on hand and is therefore not comparable and also that the findings rendered in the cited decisions for the earlier years i.e. Assessment Year 2007-08 is applicable for this year also. We agree with the submissions of the assessee that this company is functionally different from the assessee. It has also been so held by co-ordinate benches of this Tribunal in the assessee's own case for Assessment Year 2007-08 (supra) as well as in the case of Trilogy E-Business Software India Pvt. Ltd. (supra). In view of the fact that the functional profile of and other parameters of this company have not changed in this year under consideration, which fact has also been demonstrated by the assessee, following the decision of the co-ordinate benches of the Tribunal in the assessee's own case for Assessment Year 2007-08 in ITA No.845/Bang/2011 and Trilogy E-Business Software India Pvt. Ltd. in ITA No.1054/Bang/2011, we hold that this company ought to be omitted from the list of comparables. The A.O./TPO are accordingly directed.

10. KALS Information Systems Ltd.

10.1 This is a comparable selected by the TPO. Before the TPO, the assessee had objected to the inclusion of this company in the set of comparables on grounds of functional differences and that the segmental details have not been provided in the Annual Report of the company with respect to software services revenue and software products revenue. The TPO, however, rejected the objections of the assessee observing that the software products and training constitutes only 4.24% of total revenues and the revenue from software development services constitutes more than 75% of the total operating revenues for the F.Y. 2007-08 and qualifies as a comparable by the service income filter.

10.2 Before us, the learned Authorised Representative contended that this company is not functionally comparable to the assessee and ought to be rejected /excluded from the list of comparables for the following reasons:-

(i) This company is functionally different from the software activity of the assessee as it is into software products.

(ii) This company has been held to be functionally not comparable to software service providers for Assessment Year 2007-08 by the co-ordinate bench of this Tribunal in the assessee's own case. This company has been held to be different from a software development company in the decision of the Tribunal in the case of Bindview India Pvt. Ltd. V DCIT in ITA No.1386/PN/2010.

(iii) The rejection of this company as a comparable has been upheld by co-ordinate benches of the Tribunal in the case of –

- (a) Triology E-Business Software India Pvt. Ltd. (ITA No.1054/Bang/2011).
- (b) LG Soft India Pvt. Ltd. IT(TP)A No.112/Bang/2011)
- (c) CSR India Pvt. Ltd. IT(TP)A No.1119/Bang/2011) and
- (d) Transwitch India Pvt. Ltd. ITA No.6083/Del/2010)

(iv) The facts pertaining to this company has not changed from Assessment Year 2007- 08 to Assessment Year 2008-09 and therefore this company cannot be considered for the purpose of comparability in the case on hand and hence ought to be excluded from the list of comparables. In support of this contention, the learned Authorised Representative drew our attention to various parts of the Annual Report of this company.

(v) This company is engaged not only in the development of software products but also in the provision of training services as can be seen from the website and the Annual Report of the company for the year ended 31.3.2008.

(vi) This company has two segments; namely,

a) Application Software Segment which includes software product revenues from two products i.e. 'Virtual Insure' and 'La-Vision' and

b) The Training segment which does not have any product revenues.

10.3 Per contra, the learned Departmental Representative contended that the decision of the co-ordinate bench of the Tribunal in the case of Triology E-Business Software India Pvt. Ltd. (supra) was rendered with respect to F.Y.2006-07 and therefore there cannot be an assumption that it would continue to be applicable to the year under consideration i.e. A.Y. 2008-09. To

this, the counter argument of the learned Authorised Representative is that the functional profile of this company continues to remain the same for the year under consideration also and the same is evident from the details culled out from the Annual Report and quoted above (supra).

10.4 We have heard both parties and perused and carefully considered the material on record. We find from the record that the TPO has drawn conclusions as to the comparability of this company to the assessee based on information obtained u/s.133(6) of the Act. This information which was not in the public domain ought not to have been used by the TPO, more so when the same is contrary to the Annual Report of the company, as pointed out by the learned Authorised Representative. We also find that the co-ordinate benches of this Tribunal in the assessee's own case for Assessment Year 2007-08 (supra) and in the case of Triology E-Business Software India Pvt. Ltd. (supra) have held that this company was developing software products and was not purely or mainly a software service provider. Apart from relying of the above cited decisions of coordinate benches of the Tribunal (supra), the assessee has also brought on record evidence from various portions of the company's Annual Report to establish that this company is IT(TP)A 1380/Bang/2012 Page 9 of 34 functionally dis-similar and different form the assessee and that since the findings rendered in the decisions of the coordinate benches of the Tribunal for Assessment Year 2007-08 (cited supra) are applicable for this year i.e. Assessment Year 2008-09 also, this company ought to be excluded from the list of comparables. In this view of the matter, we hold that this company i.e. KALS Information Systems Ltd., is to be omitted form the list of comparable companies. It is ordered accordingly."

"11.0 Infosys Technologies Ltd.

11.1 This was a comparable selected by the TPO. Before the TPO, the assessee objected to the inclusion of the company in the set of comparables, on the grounds of turnover and brand attributable profit margin. The TPO, however, rejected these objections raised by the assessee on the grounds that turnover IT(TP)A 1380/Bang/2012 Page 24 of 34 and brand aspects were not materially relevant in the software development segment.

11.2 Before us, the learned Authorised Representative contended that this company is not functionally comparable to the assessee in the case on hand. The learned Authorised Representative drew our attention to various parts of the Annual Report of this company to submit that this company commands

substantial brand value, owns intellectual property rights and is a market leader in software development activities, whereas the assessee is merely a software service provider operating its business in India and does not possess either any brand value or own any intangible or intellectual property rights (IPRs). It was also submitted by the learned Authorised Representative that :-

(i) the co-ordinate bench of this Tribunal in the case of 24/7 Customer.Com Pvt. Ltd. in ITA No.227/Bang/2010 has held that a company owning intangibles cannot be compared to a low risk captive service provider who does not own any intangible and hence does not have an additional advantage in the market. It is submitted that this decision is applicable to the assessee's case, as the assessee does not own any intangibles and hence Infosys Technologies Ltd. cannot be comparable to the assessee ;

(ii) the observation of the ITAT, Delhi Bench in the case of Agnity India Technologies Pvt. Ltd. in ITA No.3856 (Del)/2010 at para 5.2 thereof, that Infosys Technologies Ltd. being a giant company and market leader assuming all risks leading to higher profits cannot be considered as comparable to captive service providers assuming limited risk ;

(iii) the company has generated several inventions and filed for many patents in India and USA ;

(iv) the company has substantial revenues from software products and the break up of such revenues is not available ;

(v) the company has incurred huge expenditure for research and development;

(vi) the company has made arrangements towards acquisition of IPRs in 'AUTOLAY', a commercial application product used in designing high performance structural systems.

