

**INCOME TAX APPELLATE TRIBUNAL  
DELHI BENCH "I-2": NEW DELHI  
BEFORE SMT DIVA SINGH, JUDICIAL MEMBER  
AND  
SHRI PRASHANT MAHARISHI, ACCOUNTANT MEMBER**

ITA No.1255/Del/2014  
(Assessment Year: 2009-10)

Agilent Technologies  
(International) Pvt. Ltd,  
Plot No.-CP-11, Sector-8,  
IMT Mangsar, Gurgaon  
PAN: AADCA4115C

**(Appellant)**

Vs.

ACIT,  
Circle-1,  
Gurgaon

**(Respondent)**

Assessee by :	Mr. Kanchan Kaushal, Ms. Shruti Khimta, AR
Revenue by:	Mr. Sunil Sharma, CIT DR
Date of Hearing	05/07/2016
Date of pronouncement	29/09/2016

**ORDER**

**PER PRASHANT MAHARISHI, A. M.**

1. This appeal is filed by assessee against the order of the ld Assessing Officer (in short 'AO') dated 30.12.2013 for the Assessment Year 2009-10 passed u/s 143(3) rws 144C of the Income Tax Act ( in short 'the Act') pursuant to the direction u/s 144C of the Income Tax Act by ld. Dispute Resolution Panel ( in short 'DRP') dated 3.10.2013 on draft assessment order dated 28.02.2013 of ld. AO incorporating the Transfer pricing adjustment proposed u/s 92 CA (3) by The Ld. Transfer pricing officer ( in short 'TPO') by his order dated 29.01.2013.
2. The assessee has raised the following grounds of appeal:-

- “1 The assessment order passed by the Learned Assessing Officer ("Ld. AO") pursuant to the directions of Learned Dispute Resolution Panel ("Ld. DRP") is bad in law and void ab-initio.
2. The Ld. TPO and the Ld. AO (following the directions of the Ld. DRP), erred both on facts and in law in confirming the addition of Rs. 2,10,42,855 to the income of the appellant proposed by holding that its international transaction pertaining to software development business segment do not satisfy the arm's length principle envisaged under the Act. In doing so, the Ld. DRP and the Ld. AO has grossly erred in agreeing with and upholding the Ld. TPO's action of:
- 2.1 disregarding the fact that the economic analysis undertaken by the Appellant is in accordance with the provisions of the Income Tax Act, 1961 ("the Act") read with the Income Tax Rules, 1962 ("the Rules"), and modifying the economic analysis for the determination of the Arm's Length Price ("ALP") of the Appellant's international transactions and holding that the international transactions are not at arm's length;
- 2.2 disregarding use of multiple year data, as adopted by the Appellant in Transfer Pricing documentation;
- 2.3 disregarding use of data pertaining to any other year apart from financial year 2008-09 for determining the arm's length margins/ prices ,which was not available to the Appellant at the time of complying with the Transfer Pricing documentation requirements;
- 2.4 rejecting certain comparable companies identified by the Appellant, by applying employee cost greater than 25 percent of the sales as a comparability criterion;
- 2.5 rejecting certain comparable companies identified by the Appellant, by applying export earnings less than 75 percent of operating revenues as a comparability criterion;
- 2.6 excluding companies with turnover less than Rs. 1 Crore but not applying a similar filter to exclude oversized companies.;
- 2.7 rejecting certain comparable companies identified by the Appellant, having economic performance contrary to the industry behavior/ witnessing peculiar economic circumstances (e.g. companies which showed a diminishing revenue trend);
- 2.8 rejecting certain comparable companies identified by the Appellant, having different accounting year than the Appellant (i.e. companies having accounting year other than March 31 or companies whose financial statements were for a period other than 12 months);
- 2.9 selecting certain companies which are earning super normal profits as comparable to the Appellant to benchmark the impugned transaction;
- 2.10 rejecting certain companies on an ad-hoc basis and cherry picking a few comparables 10 include in the final set of comparables to determine the arm's length price of the impugned transaction;
- 2.11 incurring computational errors in the margin used for the determination of the arm's length price;
- 2.12 failing to make suitable adjustments to account for differences in the risk profile of the Appellant vis-a-vis the comparables;
- 2.13 failing to make appropriate adjustments to account for differences in working capital employed by the Appellant vis-a-vis comparable companies.
3. Ld. AO has grossly erred on facts and in law by computing book profits after adding transfer pricing adjustment made under normal provisions of the Act;
4. The Ld. AO has grossly erred on facts and in law by initiating penalty under section 271(1)(c) of the Act mechanically and without recording any satisfaction for its initiation;

