

IN THE INCOME TAX APPELLATE TRIBUNAL
BENGALURU BENCH 'A', BENGALURU

BEFORE SMT. ASHA VIJAYARAGHAVAN, JUDICIAL MEMBER
AND
SHRI. S. JAYARAMAN, ACCOUNTANT MEMBER

I.T(TP).A No.477/Bang/2013
(Assessment Years : 2005-06)

Deputy Commissioner of Income Tax,
Circle -11(1), Bengaluru

..Assessee

v.

M/s. ACI Worldwide Solutions P. Ltd,
Salarpuria Cambridge Mall, No.9, Ulsoor,
Bengaluru 560 008
PAN : AAACV7566R

..Respondent

Cross objection No.153/Bang/2015
(In I.T(TP).A No.477/Bang/2013)
(Assessment Years : 2005-06)
(By the Assessee)

Assessee by : Shri. Padam Chand Khincha, CA
Revenue by : Shri. H. Ananda, JCIT

Heard on : 04.08.2016
Pronounced on : .10.2016

ORDER

PER S. JAYARAMAN, ACCOUNTANT MEMBER :

These appeal and cross objection filed by the Revenue and Assessee, respectively, are against the order of the CIT (A) -5, Bengaluru, dt.31.01.2013, for the assessment year 2005-06.

2. The assessee is a private limited company. During the year under consideration, it was a subsidiary of Visual Web Solutions, Inc, a company incorporated under the laws of the State of New Jersey, USA. On February 07, 2007, Visual Web Group was taken over by ACI Worldwide Group globally. Accordingly, the assessee's name was changed from Visual Web Solutions Private Limited to ACI Worldwide Solutions Private Limited. The assessee is engaged in the business of software development. It exports the entire software to its parent company. It filed a return on 31.10.2005, declaring a income of Rs 9,60,890/- after setting off the carried forward loss of Rs. 33,48,560/.

03. The assessee's international transactions with its AE consisted of software development to the tune of Rs. 6,56,40,185/. It had filed an audit report certifying that the prices charged in the international transaction with its AE were at arm's length, using Prowess database selected 16 companies as comparables with data relating to FYs 2003-04 and 2004-05 adopted the Cost Plus Method (CPM) as the most appropriate method. It also made an adjustment for differences in marketing and finance function in the process of arriving at the ALP.

04. However, the TPO rejected the CPM method adopted by the assessee and adopted the transactional net margin method (TNMM) to carry out a new TP analysis with 17 companies as comparables and computed the average net profit margin of the comparables at 26.59%. After providing for a working capital adjustment of 1.20%, the net mean margin was taken at 25.39%. Based on this margin, the TPO determined the ALP of the international transaction at Rs.7,53,15,927/- and the TP adjustment at Rs 96,75,742/- in the order passed under section 92CA on 24.10.2008. On an appeal, the CIT(A) although upheld the TP Study made by the TPO, however, directed the TPO to exclude iGate Solution Ltd., L&T Infotech Ltd., Satyam Computers Ltd., M/s Infosys Technology Ltd. & M/s Flextronics Software Systems Ltd from the comparables based on the size, turnover and brand of those companies, exclude Exensys Software Solutions Ltd and Thirdware Solutions Ltd from the comparables based on abnormal profit, exclude M/s Tata Elxsi Ltd from the comparables being functionally different and include M/s Bodhtree Consulting Ltd as a comparable in the segment. Aggrieved, the Revenue filed this appeal and the Assessee filed the cross objection. The grounds of Revenue's appeal are extracted as under :

1. The order of the Learned CIT (Appeals), in so far as it is prejudicial to the interest of revenue, is opposed to law and the facts and circumstances of the case.

2. The learned CIT(A) erred in holding that the size, turnover and brand of the company are deciding factors for treating a company as a comparable, and accordingly erred in excluding iGate Solution Ltd., L&T Infotech Ltd., Satyam Computers Ltd., *MI*s Infosys Technology Ltd., M/s Flextronics Software Systems Ltd., as a comparable in the segment.

3. The Ld.CIT(A) erred in rejecting companies on the basis of Abnormal Profit and excluding the comparable companies Exensys Software Solutions Ltd and Thirdware Solutions Ltd without defining what constitutes abnormal profit filter and how the same is determined.

4. The CIT(A), in the facts and circumstances of the case, erred in holding that M/s Bodhtree Consulting Ltd, cannot be taken as comparable, without appreciating the fact that the company qualifies all the quantitative filters applied by the TPO in selection of this company as a comparable.

5. The CIT(A), in the facts and circumstances of the case, erred in holding that M/s Tata Elxsi Ltd, cannot be taken as a comparable, being functionally different without appreciating the fact that it satisfies all the qualitative and quantitative filters applied by the TPO.