In view of the above reasons, the learned Authorised Representative pleaded that, this company i.e. Infosys Technologies Ltd., be excluded from the list of comparable companies.

11.3 Per contra, opposing the contentions of the assessee, the learned Departmental Representative submitted that comparability cannot be decided merely on the basis of scale of operations and the brand attributable profit margins of this company have not been extraordinary. In view of this, the learned Departmental Representative supported the decision of the TPO to include this company in the list of comparable companies.

11.4 We have heard the rival submissions and perused and carefully considered the material on record. We find that the assessee has brought on record sufficient evidence to establish that this company is functionally dissimilar and different from the assessee and hence is not comparable and the finding rendered in the case of Trilogy E-Business Software India Pvt. Ltd. (supra) for Assessment Year 2007-08 is applicable to this year also. We are inclined to concur with the argument put forth by the assessee that Infosys Technologies Ltd is not functionally comparable since it owns significant intangible and has huge revenues from software products. It is also seen that the break up of revenue from software services and software products is not available. In this view of the matter, we hold that this company ought to be omitted from the set of comparable companies. It is ordered accordingly.

12. Wipro Ltd.

12.1 This company was selected as a comparable by the TPO. Before the TPO, the assessee had objected to the inclusion of this company in the list of comparables on several grounds like functional dissimilarity, brand value, size, etc. The TPO, IT(TP)A 1380/Bang/2012 Page 26 of 34 however, brushed aside the objections of the assessee and included this company in the set of comparables.

12.2 Before us, the learned Authorised Representative of the assessee contended that this company i.e. Wipro Ltd., is not functionally comparable to the assessee for the following reasons :-

(i) This company owns significant intangibles in the nature of customer related intangibles and technology related intangibles, owns IPRs and has been granted 40 registered patents and has 62 pending applications and its Annual Report confirms that it owns patents and intangibles.

(ii) the ITAT, Delhi observation in the case of Agnity India Technologies Pvt. Ltd. in ITA No.3856(Del)/2010 at para 5.2 thereof, that Infosys Technologies Ltd. being a giant company and a market leader assuming all risks leading to higher profits, cannot be considered as comparable to captive service providers assuming limited risk;

(iii) the co-ordinate bench of the ITAT, Mumbai in the case of Telecordia Technologies India Pvt. Ltd. (ITA No.7821/Mum/2011) has held that Wipro Ltd. is not functionally comparable to a software service provider.

(iv) this company has acquired new companies pursuant to a scheme of amalgamation in the last two years.

(v) Wipro Ltd. is engaged in both software development and product development services. No information is available on the segmental bifurcation of revenue from sale of products and software services.

(vi) the TPO has adopted consolidated financial statements for comparability purposes and for computing the margins, which is in contradiction to the TPO's own filter of rejecting companies with consolidated financial statements.

12.3 Per contra, the learned Departmental Representative supported the action of the TPO in including this company in the list of comparables.

12.4.1 We have heard both parties and carefully perused and considered the material on record. We find merit in the contentions of the assessee for exclusion of this company from the set of comparables. It is seen that this company is engaged both in software development and product development services. There is no information on the segmental bifurcation of revenue from sale of product and software services. The TPO appears to have adopted this company as a comparable without demonstrating how the company satisfies the software development sales 75% of the total revenue filter adopted by him. Another major flaw in the comparability analysis carried out by the TPO is that he adopted comparison of the consolidated financial statements of Wipro with the stand alone financials of the assessee; which is not an appropriate comparison. 12.4.2 We also find that this company owns intellectual property in the form of registered patents and several pending applications for grant of patents. In this regard, the coordinate bench of this Tribunal in the case of 24/7 Customer.Com Pvt. Ltd. (ITA No.227/Bang/2010) has held that a company owning intangibles cannot be compared to a low risk captive service provider who does not own any such intangible and hence does not have an additional advantage in the market. As the assessee in the case on hand does not own any intangibles, following the aforesaid decision of the co-ordinate bench of the Tribunal i.e. 24/7 Customer.Com Pvt. Ltd. (supra), we hold that this company cannot be considered as a comparable to the assessee. We, therefore, direct the Assessing Officer/TPO to omit this company from the set of comparable companies in the case on hand for the year under consideration."

13. Tata Elxsi Ltd.

13.1 This company was a comparable selected by the TPO. Before the TPO, the assessee had objected to the inclusion of this company in the set of comparables on several counts like, functional dis-similarity, significant R&D activity, brand value, size, etc. The TPO, however, rejected the contention put forth by the assessee and included this company in the set of comparables.

13.2 Before us it was reiterated by the learned Authorised Representative that this company is not functionally comparable to the assessee as it performs a variety of functions under software development and services segment namely - (a) product design, (b) innovation design engineering and (c) visual computing labs as is reflected in the annual report of the company. The learned Authorised Representative submitted that,

- (i) The co-ordinate bench of the Mumbai Tribunal in the case of *Telcordia Technologies (P.) Ltd. (supra)* has held that *Tata Elxsi Ltd.* is not a functionally comparable for a software development service provider.

- (ii) The facts pertaining to *Tata Elxsi Ltd.* have not changed from the earlier year *i.e.* Assessment Year 2007-08 to the period under consideration *i.e.* Assessment Year 2008-09 and therefore this company cannot be considered as a comparable to the assessee in the case on hand.