5. The Ld. AO has grossly erred on facts and in law by proposing to compute interest under section 234A, 234B, 234C and 234D of the Act mechanically and without recording any satisfactory reasons for the same;
  6. The Ld. TPO has disregarding judicial pronouncements in India in undertaking the TP adjustment. That the above grounds of appeal are independent and without prejudice to each other.
3. Appellant company is a private limited company being 100 % subsidiary of Agilent Technologies International Europe, BV who is also in turn subsidiary of Agilent technologies US. European company is a leading measurement company-providing core bio-analytical and electronic measurement solution to the common indications, electronics, life sciences and chemical analysis industries.
4. For the year assessee e-filed its return of income on 2<sup>nd</sup> of March 2011 declaring taxable income of Rs. 24601344/-. As it was found that assessee has entered into international transactions with its associated enterprise reference was made to the Ld. Transfer Pricing Officer to determine arm's length price of the international transactions with respect to software development segment and ITES segment of the assessee.
5. Brief facts of the international transaction of the appellant company is that that assessee primarily operates into two segments (i) provision of information technologies enabled services and (ii) provision of software development services. The software development segment includes providing software development services and maintenance support services to its associated enterprises. Software development services includes development of modules as well as a part of modules for software being used by its overseas group entities in their products whereas maintenance support services include bug fixing, carrying on maintenance and support services. In the provision

of information technologies enabled services, it involves IT support and network management and financial back-office support to associated enterprises. The financial backup office support includes internal financial transactions processing for sales accounting and vendor is payable for the associated enterprise and IT support and network management includes providing knowledge management for engineering design and network management for the wireless network solutions business of the US parent company. During the year international transactions with respect to the provision of ITES segment was Rs. 1727080283/- and with respect to the provision of software development services is Rs. 336550515/-. In its transfer pricing study report the appellant selected Transactional Net Marginal Method (TNMM) as most appropriate method adopting (MAM) profit level indicator (PLI) as operating profit/total cost (OP/TC) using multiple year data selecting 21 comparables in software development service segment and ex comparables in IT enabled services segment. On the basis of the above analysis the assessee has demonstrated that the average operating profit/total cost of the comparable companies in software development service segment is 9.97% and in case of IT enabled services segment it is 14.90 % whereas the appellant's profit level indicator with respect to software development service segment is 15.26 % and in ITES segment 19% and therefore the international transactions entered into by the appellant with its associated enterprise are at arm's length.

6. On perusal of the FAR of the appellant, it was noted that it performs functions of strategic management functions which include the day today management of the business based on the

overall strategy for the group decided by the associated enterprise of the assessee. Regarding corporate service function, it is responsible for human resources financial management, routine administrative activities and for personnel management and control ship, appellant is involved along with its associated enterprises. It also undertakes the coding and documentation function with respect to the software modules that it develops however for this function it required receives technical assistance from its associated enterprises. However, the development of modules is with respect to the software for internal usage by the associated enterprises. The associated enterprises supervise and manage the coding and documentation for functions performed by the appellant. It also undertakes the design and development function pertaining to a particular module based on the specifications provided by associated enterprise where the ultimate responsibility for undertaking the coding and documentation function for the complete software product rests with its associated enterprises. It is the responsibility of the appellant for the quality of the work performed by it and it seeks to ensure that the work performed by it, complies with the quality standards set by the associated enterprises however ultimately the associated enterprises are responsible for the quality control and for the development of the common standards. In addition, for this purpose its associated enterprises conduct frequent quality audits of the activity performed by the appellant.