6. For these and such other grounds that may be urged at the time of hearing, it is humbly prayed that the order of the CIT(A) be reversed and that of the Assessing Officer be restored.

7. The appellant craves leave to add, to alter, to amend or delete any of the grounds that may be urged at the time of hearing of the appeal.

05.The effective grounds of cross objections are extracted as under:

1. The Order of the learned Commissioner of Income Tax (Appeals) – IV [CIT (A)], to the extent prejudicial to the Respondent is bad in law.
5. The learned CIT(A) has erred in confirming the action of the Assessing officer and Transfer Pricing Officer in:
 - a. Adopting unjustifiable and inappropriate filters while selecting comparables under TNMM;
 - b. Adopting companies as comparables even though they are not comparables in terms of functions performed, risks assumed, assets utilized etc.
 - c. Adopting companies like Foursoft Ltd, Geometric Software Solutions Company and Sankhya Infotech Ltd. as comparables even though they are not comparable in terms of functions performed, risks assumed, assets utilized, etc.
 - d. Adopting Foursoft Ltd. and Geometric Software Solutions as comparables even though they are not comparables as their related party transactions are more than 15% of operating revenue.
6. The learned CIT(A) has erred in confirming the action of the Assessing officer and Transfer Pricing Officer in:
 - a. Not making appropriate adjustments for qualitative and quantitative difference between the business of the Respondent and those of the comparable companies; and
 - b. Not appreciating that the Respondent is insulated from certain risks, as against comparables, which assume these risks and therefore have to be credited with a risk premium on this account.
7. The CIT (A) after going through the disclosures available in the website www.bodhtree.com, its reply u/s133(6) and non-availability of break up of segmental revenue ,inter alia, held

that Bodhtree Consulting Ltd is functionally different from the assessee and it fails the functionality filter set by the TPO.

7.1 On Exensys Software Solutions Ltd and Thirdware Solutions Ltd, the CIT(A) held that since these companies had abnormally high profit margins ie above 50%, he directed the TPO to exclude them as comparables.

7.2 Before the CIT(A), the assessee pleaded that Sankhya Infotech Ltd is not a comparable as it is engaged in the business of eLearning application practices, it had been focusing on development of niche products for the transport and aviation industry etc. However, the CIT(A) did not find any merit in such contention.

7.3 In respect of Geometric Software Solutions Ltd, the assessee pleaded before the CIT(A) that this company specializes in Product Life Management solutions for mechanical design, manufacturing and industrial markets etc, the company had software products and services but no segmental information was available on the software services, even if the onsite filter is had to be applied there was no information pertaining to the split between onsite and offshore revenues in its annual report etc and hence it is not a comparable. However, the CIT(A) did not find any merit in such contention.

7.4 With regard to Tata Elxsi Ltd, the CIT(A) relying on the hon'ble Mumbai ITAT decision of Telcordia Technologies held that the range of activities of that company is substantially and significantly different from this assessee and hence directed the AO to exclude it from the comparables.

06. Before us, the AR pleaded that the comparables Bodhtree Consulting Ltd, Exensys Software Solutions Ltd , Thirdware Solutions Ltd, Sankhya Infotech Ltd, Foursoft Ltd, Tata Elxsi Ltd have to be rejected as they are functionally different . In this regard, he relied on a host of the decisions. A

few are listed below :

- NetHawk Networks India Private Ltd Vs ITO TS-303-ITAT-2013 AY 2008-09
- M/s. CISCO Systems (India) Pvt Ltd vs. DCIT TS-246-ITAT-2014(Bang)-TP AY 2009-10
- M/s Mindteck India Ltd vs. DCIT TS-291-ITAT-2014(Bang)-TP AY 2009-10
- DCIT v Kodiak Networks India Pvt. Ltd IT(TP)A No. 532/ Bang/ 2013 AY 2005-06.
- ITO vs. Vendio Technologies India Pvt Ltd TS-333-ITAT-2014(Bang)-TP AY 2005-06.
- ITO vs. Sunquest Information Systems (India) Private Limited IS - 299-ITAT-2015 (Bang)-TP AY 2005-06.

6.1 Further, the AR has pleaded that the comparables Exensys Software Solutions Ltd has to be rejected as there is an exceptional event of merger, Sankhya Infotech Ltd has to be rejected as it fails onsite revenue filter, Foursoft Ltd has to be rejected as its RPT is greater than 15% of turnover & further it fails onsite revenue filter also . Geometric Software Solutions Ltd has to be rejected as the RPT is greater than 15% of the turnover and furnished a copy of RPT computation showing it at 21.29% . In this regard, he relied on a host of the decisions. A few are listed below :

- i ITO vs. Sunquest Information Systems (India) Private Limited IS - 299-ITAT-2015 (Bang)-TP AY 2005-06
- ii. M/s Hellosoft India Pvt. Ltd. hA No.645/Hyd/09 AY 2005-06
- iii M/s IVY Comptech Pvt. Ltd. [2014] 43 taxmann.com 183 (Hyderabad - Trib.) AY 2005-06
- iv ITO vs. Vendio Technologies India Pvt Ltd TS-333-ITAT-2014(Bang)-TP AY 2005-06
- v. M/s 24/7 Customer.Com Pvt Ltd [2012] 28 taxmann.com 258 (Bang.)