- (iii) *Tata Elxsi Ltd.* is predominantly engaged in product designing services and is not purely a software development service provider. In the Annual Report of this company the description of the segment 'software development services' relates to design services and are not to software services provided by the assessee.

- (iv) *Tata Elxsi Ltd.* invests substantial funds in research and development activities which has resulted in the 'Embedded Product Design Services Segment' of the company to create a portfolio of reusable software components, ready to deploy frameworks, licensable IPs and products. The learned Authorised

Representative pleads that in view of the above reasons, Tata Elxsi *Ltd*. is clearly functionally different/dis-similar from the assessee and therefore ought to be omitted from the list of comparables.

13.3 Per contra, the learned Departmental Representative supported the stand of the TPO in including this company in the list of comparables.

13.4 We have heard both parties and carefully perused and considered the material on record. From the details on record, we find that this company is predominantly engaged in product designing services and not purely software development services. The details in the Annual Report show that the segment " software development services" relates to design services and are not similar to software development services performed by the assessee.

13.5 The Hon'ble Mumbai Tribunal in the case of *Telcordia Technologies India (P.) Ltd.* (*supra*) has held that Tata Elxsi *Ltd*. is not a software development service provider and therefore it is not functionally comparable. In this context the relevant portion of this order is extracted and reproduced below :—

" Tata Elxsi is engaged in development of niche product and development services which is entirely different from the assessee company. We agree with the contention of the learned Authorised Representative that the nature of product developed and services provided by this company are different from the assessee as have been narrated in para 6.6 above. Even the segmental details for revenue sales have not been provided by the TPO so as to consider it as a comparable party for comparing the profit ratio from product and services. Thus, on these facts, we are unable to treat this company as fit for comparability analysis for determining the arm's length price for the assessee, hence, should be excluded from the list of comparable portion."

As can be seen from the extracts of the Annual Report of this company produced before us, the facts pertaining to Tata Elxsi have not changed from Assessment Year 2007-08 to Assessment Year 2008-09. We, therefore, hold that this company is not to be considered for inclusion in the set of comparables in the case on hand. It is ordered accordingly.

14. E-Zest Solutions Ltd.

14.1 This company was selected by the TPO as a comparable. Before the TPO, the assessee had objected to the inclusion of this company as a comparable on the ground that it was functionally different from the assessee. The TPO had rejected the objections raised by the assessee on the ground that as per the information received in response to notice under section 133(6) of the Act, this company is engaged in software development services and satisfies all the filters.

14.2 Before us, the learned Authorised Representative contended that this company ought to be excluded from the list of comparables on the ground that it is functionally different to the assessee. It is submitted by the learned Authorised Representative that this company is engaged in 'e-Business Consulting Services', consisting of Web Strategy Services, I T design services and in Technology Consulting Services including product development consulting services. These services, the learned Authorised Representative contends, are high end ITES normally categorised as knowledge process Outsourcing ('KPO') services. It is further submitted that this company has not provided segmental data in its Annual Report. The learned Authorised Representative submits that since the Annual Report of the company does not contain detailed descriptive information on the business of the company, the assessee places reliance on the details available on the company's website which should be considered while evaluating the company's functional profile. It is also submitted by the learned Authorised Representative that KPO services are not comparable to software development services and therefore companies rendering KPO services ought not to be considered as comparable to software development companies and relied on the decision of the co-ordinate bench in the case of *Capital IQ Information Systems (India) (P.) Ltd. v. Dy. CIT (International Taxation)* [2013] 32 taxmann.com 21 (Hyd. - Trib.) and prayed that in view of the above reasons, this company *i.e.* e-Zest software *Ltd.*, ought to be omitted from the list of comparables.

14.3 Per contra, the learned Departmental Representative supported the inclusion of this company in the list of comparables by the TPO.

14.4 We have heard the rival submissions and perused and carefully considered the material on record. It is seen from the record that the TPO has included this company in the list of comparables only on the basis of the statement made by the company in its reply to the notice under section 133(6) of the Act. It appears that the TPO has not examined the services rendered by the company to give a finding

whether the services performed by this company are similar to the software development services performed by the assessee. From the details on record, we find that while the assessee is into software development services, this company *i.e.* e-Zest software *Ltd.*, is rendering product development services and high end technical services which come under the category of KPO services. It has been held by the co-ordinate bench of this Tribunal in the case of *Capital I-Q Information Systems (India) (P.) Ltd. (supra)* that KPO services are not comparable to software development services and are therefore not comparable. Following the aforesaid decision of the co-ordinate bench of the Hyderabad Tribunal in the aforesaid case, we hold that this company, *i.e.* e-Zest software *Ltd.* be omitted from the set of comparables for the period under consideration in the case on hand. The A.O./TPO is accordingly directed.

15. Thirdware Solutions *Ltd.* (Segment)

15.1 This company was proposed for inclusion in the list of comparables by the TPO. Before the TPO, the assessee objected to the inclusion of this company in the list of comparables on the ground that its turnover was in excess of Rs. 500 Crores. Before us, the assessee has objected to the inclusion of this company as a comparable for the reason that apart from software development services, it is in the business of product development and trading in software and giving licenses for use of software. In this regard, the learned Authorised Representative submitted that :—

- (i) This company is engaged in product development and earns revenue from sale of licences and subscription. It has been pointed out from the Annual Report that the company has not provided any separate segmental profit and loss account for software development services and product development services.
- (ii) In the case of *E-Gain Communications (P.) Ltd.* *v.* *ITO* [2009] 118 ITD 243/[2008] 23 SOT 385 (Pune), the Tribunal has directed that this company be omitted as a comparable for software service providers, as its income includes income from sale of licences which has increased the margins of the company.

The learned A.R. prayed that in the light of the above facts and in view of the afore cited decision of the Tribunal (*supra*), this company ought to be omitted from the list of comparables.

15.2 Per contra, the learned Departmental Representative supported the action of the TPO in including this company in the list of comparables.