7. On the aspect of risk assumed the appellant, as it is a captive service provider, is assured of a specified return on its cost it does not assume any business risk, Capacity utilization risk,

- service liability risk and any credit and collection risk. With respect to the foreign exchange risk, it assumes minimum risk.
8. On the aspects of the assets deployed by the appellant for performance of services, it has normal assets which did not include any intangible. Intangibles used by the appellant are owned by associated enterprises.
  9. On proceedings before the Ld. Transfer pricing officer with respect to the software development services segment wherein appellant selected 21 comparables. Ld TPO rejected 12 comparables and further selected 4 comparables and therefore 9 comparables from the set of the comparable selected by the assessee and 4 comparables selected by the Ld. Transfer Pricing Officer out of the 13 comparables the average PLI of operating profit /operating cost was worked out that 24.683 % and applying the same Ld. TPO proposed adjustment under section 92CA of Rs. 28858130/.
  10. With respect to the ITES segment out of the 6 comparable selected by the appellant, Ld. TPO rejected 3 comparables and selected 4 comparables whose average PLI was determined at 26.714 % and an adjustment of Rs. 117968443/-was made.
  11. Further during the course of transfer pricing assessment proceedings be Ld. TPO came to know that there is a delay in the realization of dues of the various invoices raised by the appellant on its associated enterprises, therefore according to him the credit period is in the range of 60 to 90 days and no interest has been charged on the outstanding receivables. It was further found by him that even in the service agreement no standard credit period is mentioned. Based on this he calculated

interest after allowing the normal credit period of 30 days at Rs. 4813188/-.

12. In nutshell the Ld. TPO proposed an adjustment on account of the arm's length pricing of the international transactions with respect to the software development segment of Rs. 2885 8130/- , with respect to ITES segment Rs. 1179 8443/- and on account of interest on outstanding receivable of Rs. 48123188/-. Based on this the Ld. AO framed draft assessment order under section 143 (3) of the Income Tax Act which was challenged before the Ld. Dispute Resolution Panel (in short DRP). The ld. DRP issued direction under section 144C (5) of the Income Tax Act 1961 on 03/10/2013. The Ld. Dispute Resolution Panel in software development services directed Ld. TPO to exclude only one comparable that is Goldstone technologies Ltd. and to verify with respect to the other comparable Qunitegra solutions Ltd whether it crosses the export sales filter adopted by the Ld. TPO. Consequently, the Ld. DRP confirmed adjustment on account of provision of software development services of Rs. 21042855/- In the ITES segment the Ld. DRP directed Ld. TPO to include 2 comparables selected by the appellant and did not interfere with the other comparable as included by the Ld. TPO. Consequently Ld. DRP did not upheld any adjustment to the provision of ITES segment. On the issue of holding intercompany receivable to constitute an international transaction and benchmarking of the same by the application of the CUP method by the Ld. TPO and thereby proposing an adjustment on account of the overdue credit extended to the associated enterprises it also directed the actual amount of the receivable and to appropriately apply on the time basis prime lending rate of state bank of India. Therefore in

substance the Ld. DRP restricted that the adjustment under section 92CA of Rs. 21042855 /-.On receipt of the above direction the Ld. AO passed assessment order under section 143 (3) read with section 144 C of the Act on 30/12/2013. However while passing the assessment order the Ld. AO made the identical adjustment amounting to Rs. 21042855/- to the book profit calculated under section 115JB of the Act of Rs. 389097684/- and determining the adjusted book profit amounting to Rs. 410140539/-

13. Aggrieved by the order of the Ld. AO the appellant filed appeal before us raising 6 grounds of appeal. However, at the time of hearing the Ld. authorized representative submitted that ground No. 1; ground No. 2 except ground Nos. 2.9 to 2.11 is not pressed. Further ground No. 4 is with respect to the penalty proceedings initiated under section 271 (1) © of the income tax act and ground No. 5 is with respect to the charging of the interest and ground No. 6 is regarding various judicial pronouncement. Penalty and interest are consequential. In view of the above facts, we dismiss those grounds as stated above. Therefore only grounds to be adjudicated remain are ground no 2.9 to 2.11 and ground no 3.
14. We first take ground nos. 2.9 to 2.11 related to the adjustment on account of software development service segment. Ld. authorized representative submitted that the software development segment the comparables selected by the Ld. transfer pricing officer with respect to Infosys technologies Ltd, Bodhtree consulting Ltd & Sonata software Ltd are required to be excluded. For the arguments he submitted detailed note with respect to each of the comparables stating that they are