7. We have considered the above submissions. This Tribunal in the case of the DCIT v Kodiak Networks India Pvt. Ltd IT(TP)A No. 532/Bang/ 2013 AY 2005-06, examined the Bodhtree Consulting Ltd's accounts and, inter alia, found that that company had erratic margins and growth over the years, its margins are consistently changing , its revenue recognition policy is not proper, its growth rate is over the years is fluctuating to extremes etc these circumstances are peculiar in nature and further require analysis without which this company should be rejected as a comparable .

7.1 On Exensys Software Solutions Ltd, this Tribunal in the above case , found that that company operates atleast in 3 business segments viz provisions of software services, BPO services and has developed its own software products like exensys financials , exensys site etc while that assessee like this assessee is a mere software service provider to its AE and on such facts held that Exensys Software Solutions Ltd is functionally different and hence directed the TPO to exclude it from the list of comparable and treated the abnormal profits issue as an academic in nature.

7.2 In respect of Thirdware Solutions Ltd , the CIT(A) directed to exclude this company as it had high profit margins of 66.09% without

the assessee demonstrating that such profits were abnormally high due to any extraordinary event or reason and hence , relying on the ratio of 24/7 customer.com Pvt Ltd in ITA No 227/ Bang/2010 dt 09.11.2012 , this Tribunal reversed the order of the CIT(A) but held that since the assessee's claim that it is functionally different from it has not been examined by the CIT(A), it directed the CIT(A) to examine this claim for exclusion after affording the assessee adequate opportunity of being heard.

7.3 In respect of Sankhya Infotech Ltd , this Tribunal in the case of the ITO v M/s Sunquest information Systems (India) P Ltd, in IT(TP)A No. 1032/ Bang/ 2011, AY 2005-06, after examining the activities of Sankhya Infotech Ltd and the decision of the Delhi Tribunal in ITO v Colt Technology Services India P Ltd in ITA No.6091/Del/ 2011, AY 2005-06 wherein it was held that Sankhya Infotech Ltd is not comparable to Colt Technology Services India P Ltd which was in the business of software development, held that it can not be a comparable with M/s Sunquest information Systems (India) P Ltd which is software development company . This assessee is also in software development.

7.4 In respect of Foursoft Ltd, this Tribunal in the case of the ITO v

M/s Sunquest information Systems (India) P ltd, in IT(TP)A No. 1032/Bang/ 2011, AY 2005-06, after examining the Hyderabad Tribunal decision, inter alia, found that this company is in the product development and owns products namely 4SeTrans etc, having IP rights and hence is not a comparable.

7.5 In respect of Geometric Software Solutions Ltd, the assessee has not challenged the finding of the TPO on the ground of the RPT. Hence following this Tribunal decision in ITO vs. Vendio Technologies India Pvt Ltd TS 333-ITAT-2014(Bang)-TP AY 2005-06, this issue is set aside to the TPO for fresh examination and decision after affording the assessee adequate opportunity of being heard.

7.6 In respect of Tata Elxsi Ltd, this Tribunal in ITO vs. Vendio Technologies India Pvt Ltd IT (TP)A No 1374/Bang/2011 AY 2005-06, after referring to the hon'ble Mumbai ITAT decision Telcordia Technologies, inter alia, held that the range of activities of that company is substantially and significantly different from this assessee and hence directed the TPO to exclude it from the comparables.

08. Following the above decisions of the Tribunal, we hold that Bodhtree Consulting Ltd, Exensys Software Solutions Ltd, Sankhya

Infotech Ltd, Foursoft Ltd and Tata Elxsi Ltd should be excluded as a comparable from the list of comparable. Thus, the Revenues appeal grounds no 3 in part, no 4 & no 5 are treated as dismissed. The issues in respect of Thirdware Solutions Ltd and Geometric Software Solutions Ltd are set aside to the CIT(A) and the TPO, respectively, as discussed above. To this extent, the Revenue's and Assessee's appeal are treated as allowed for statistical purposes.