15.3 We have heard the rival submissions and perused and carefully considered the material on record. It is seen from the material on record that the company is engaged in product development and earns revenue from sale of licenses and subscription. However, the segmental profit and loss accounts for software development services and product development are not given separately. Further, as pointed out by the learned Authorised Representative, the Pune Bench of the Tribunal in the case of *E-Gain Communications (P.) Ltd. (supra)* has directed that since the income of this company includes income from sale of licenses, it ought to be rejected as a comparable for software development services. In the case on hand, the assessee is rendering software development services. In this factual view of the matter and following the afore cited decision of the *Pune Tribunal (supra)*, we direct that this company be omitted from the list of comparables for the period under consideration in the case on hand.

16. Lucid Software Ltd.

16.1 This company was selected as a comparable by the TPO. Before us, the assessee has objected to the inclusion of this company as a comparable on the grounds that it is into software product development and therefore functionally different from the assessee. In this regard, the learned Authorised Representative submitted that —

- (i) This company is engaged in the development of software products.
- (ii) This company has been held to be functionally different and therefore not comparable to software service providers by the order of a co-ordinate bench of the Tribunal in the assessee's own case for Assessment Year 2007-08 (IT(TP)A No.845/Bang/2011), following the decision of Mumbai Tribunal in the case of *Telcordia Technologies India (P.) Ltd. (ITA No.7821/Mum/2011)*

- (iii) The rejection of this company as a comparable to software service providers has been upheld by the co-ordinate benches of this Tribunal in the cases of *LG Soft India (P.) Ltd.* and *CSR India (P.) Ltd. (supra)* and by the Delhi Bench of the Tribunal in the case of *Transwitch India (P.) Ltd. (supra)*. (ITA No.6083/Del/2010)
- (iv) The factual position and circumstances pertaining to this company has not changed from the earlier Assessment Year 2007-08 to the period under consideration i.e. Assessment Year 2008-09 and therefore on this basis, this company cannot be considered as a comparable in the case on hand.
- (v) The relevant portion of the Annual Report of this company evidences that it is in the business of product development.

The learned Authorised Representative prays that in view of the factual position as laid out above and the decisions of the co-ordinate benches of the Tribunal in the assessee's own case for Assessment Year 2007-08 and other cases cited above, it is clear that this company being into product development cannot be considered as a comparable to the assessee in the case on hand who is a software service provider and therefore this company *i.e.* Lucid software *Ltd.*, ought to be omitted from the list of comparables.

16.2 per contra, the learned Departmental Representative supported the action and finding of the TPO in including this company in the list of comparables.

16.3 We have heard the rival submissions and perused and carefully considered the material on record. It is seen from the details on record that the company *i.e.* Lucid software *Ltd.*, is engaged in the development of software products whereas the assessee, in the case on hand, is in the business of providing software development services. We also find that, co-ordinate benches of the Tribunal in the assessee's own case for Assessment Year 2007-08 (IT(TP)A No.845/Bang/2011), *LG Soft India (P.) Ltd. (supra)*, *CSR India (P.) Ltd. (supra)*; the ITAT, Mumbai Bench in the case of *Telcordia Technologies India (P.) Ltd. (supra)* and the Delhi ITAT in the case of *Transwitch India (P.) Ltd. (supra)* have held, that since this company, is engaged in the software product development and not software development services, it is functionally different and dis-similar and is therefore to be omitted from the list of comparables for software development service providers. The assessee has also brought on record details to demonstrate that the factual and

other circumstances pertaining to this company have not changed materially from the earlier year *i.e.* Assessment Year 2007-08 to the period under consideration *i.e.* Assessment Year 2008-09. In this factual matrix and following the afore cited decisions of the co-ordinate benches of this Tribunal and of the ITAT, Mumbai and *Delhi Benches (supra)*, we direct that this company be omitted from the list of comparables for the period under consideration in the case on hand.

17. Persistent Systems Ltd.

17.1 This company was selected by the TPO as a comparable. The assessee objected to the inclusion of this company as a comparable for the reasons that this company being engaged in software product designing and analytic services, it is functionally different and further that segmental results are not available. The TPO rejected the assessee's objections on the ground that as per the Annual Report for the company for Financial Year 2007-08, it is mainly a software development company and as per the details furnished in reply to the notice under section 133(6) of the Act, software development constitutes 96% of its revenues. In this view of the matter, the Assessing Officer included this company *i.e.* Persistent Systems *Ltd.*, in the list of comparables as it qualified the functionality criterion.

17.2 Before us, the assessee objected to the inclusion of this company as a comparable submitting that this company is functionally different and also that there are several other factors on which this company cannot be taken as a comparable. In this regard, the learned Authorised Representative submitted that :

- (i) This company is engaged in software designing services and analytic services and therefore it is not purely a software development service provider as is the assessee in the case on hand.
- (ii) Page 60 of the Annual Report of the company for F.Y. 2007-08 indicates that this company, is predominantly engaged in 'Outsourced software Product Development Services' for independent software vendors and enterprises.
- (iii) Website extracts indicate that this company is in the business of product design services.

- (iv) The ITAT, Mumbai Bench in the case of *Telcordia Technologies India (P.) Ltd. (supra)* while discussing the comparability of another company, namely Lucid Software Ltd. had rendered a finding that in the absence of segmental information, a company be taken into account for comparability analysis. This principle is squarely applicable to the company presently under consideration, which is into product development and product design services and for which the segmental data is not available.

The learned Authorised Representative prays that in view of the above, this company i.e. Persistent Systems *Ltd.* be omitted from the list of comparables.

17.2 Per contra, the learned Departmental Representative support the action of the TPO in including this company in the list of comparables.

17.3 We have heard the rival submissions and perused and carefully considered the material on record. It is seen from the details on record that this company i.e. Persistent Systems *Ltd.*, is engaged in product development and product design services while the assessee is a software development services provider. We find that, as submitted by the assessee, the segmental details are not given separately. Therefore, following the principle enunciated in the decision of the Mumbai Tribunal in the case of *Telcordia Technologies India (P.) Ltd. (supra)* that in the absence of segmental details/information a company cannot be taken into account for comparability analysis, we hold that this company i.e. Persistent Systems *Ltd.* ought to be omitted from the set of comparables for the year under consideration. It is ordered accordingly.