functionally not comparable, there is brand value involved in some of the comparables and some of the comparables are excludable on account of judicial pronouncements and filters. It was further submitted that if the above 3 comparables contested by the appellant are excluded the profit level indicator of the assessee falls within the +/-5% range. He further submitted that in some of the cases there is a computational error made by the Ld. Transfer pricing officer with respect to computing the margin of the comparables.

15. Ld. departmental representative submitted that in the comparables selected by Ld. transfer pricing officer by proper study of the functional analysis of those parties and he further relied on the order of the transfer-pricing officer and Ld. dispute resolution panel.
16. We have carefully considered the rival contentions and we discuss each of the comparables contested by appellant before us.

- a. Infosys Limited

- i. This comparable is contested by the appellant stating that it is engaged in providing development and maintenance of computer software. It also produces and sales software. It is further stated that there is no segmental data available and it is a very high turnover company compared to the appellant. He further stated that it has software engineer and technology labs for applied research in software engineering on enterprise technology. It spends on research and development its expenses are to the tune of Rs. 267 crores. Expenses amounting to Rs. 77 crores have been spent by this

company for brand building and marketing expenses. He further stated that this is a product development company, The Finncle software of the company is one of the prime products for the banking industry. On the basis of this, he stated that Hon'ble Delhi High Court in case of Agnity (India) technologies private limited has held that this company is not comparable with the company like appellant. He further relied on the several decision of the coordinate benches as well as the decision of the Hon'ble Delhi High Court in case of DCIT versus Fiserv India private limited where the Hon'ble high court has confirmed the order of the Delhi tribunal excluding the above comparable.

- ii. Ld. Transfer pricing officer has held it to be comparable and the learned DRP based on the annual report rejected the contention of the assessee on all the above counts.
- iii. We have carefully considered the rival contentions with respect to this comparable. The copies of the annual report of this comparable were provided by assessee at page No. 558 – 725 of the paper book for FY 2008 – 09. At page No. 580 in Para No. 4 of the director's report it is mentioned that 'Finacle' software is an integrated yet modular solution which addresses the core banking, Treasury, wealth management, Islamic banking, consumer and corporate banking, mobile banking and web-based cash management requirements of universal, retail and corporate banks worldwide. It is further mentioned that that this

software currently powers 114 banks across the 62 countries helping them serve more than 25,000 branches, 244 million customers, 297 million accounts and over 200000 current users. It is further mentioned that independent reports by renowned research firms have positioned this among the leaders in the global evaluation of retail core banking solution vendors. It has also emerged as one of the most scalable core banking solution in the world by achieving an unparalleled performance benchmarking of 104 million effective transactions per hour. Therefore, it is very apparent that it produces and sells software. At page No. 587 of the paper book shows that it spends 1.3% of its revenue on research and development expenditure and consequently it is incurred revenue expenditure of Rs 236 crores whereas capital expenditure of Rs. 31 crores on account of research and development expenditure. Further at page No. 615 of the paper book in the annual report of this company it is mentioned that it is spending Rs. 77 crores towards brand building & marketing expenditure. Coordinate bench in Fiserv ( India) private limited versus DCIT has held that a captive unit of a comparable company which assumes only a limited risk, cannot be compared with a giant company in area of development of software who assumes all types of risks leading to higher profits while dealing with Infosys Ltd as comparable. It held as under:-

*“INFOSYS LTD.:*

**“11.4** We have considered rival submissions, perused the material on the record. In the case of *Agnity Technologies (supra)* a coordinate Bench has held as under:—