09. In respect of the five comparables, viz iGate Global Solutions Ltd, Flextronics Software Systems Ltd, Larsen Infotech Ltd. , Satyam Computer Services Ltd and Infosys Ltd it is submitted that they fail upper turnover filter of Rs. 200 crores and should be rejected as comparables in view of a host of decisions. Further, it was submitted that Flextronics Software Systems Ltd , Satyam Computer Services Ltd & Infosys Ltd are to be rejected as they are functionally different. Besides Satyam Computer Services Ltd has to be rejected as the financials of that company is not reliable and Infosys Ltd has to be rejected as it is has high brand value etc relying on the following decisions.

i M/s Genisys Integrating Systems (India) Pvt. Ltd v DCIT ITA No. 1231 /Bang/2010

ii M/s Kodiak Networks (India) Private Limited Vs. ACIT (ITA No.1413/Bang/2010) : [2012]18 taxmann.com 32 (Bang)

iii M/s Genesis Microchip (I) Private Limited Vs. DCIT (ITA No.1254/Bang/2010): [2012] 20 taxmann.com 237 (Bang)

iv M/s. Trilogy E-Business Software India Private Ltd. v. DCIT -ITA

- No.1054/Bang/2011 dated 23.11.2012: [2013] 29 taxmann.com 310 (Bang)
- v M/s Bearing Point Business Consulting Pvt. Ltd Vs. DCIT -ITA No. 1124/Bang/2011: [2013] 33 taxmann.com 92 (Bang)
- vi M/s CSR India Pvt. Ltd Vs. ITO - IT(TP)A No.1119/Bang/2011: [2013] 31 taxmann.com 265(Bang)
- vii M/s. Mercedes Benz Research & Development India Pvt Ltd Vs. DCIT-IT(TP)A No. 1222/Bang/201 1: TS-108-ITAT-2013-Bang-TP
- viii LG Soft India Private Limited TS-64-ITAT-2013
- ix I.P. Unity Communications Pvt Ltd Vs ITO [TS-292-ITAT-2014(Bang)-TP]
- x EMC Data Storage Systems (India) Pvt Ltd Vs DCIT [TS-276-ITAT-2014(Bang)-TP]
- xi Huawei Technologies (I) P. Ltd Vs ITO [TS-270-ITAT-2014(Bang)-TP]
- xii ITO vs. Sunquest Information Systems (India) Private Limited TS -299-ITAT-201 5 (Bang)-TP AY 2005-06.

9.1 In this regard, the CIT (A) also placed reliance on the decisions of the Hon'ble jurisdictional Bench of ITAT in the case of Genisys Integrating Systems (India) Ltd. v. DCIT [2012] 53 SOT 159 (Bang) wherein it has been held that when there is a limit for the lower end for identifying comparables, there is no reason why there should not be an upper limit also, as size matters in business, etc., Although this Tribunal in its later decision in the case of ACIT v. M/s. McAfee Software (India) P. Ltd in IT(TP)A No.04/Bang.2012, dt.18.03.2016, for the assessment year 2005-06, held that the turnover of M/s. McAfee was about Rs.63 crores, turnover of Igate Global Solutions Ltd (seg) was about Rs.405 crores and that of L & T Infotech Ltd was about 562 crores, which was within the range of ten times the upper limit and hence retained Igate Global Solutions Ltd

(seg) and L & T Infotech Ltd as comparables. In the present case, the assessee's turnover is only Rs.6.56 crores. This is beyond the range of ten times the upper limit. In view of the same the TPO is directed to exclude Igate Global Solutions Ltd (seg) and L & T Infotech Ltd from the list of comparables.

9.2 In the same decision, the coordinate bench of this Tribunal has by following the decision of the coordinate bench of the Tribunal in ITO v. M/s. Sunquest Information Systems (India) P. Ltd in IT(TP)A No.1302/Bamg/2011, dt.11.06.2015, held that M/s. Flextronics Software Systems Ltd is functionally different and directed the TPO to exclude the same. Following the same, we direct the TPO to exclude Flextronics Software Systems Ltd, from the list of comparables.

9.3 Rejection of the comparability of M/s. Sathyam Computers Ltd, on the basis of non-reliability of financial data and the rejection of M/s. Infosys Technology Ltd on the basis of functional dissimilarity, having high turnover and brand name etc, in accordance with the decisions relied on by the Ld. AR is found in order and accordingly the TPO is directed to exclude them from the list of comparables.

9.4 Thus, the Revenue's appeal ground no 2 is treated as dismissed and the Assessee's corresponding appeal grounds are treated as allowed.

10. In the result, the Revenue's appeal and the cross objection filed by the Assessee are treated as 'partly allowed'.

Order pronounced in the open court on 31st day of October, 2016.

Sd/-

Sd/-

(SMT. ASHA VIJAYARAGHAVAN)
JUDICIAL MEMBER

(S. JAYARAMAN)
ACCOUNTANT MEMBER

MCN*

Copy to:

1. The assessee
2. The Assessing Officer
3. The Commissioner of Income Tax
4. The Commissioner of Income Tax (A)
5. DR
6. GF, ITAT, Bangalore

By Order

Assistant Registrar