18. Quintegra SolutionsLtd.

18.1 This case was selected by the TPO as a comparable. Before the TPO, the assessee objected to the inclusion of this company in the set of comparables on the ground that this company is functionally different and also that there were peculiar economic circumstances in the form of acquisitions made during the year. The TPO rejected the assessee's objections holding that this company qualifies all the filters applied by the TPO. On the issue of acquisitions, the TPO rejected the assessee's objections observing that the assessee has not adduced any evidence as to how this event had an any influence on the pricing or the margin earned.

18.2 Before us, the assessee objected to the inclusion of this company for the reason that it is functionally different and also that there are other factors for which this company cannot be considered as a comparable. It was submitted that,

- (i) Quintegra Solutions Ltd., the company under consideration, is engaged in product engineering services and not in purely software development services. The Annual Report of this company also states that it is engaged in preparatory software products and is therefore not similar to the assessee in the case on hand.

- (ii) In its Annual Report, the services rendered by the company are described as under :

"Leveraging its proven global model, Quintegra provides a full range of custom IT Solution (such as development, testing, maintenance, SAP, product engineering and infrastructure management services), proprietary software products and consultancy services in IT on various platforms and technologies."

- (iii) This company is also engaged in research and development activities which resulted in the creation of Intellectual Proprietary Rights (IPRs) as can be evidenced from the statements made in the Annual Report of the company for the period under consideration, which is as under :

"Quintegra has taken various measures to preserve its intellectual property. Accordingly, some of the products developed by the company have been covered by the patent rights. The company has also applied for trade mark registration for one of its products, viz. Investor Protection Index Fund (IPIF). These measures will help the company enhance its products value and also mitigate risks."

- (iv) The TPO has applied the filter of excluding companies having peculiar economic circumstances. Quintegra fails the TPO's own filter since there have been acquisitions in this case, as is evidenced from the company's Annual Report for F.Y. 2007-

08, the period under consideration.

The learned Authorised Representative prays that in view of the submissions made above, it is clear that *inter alia*, this company i.e. Quintegra Solution *Ltd.* being functionally different and possessing its own intangibles/IPRs, it cannot be considered as a comparable to the assessee in the case on hand and therefore ought to be excluded from the list of comparables for the period under consideration.

18.3 Per contra, the learned Departmental Representative supported the action of the TPO in including this company in the set of comparables to the assessee for the period under consideration.

18.4 We have heard the rival submissions and perused and carefully considered the material on record. It is seen from the details brought on record that this company *i.e.* Quintegra Solutions *Ltd.* is engaged in product engineering services and is not purely a software development service provider as is the assessee in the case on hand. It is also seen that this company is also engaged in proprietary software products and has substantial R&D activity which has resulted in creation of its IPRs. Having applied for trade mark registration of its products, it evidences the fact that this company owns intangible assets. The co-ordinate bench of this Tribunal in the case of *24/7 Customer.Com (P.) Ltd. (supra)* has held that if a company possesses or owns intangibles or IPRs, then it cannot be considered as a comparable company to one that does not own intangibles and requires to be omitted from the list of comparables, as in the case on hand.

18.5 We also find from the Annual Report of Quintegra Solution *Ltd.* that there have been acquisitions made by it in the period under consideration. It is settled principle that where extraordinary events have taken place, which has an effect on the performance of the company, then that company shall be removed from the list of comparables.

18.6 Respectfully following the decision of the co-ordinate bench of the Tribunal in the case of *24/7 Customer.Com (P.) Ltd. (supra)*, we direct that this company i.e. Quintegra Solution *Ltd.* be excluded from the list of comparables in the case on hand since it is engaged in proprietary software products and owns its own intangibles unlike the assessee in the case on hand who is a software service provider.

19. Softsol India Ltd.

19.1 This company was selected by the TPO as a comparable. The assessee objected to the inclusion of this company as a comparable on the grounds that this company is functionally different and dis-similar from it. The TPO rejected the assessee's objections on the ground that as per the company's reply to the notice under section 133(6) of the Act, the company has categorized itself as a pure software developer and therefore included this company as a comparable as the assessee was also a provider of software development services. Before us, in addition to the plea that the company was functionally different, the assessee submitted that this company was excluded from the list of comparables by the order of the co-ordinate bench of this Tribunal in the assessee's own case for Assessment Year 2007-08 (ITA No. 845/Bang./2011) on the ground that the 'Related Party Transactions ('RPT') is in excess of 15%. The learned Authorised Representative submitted that for the current period under consideration, the RPT is 18.3% and therefore this company requires to be omitted from the list of comparables.

19.2 Per contra, the learned Departmental Representative supported the action of the TPO in including this company in the list of comparables as this company was a pure software development service provider like the assessee.

19.3 We have heard both parties and perused and carefully considered the material on record. We find that the co-ordinate bench of this Tribunal in the assessee's own case for Assessment Year 2007-08 in ITA No.845/Bang/2011 has excluded this company from the set of comparables for the reason that RPT is in excess of 15% following the decision of another bench of this Tribunal in the case of *24/7 Customer.Com (P.) Ltd. (supra)*. As the facts for this year are similar and material on record also indicates that RPT is 18.3%, following the afore cited decisions of the co-ordinate benches (*supra*), we hold that this company is to be omitted from the list of comparables to the assessee in the case on hand.

23. Thus, it is clear from the findings of the Co-ordinate Bench of the Tribunal in the case of M/s 3DPLM Software Solutions Ltd (*supra*) that except Bodhtree Ltd all other 12 companies were found to be not good comparables of the software development services as provided by assessee.