"It is argued that the case of the assessee is not comparable with Infosys Technologies Ltd., the reason being that the latter is giant in the area of development of software and it assumes all risks, leading to higher profit. On the other hand, the assessee is a captive unit of its parent company in the USA and it assumes only limited Currency risk. Having considered these points, we are of the view that the case of aforesaid Infosys and the assessee are not comparable at all as seen from the financial data etc. of the two companies mentioned earlier in this order. Therefore, we are of the view that this case is required to be excluded"

**11.5** The aforesaid order was upheld by the Hon'ble Delhi High Court after taking note of the chart as given below:

Basic Particular	Infosys Technologies Ltd.	Assessee
Risk Profile	Operate as full-fledged risk taking entrepreneurs	Operate at minimal risks as the 100 percent services are provided to AEs
Nature of services	Diversified-consulting, application design, development, re-engineering and maintenance system integration, package evaluation and implementation and business process management, etc. (refer page 117 of the Paper Book)	Contract software development services
Turnover	20,264 crores	209.83 crores
Ownership branded/proprietary products	Develops/owns proprietary products like Finacle, Infosys Actice Desk, Infosys iProve, Infosys	

		mConnect. Also the company derives substantial portion of its proprietary products (including its flagship banking product suite 'Finacle')	
Onsite vs. Offshore		As much as half of the software development services rendered by Infosys are onsite (i.e. services performed at the customer's location overseas). And offshore (50.20 per cent) Refer p. 117 of the Paper Book) than half of its service, income from onsite services	The appellant provides only offshore services (i.e. remotely from India)
Expenditure on advertising/sales promotion and brand building	Rs. 80 crores		Rs. Nil (as the 1-percent services are provided to AEs)
Expenditure on Research and Development	Rs. 236 crores		Rs. Nil
Other			100 per cent offshore (from India)

**11.6** On the basis of the above chart, the Hon'ble High Court affirmed the conclusion that a captive unit of a comparable company which assumed only a limited risk, cannot be compared with a giant company in the area of development of software who assumes all types of risks leading to higher profits. The facts of the appellant are akin and therefore, do not warrant any different conclusion. The appellant is also captive service provider to its AE and as such, M/s. Infosys Ltd. is not a valid comparable with the appellant.”

The above decision of the coordinate bench has been affirmed by the Hon'ble Delhi high court in ITA No. 17/2016. The appellant in its software development activities performed development of modules as well as a part of modules for software being used by its overseas

group entities in their products whereas maintenance support services include bug fixing, carrying on maintenance and support services. Therefore it is a captive software developer, does not have any intangibles, and also do not incur any expenditure on research and development. Furthermore Hon'ble Delhi high court in [2013] 36 taxmann.com 289 (Delhi) Commissioner of Income-tax *v.* Agnity India Technologies (P.) Ltd. in case of software developer for a parent company has held that Infosys Ltd is not a comparable. Therefore respectfully following Hon'ble Delhi high court as well as comparisons of the functional profile of software development services of the appellant with the Infosys Ltd we hold that it is not at all comparable hence we direct exclusion of this comparable for making comparability analysis in software development services segment of the appellant.

**b. Bodhtree Consulting limited**

- i. The appellant submitted that this comparable is engaged in the software development products and also engaged in providing (and 2 and web solutions software consultancy and designing and development of software using latest technology. He further submitted that it provides cloud services, analytics, digital customization and enterprise services. He further submitted that it has fluctuating margins. In view of this he submitted that the above comparable requires to be excluded.
- ii. Ld. TPO as well as the Ld DRP rejected the contention of the assessee stating that it is the perfect comparable for software development services segment of the assessee.
- iii. We have carefully considered the rival contentions . Appellant has placed the annual accounts of the above company at page No. 482 to 557 of the paper book submitted. At page No. 496 of the annual report it is Annexure III to the director's report it says that it is engaged in the business of off shoring data management, data warehousing, software consultancy, design and development of solutions using the latest technologies. The

coordinate bench in case of Fiserve ( Supra) held that a software development services provider has held that the above comparable is engaging the software product development services and therefore same cannot be compared with the software development service provider as under:

*“10.5 Having considered rival submissions, we find that the issue regarding the exclusion of the instant comparable stands examined by a coordinate bench of this Tribunal in the case of M/s. Softek India (P.) Ltd. (supra) for assessment year 2009-10 wherein in an order dated 31.10.2014 it was held as under:*

*"4.3 Having regard to the contentions of the rival parties and also the material on record, we find that the assessee is only a software services company whereas M/s. Bodhtree Consulting Ltd. is also into the business of software product development and segmented data is not available in the public domain. Therefore, we are satisfied that it is functionally different and cannot be considered as a comparable to the assessee-company. As regards revenue recognition model of the assessee and M/s. Bodhtree Consulting Ltd., are concerned, since the relevant material to determine the revenue model of the assessee herein is not available on record, we are not inclined to give any finding on this issue. Therefore, we direct the AO to exclude M/s. Bodhtree Consulting Ltd., from the list of comparables as it is functionally different."*

**10.6** Also another coordinate bench in the case of Cisco Systems (India) (P.) Ltd. v. Dy. CIT [2014] 66 SOT 82/50 [taxmann.com](http://taxmann.com) 280 (Bang.) has held as under:

*"26.1 Bodhtree Consulting Ltd.:- As far as this company is concerned, it is not in dispute that in the*

*list of comparables chosen by the assessee, this company was also included by the assessee. The assessee, however, submits before us that later on it came to the assessee's notice that this company is not being considered as a comparable company in the case of companies rendering software development services. In this regard, the ld. counsel for the assessee has brought to our notice the decision of the Mumbai Bench of the Tribunal in the case of Nethawk Networks (P.) Ltd. v. ITO [2014] 41 taxmann.com 250 (Mum. - Trib.). In this case, the Tribunal followed the decision rendered by the Mumbai Bench of the Tribunal in the case of Wills Processing Services (I) P. Ltd. v. Dy. CIT IT Appeal No.4547/Mum/2012, dated 13-11-2013. In the aforesaid decisions, the Tribunal has taken the view that Bodhtree Consulting Ltd. is in the business of software products and was engaged in providing open & end to end web solutions software consultancy and design & development of software using latest technology. The decision rendered by the Mumbai Bench of the Tribunal in the case of Nethawk Networks (P.) Ltd. (supra) is in relation to A.Y. 2008-09. It was affirmed by the learned counsel for the Assessee that the facts and circumstances in the present year also remains identical to the facts and circumstances as it prevailed in AY 08-09 as far as this comparable company is concerned. Following the aforesaid decision of the Mumbai Bench of the Tribunal, we hold that Bodhtree Consulting Ltd. cannot be regarded as a comparable. In this regards, the fact that the assessee had itself proposed this company as comparable, in our opinion, should not be the*

basis on which the said company should be retained as a comparable, when factually it is shown that the said company is a software product company and not a software development services company."

**10.7** Having considered the above, we hold that since the assessee company is engaged in software development services; whereas M/s. Bodhtree Consulting Ltd. was engaged into software product development, we find force in the argument of the ld counsel for the assessee that M/s. Bodhtree Consulting Ltd. is functionally different from assessee company."

Hon'ble Delhi high court in ITA No. 17/2016 has affirmed the finding of the coordinate bench. Therefore respectfully following the decision of the Hon'ble Delhi high court we also direct that comparable companies engaged in the business of software product development and not software development services and therefore it is not comparable with the appellant hence it is directed to be excluded.

c. Sonata Software Limited

- i. For this comparable appellant has submitted that the it is providing software services such as IT consulting and remote infrastructure management and provides offshore development services. According to the Ld. authorized representative it fails the related party transactions filter of 25% on sales which is adopted by the Ld. TPO and therefore on that ground it should have been rejected in 'accept reject matrix' of the transfer pricing comparability analysis itself. He further stated that the comparable company is performing significant research and development functions unlike a software development company like appellant. He relied on the decision of the coordinate bench in Fiserve V ITO in ITA No. 1822/del/2014 where Sonata has been rejected by the tribunal on failing related party

transactions filter of 25% for assessment year 2009 2010. He further submitted that that the above decision has been affirmed by the Hon'ble Delhi high court in ITA No. 17/2016 . He further submitted a chart wherein he demonstrated that the related party transactions to sales in case of the above comparable is 49.37% and therefore it should be excluded on this count.