24. As regard the objection of the Id. DR that Quintegra Solution *Ltd.* has been selected by the assessee itself, we notice that the functional comparability of this company has been examined by the Tribunal in the case of M/s 3DPLM Software Solutions Ltd (*supra*) and it was found that the said company is engaged in the different field of services i.e. product designing and analytic services as well as in proprietary of software product and are in research and development activity which has resulted in creation of its intellectual property rights. Therefore, the said

company is not functionally comparable with pure software development service activity. Once the company is found to be a non-comparable company with the assessee, the same is required to be excluded from the set of comparables even if the said company is selected by the assessee itself. This view was taken by the decision of the Special Bench of Chandigarh Tribunal in the case QUARK SYSTEMS (P.) LTD (supra).

25. Thus, out of 20 comparables 12 companies are required to be excluded from the list of comparables for determining the ALP. Accordingly, we direct the TPO/AO to exclude the following companies from the set of comparables and recomputed the ALP after considering the claim of risk adjustment as well as working capital adjustment:

S.No.	Name of the Company
1	AvaniCimcon Technologies Ltd
2	Celestial Biolabs Ltd
3	E-Zest Solutions Ltd
4	Infosys Technologies Ltd
5	KALS Information Systems Ltd (Seg.)
6	Lucid Software Ltd
7	Persistent Systems Ltd
8	Quintegra Solutions Ltd
9	Softsole India Ltd
10	Tata Elxsi Ltd (Seg.)
11	Thirdware Solutions Ltd (Seg
12	Wipro Ltd (Seg.)”

Thus it is clear from the decision of co-ordinate bench of this Tribunal in the case of Kodiak Network (India) Pvt. Ltd. (supra) that out of 13 comparables sought to be excluded from the set of comparables the Tribunal found that 12 comparables as listed above are not functionally not comparable with software development service provider. Accordingly, following the order of this Tribunal in the case of Kodiak Network (India)

Pvt. Ltd. (supra), we direct the A.O./TPO to exclude 12 comparable companies from the set of comparables.

11.1 The next grievance of the assessee is regarding incorrect operating margin taken by the TPO. The learned Authorised Representative of the assessee has submitted that the TPO has computed the profit margin of the assessee without excluding the Fringe Benefit Tax ('FBT'). The learned Authorised Representative has referred to the decision of the Tribunal in assessee's case for the asst. year 2007-08 and submitted that an identical issue has been decided by the Tribunal by directing the A.O./TPO not to consider the FBT as part of the operating cost of the assessee when the same was not considered as part of the OC in the case of the comparables. The learned Authorised Representative has submitted that while computing the operating margin the TPO has considered the total expenditure at page 138 of the paper book showing that the total cost includes FBT. The learned Authorised Representative has then referred to page 176 of the paper book, the computation of total income at page 176 of paper book wherein the provision for FBT has been separately shown as an item not allowable. Thus he has pleaded

that the TPO may be directed to compute the correct PLI after excluding the FBT from the operating cost.

11.2 On the other hand, the learned Departmental Representative has relied upon the orders of the authorities below.

11.3 Having considered the rival submissions and careful perusal of the relevant record, we find that in the segment-wise margin the total expenses includes FBT. The assessee has given the details of FBT in the computation statement amounting to Rs.13,46,722/-. We find that for the asst. year 2007-08, this Tribunal in assessee's own case vide order dt. 23.11.2012 has directed the TPO that the FBT should not be considered as part of the operating cost of the assessee when the same was not considered by the TPO as part of the operating cost. Accordingly, we direct the TPO to consider the operating margin of the assessee after excluding the FBT from the operating cost.

12. The assessee is also seeking risk adjustment being a captive service provider. The learned Authorised Representative of the assessee has submitted that the Tribunal in the case of Kodiak Network (India) Pvt. Ltd. (supra) as well as in the case of 3DPLM Software Solution Ltd.

Vs. DCIT in IT(TP)A No.1303/Bang/2012 has held that the TPO should consider the risk adjustment while computing the ALP.

12.1 The learned Departmental Representative has submitted that the assessee is required to furnish complete details and computation of the risk adjustment. In the absence of complete details of computation the risk adjustment cannot be granted as a matter of right. He has relied upon the orders of the authorities below.

12.2 Having considered the rival submissions and relevant material on record, we find that in the case of Kodiak Network (India) Pvt. Ltd. (supra), the Tribunal in para 25 has directed the TPO to consider the risk adjustment. Similarly in the case of 3DPLM Software Solutions Ltd. (supra) the Tribunal has held as under :

" 20.3 We have heard both the learned Authorised Representative and learned Departmental Representative in the matter and perused and carefully considered the material on record. As regards risk adjustment, the TPO has not allowed any adjustment by observing that this has been considered and discussed in detail in the order for earlier years. We find that on similar facts, different co-ordinate benches of this Tribunal in the case of Intellinet Technologies India Pvt. Ltd. (ITA No.237/Bang/2010) and Bearing Point Business Consulting Pvt. Ltd. (ITA No.1124/Bang/2011) have held that the TPO ought to have given risk adjustment to the margins of the comparables for bringing them on par with the assessee and remanded the issue back to the file of the TPO. Following the decisions in the aforementioned cases of the co-ordinate benches of this Tribunal (supra), we remand the issue of market risk adjustment to the file of the Assessing Officer/TPO for examining the issue in the light of the decisions cited."

In view of the above decisions of the co-ordinate benches of the Tribunal, we direct the TPO to consider the risk adjustment of the margins of comparables for bringing them on par with the assessee.

12.1 The next issue raised by the assessee is regarding web site creation expenses which has been disallowed by the A.O by treating the same as capital in nature.

12.2 The learned Authorised Representative of the assessee has submitted that an identical issue has been considered by the Tribunal in the assessee's own case for the asst. year 2007-08 and the issue was remanded to the record of the A.O. for proper verification and examination. He has further submitted that for the asst. year 2010-11, the A.O. has allowed the depreciation on the amount of expenditure incurred on the web site creation. However, since the dispute regarding the earlier year is pending therefore the A.O. allowed the depreciation only on the expenditure incurred during the said year. Thus the learned Authorised Representative has submitted that the Tribunal may pass appropriate direction to the A.O./TPO in this regard.

12.3 On the other hand, the learned Departmental Representative has relied upon the orders of the authorities below and submitted that the Tribunal has already set aside to the record of the A.O./TPO for proper verification for the A.Y. 2007-08. By following the same, the issue may be remitted to the A.O. with similar direction.

12.4 We have considered the rival submission as well as relevant material on record. Without going into the controversy of allowable revenue expenditure we are of the view that even if this expenditure is considered as capital in nature, the assessee is entitled for depreciation on the entire expenditure incurred once the work of web site creation is completed. The A.O has already allowed the depreciation for the asst. year 2010-11. Therefore, we uphold the orders of the authorities below treating the said expenditure as capital in nature, however, the assessee may claim depreciation on the entire amount from the year in which the work is completed and the asset has come into existence.

13. Now we will take up the revenue's appeal wherein the revenue has raised the following grounds :

"1. The order of the learned CIT (Appeals) is opposed to law and facts of the case.

2. *On the facts and in the circumstances of the case the learned CIT (Appeals) has erred in holding that the size and turnover of the company are deciding factors for treating a company as a comparable, and accordingly erred in excluding M/s. Flextronics Ltd., M/s. iGATE Global Solutions Ltd., M/s. Infosys Technologies Ltd., M/s. Mindtree Ltd., M/s. Persistent Systems Ltd., M/s. Sasken Communications Technologies Ltd., M/s. Tata Elxsi Ltd. and M/s. Wipro Ltd. as comparable.*
3. *On the facts and in the circumstances of the case the learned CIT (Appeals) has erred in rejecting the diminishing revenue filter used by the TPO to exclude companies that do not reflect the normal industry trend.*
4. *On the facts and in the circumstances of the case the learned CIT (Appeals) has erred in accepting M/s. VGL Softech Ltd. as a comparable.*
5. *On the facts and in the circumstances of the case the learned CIT (Appeals) has erred in deleting M/s. Celestial Biolabs from the comparables as functionally different.*
6. *On the facts and in the circumstances of the case the learned CIT (Appeals) has erred in holding that the reimbursement of expenditure towards freight of Rs.1,27,288, telecommunication charges of Rs.65,70,127, insurance charges of Rs.18,57,172, travelling and conveyance charges of Rs.2,71,19,823 are to be excluded from the total turnover as well, for computation of deduction under Section 10A of the IT Act whereas such exclusion is permitted to arrive at the export turnover only as per the definitions given in section 10A of the IT Act and total turnover has not been defined in section 10A of the Act.*
7. *The CIT (Appeals) ought to have appreciated that the decision of Hon'ble High Court of Karnataka in the case of M/s. Tata Elxsi Ltd. on the issue of computing deduction under Section 10A by excluding the above expenses from export turnover and total turnover as well, has not reached finality in view of the pending Department's SLP before the Hon'ble Supreme Court.*
8. *For these and other grounds that may be urged at the time of hearing, it is prayed that the order of the CIT (Appeals) in so far as it relates to the above grounds may be reversed and that of the Assessing Officer may be restored.*

9. The appellant craves leave to add, alter, amend and / or delete any of the grounds mentioned above."

13.1 The first grievance of the revenue's appeal is regarding the turnover filter applied by the Id. CIT (Appeals). At the outset, the learned A.R. of the assessee has submitted that when the comparable companies are otherwise functionally dis-similar then at this stage the assessee will not insist for application of turnover filter.

13.2 Having considered the rival submissions and in view of the fact that we have already decided the functional comparability of the companies objected by the assessee as well as the contention of the Id. A.R. we allow this ground of the revenue's appeal and consequently modify the impugned order of the CIT (Appeals).

14.1 The next grievance of the revenue's appeal is that VGS Software Tech Ltd. was excluded by the TPO on the ground that the relevant data was not available whereas the CIT (Appeals) has included this company by considering the data filed by the assessee. Thus the learned Departmental Representative has submitted that the CIT (Appeals) has decided the issue of comparability of this company without giving an opportunity to the TPO/A.O to examine the same.

14.2 On the other hand, the learned Authorised Representative of the assessee has submitted that relevant details were available before the TPO/A.O, however, the TPO without considering the relevant details has decided not to include this company in the set of comparables. He has further contended that this company is otherwise functionally comparable and the CIT (Appeals) has given a finding after considering the relevant details and functional information.

14.3 Having considered the rival submission as well as the relevant material on record, we find that the TPO has rejected this company on the ground that the relevant data is not available in the public domain. The CIT (Appeals) has considered the relevant details obtained under section 133(6) of the Act.

14.4 In view of the above facts when the TPO did not examine the relevant details and data, we set aside this issue to the record of the TPO to consider the relevant information of this company as filed by the assessee before the CIT (Appeals) as well as before us. However, the learned Authorised Representative has submitted that these details were available with the TPO. In any case, we direct the TPO to consider the

relevant details and then decide the issue of comparability after giving an opportunity of hearing to the assessee.

15. The other objections of the revenue is regarding exclusion of certain companies including Celestial Biolabs which stand decided in view of our finding in the assessee's appeal in directing the 12 companies to be excluded from the set of comparables.

16. The next ground is regarding exclusion of freight charges, telecommunication charges, insurance charges, travelling and financial charges from the export turnover as well as total turnover while computing the deduction u/s. 10A of the Act.

16.1 We have heard the rival submission and perused the material on record. The Hon'ble Karnataka High Court in the case of CIT v M/s Tata Elxsi Ltd. & Others 349 ITR 98 (Kar) had held that while computing the exemption u/s 10A, if the export turnover in the numerator is to be arrived at after excluding certain expenses, the same should also be excluded from the total turnover in the denominator. The relevant finding of the Hon'ble jurisdictional High Court reads as follows:-

".....Section 10A is enacted as an incentive to exporters to enable their products to be competitive in the global market

and consequently earn precious foreign exchange for the country. This aspect has to be borne in mind. While computing the consideration received from such export turnover, the expenses incurred towards freight, telecommunication charges, or insurance attributable to the delivery of the articles or things or computer software outside India, or expenses if any incurred in foreign exchange, in providing the technical services outside India should not be included. However, the word total turnover is not defined for the purpose of this section. It is because of this omission to define 'total turnover', the word 'total turnover' falls for interpretation by this Court;

.....In section 10A, not only the word 'total turnover' is not defined, there is no clue regarding what is to be excluded while arriving at the total turnover. However, while interpreting the provisions of section 80HHC, the courts have laid down various principles, which are independent of the statutory provisions. There should be uniformity in the ingredients of both the numerator and the denominator of the formula, since otherwise it would produce anomalies or absurd results. Section 10A is a beneficial section which intends to provide incentives to promote exports. In the case of combined business of an assessee, having export business and domestic business, the legislature intended to have a formula to ascertain the profits from export business by apportioning the total profits of the business on the basis of turnovers. Apportionment of profits on the basis of turnover was accepted as a method of arriving at export profits. In the case of section 80HHC, the export profit is to be derived from the total business income of the assessee, whereas in section 10-A, the export profit is to be derived from the total business of the undertaking. Even in the case of business of an undertaking, it may include export business and domestic business, in other words, export turnover and domestic turnover. To the extent of export turnover, there would be a commonality between the numerator and the

denominator of the formula. If the export turnover in the numerator is to be arrived at after excluding certain expenses, the same should also be excluded in computing the export turnover as a component of total turnover in the denominator. The reason being the total turnover includes export turnover. The components of the export turnover in the numerator and the denominator cannot be different. Therefore, though there is no definition of the term 'total turnover' in section 10A, there is nothing in the said section to mandate that, what is excluded from the numerator that is export turnover would nevertheless form part of the denominator. When the statute prescribed a formula and in the said formula, 'export turnover' is defined, and when the 'total turnover' includes export turnover, the very same meaning given to the export turnover by the legislature is to be adopted while understanding the meaning of the total turnover, when the total turnover includes export turnover. If what is excluded in computing the export turnover is included while arriving at the total turnover, when the export turnover is a component of total turnover, such an interpretation would run counter to the legislative intent and impermissible. Thus, there is no error committed by the Tribunal in following the judgements rendered in the context of section 80HHC in interpreting section 10A when the principle underlying both these provisions is one and the same".

16.2 The Hon'ble Bombay High Court in the case of CIT Vs. Gem Plus Jewellery India Ltd. 330 ITR 175, in identical circumstances, held that since the export turnover forms part of the total turnover, if an item is excluded from the export turnover, the same should also be reduced from the total turnover to maintain parity between numerator

and denominator while calculating deduction u/s 10A of the Act. The relevant finding of the Hon'ble Mumbai High Court reads as follows:-

"The total turnover of the business carried on by the undertaking would consist of the turnover from export and the turnover from local sales. The export turnover constitutes the numerator in the formula prescribed by sub-section (4). Export turnover also forms a constituent element of the denominator in as much as the export turnover is a part of the total turnover. The export turnover, in the numerator must have the same meaning as the export turnover which is constituent element of the total turnover in the denominator. The legislature has provided a definition of the expression "export turnover" in Explan.2 to s.10A which the expression is defined to mean the consideration in respect of export by the undertaking of articles, things or computer software received in or brought into India by the assessee in convertible foreign exchange but so as not to include inter alia freight, telecommunication charges or insurance attributable to the delivery of the articles, things or software outside India. Therefore in computing the export turnover the legislature has made a specific exclusion of freight and insurance charges. The submission which has been urged on behalf of the revenue is that while freight and insurance charges are liable to be excluded in computing export turnover, a similar exclusion has not been provided in regard to total turnover. The submission of the revenue, however, misses the point that the expression "total turnover" has not been defined at all by Parliament for the purposes of s.10A. However, the expression "export turnover" has been defined. The definition of "export turnover" excludes freight and insurance. Since export turnover has been defined by Parliament and there is a specific exclusion of freight and insurance, the expression "export turnover" cannot have a different meaning when

it forms a constituent part of the total turnover for the purposes of the application of the formula. Undoubtedly, it was open to Parliament to make a provision which has been enunciated earlier must prevail as a matter of correct statutory interpretation. Any other interpretation would lead to an absurdity. If the contention of the Revenue were to be accepted, the same expression viz. 'export turnover' would have a different connotation in the application of the same formula. The submission of the Revenue would lead to a situation where freight and insurance, though these have been specifically excluded from 'export turnover' for the purposes of the numerator would be brought in as part of the 'export turnover' when it forms an element of the total turnover as a denominator in the formula. A construction of a statutory provision which would lead to an absurdity must be avoided. Moreover, a receipt such as freight and insurance which does not have any element of profit cannot be included in the total turnover. Freight and insurance charges do not have any element of turnover. For this reason in addition, these two items would have to be excluded from the total turnover particularly in the absence of a legislative prescription to the contrary - CIT v Sudarshan Chemicals Industries Ltd. (2000) 163 CTR (Bom) 596; (2000) 245 ITR 769 (Bom) applied; CIT v Lakshmi Machine Works (2007) 210 CTR (SC) 1; (2007) 290 ITR 667 (SC) and CIT v Catapharma (India) (P) Ltd. (2007) 211 CTR (SC) 83; (2007) 292 ITR 641 (SC) relied on"

16.3 In the light of the above binding precedent, we are of the view that the order of the CIT(A) is correct and in accordance with law and he is justified in directing the AO to exclude the above mentioned expenses both from the export turnover as well as from the total turnover while

calculating deduction u/s 10A of the Act. Accordingly, the grounds raised on this issue by revenue are dismissed.

17. In view of the above findings when we have directed the TPO to exclude 12 comparable companies and also to re-examine one of the companies, it is directed to recompute the ALP after considering the correct operating margin of the assessee as well as considering the risk adjustment. Needless to say that the benefit of proviso to Section 92C(2) has to be considered if the assessee's operating margin is within the tolerance range of mean margin.

18. In the result, the appeals of the assessee as well as the revenue are partly allowed.

Order pronounced in the open court on the 8th day of June, 2016.

Sd/-
(INTURI RAMA RAO)
Accountant Member

Sd/-
(VIJAY PAL RAO)
Judicial Member

*Reddy gp