- ii. Ld. Transfer pricing officer as well as Ld. Dispute resolution panel rejected the contention of the appellant and held that Sonata software is a good comparable.
- iii. We have carefully considered the rival contentions. Assessee has submitted the annual accounts of Sonata software Limited for FY 2008 – 09 at pages No. 726 to 829 of the paper book. We have also carefully perused the decision of the coordinate bench in case of Fiserv (India) private Ltd versus Income Tax officer in ITA No. 1822/del/2014 wherein this comparable was considered and was excluded on the basis of not passing the RPT filter for the same year as under:-

*“SONATA SOFTWARE:*

**13.** The assessee's objection to include this company was dealt by the TPO as under:—

"Assessee objected on the use of this comparable on the ground that this comparable fails RPT filter since it is having RPT/sale of >10% and calculated the RPT of 16.20. It has also referred to investment in setting up a company in Dubai which has been taken as an extraordinary event.

TPO's remarks:

The RPT filter has been discussed in the preceding paras. As far investment in the company in Dubai is concerned, the assessee has not demonstrated how this even has affected the profitability of the company. Hence the objection is rejected."

**13.1** The assessee's challenge before the DRP was dealt as under the DRP:

"The annual report is verified and it is observed that as per P&L of annual report:

"Income service 2,43,57,68,787/- Other Income 1,05,30,957

It can be seen from the above, main income is from software development. Therefore the company is includible so far as its functionality is concerned

However, as per annual report of the company RPT of this company is 14.65% and is within the overall limit of 25%. As per the taxpayer's argument of taking the receivable into the calculation of RPT, it is seen that it is balance sheet item. The sonata Software limited has 4 related parties it is seen that the service charge credited in the P&L account of Sonata Software Ltd. is Rs. 243.57 crores. The only related party with which this comparable is having transaction in services is Sonata Information Technology Limited (SITL) amounting to Rs. 16.11 crores which is around 6.61% of the total service income. Similarly, the other

debit items of the profit and loss account like deputation expenses, travelling expenses, other expenses and reimbursement of expenses have been considered as the part of RPT. The other items like interest, though a P&L account item has not been considered as this is non operational. On the contrary balance sheet items like assets, loans, deposits whether receivables or payables have been excluded from the calculation of RPT. This approach of the TPO was well justified in view of the accounting norms. Therefore, the taxpayer's contention to exclude Sonata Software Ltd. is rejected."

**13.2** The Id. counsel submitted that M/s Sonata Software majorly deals into product, sale, offshore development services and significant related party transactions. The company is also engaged in research and development. It was submitted as under:

"As per segmental results of Sonata Software, the company deals in software products (tab 6 of Vol 4)

Extraordinary events: During the relevant previous year, it is also set up a new subsidiary in Dubai which acquired major business in Dubai (Tab 6 of Vol 4)

Refer *Capital IQ v. DCIT: Capital IQ v. DCIT* wherein it is held that extraordinary events will have impact on profitability.

Failure of RPT filter: Even otherwise, it can be seen that its related party transaction exceeds 25% of the revenues, which makes it an unviable comparable. It is seen from the annual report that the RPT to sales ratio is more than 40% during the relevant previous year. Therefore, it fails the 25% filter applied by the TPO."

**13.3** Having considered the rival submissions, we find that in the instant case, aggregate related party transactions are roughly around 95 crores which is approximately about 40% of the total service income of Rs. 243.57 crores. As such, the said comparable is not a valid comparable and hence is directed to be excluded as it fails the RTP filter of 25% applied by the TPO

Hon'ble Delhi high court has affirmed the above decision in ITA No. 17/2016. Therefore respectfully following the decision of the coordinate coordinate bench we also direct for exclusion of Sonata software as a comparable as it exceeds the RPT filter of 25%.

17. It was further one of the contentions of the Ld. authorized representative that in case of 4 comparables the Ld. Transfer pricing officer has computed margin which included foreign exchange gain as operating income/ loss and also non-allocation of certain expenditure or income to the relevant segment. In one of the comparable the other income is considered as an operating income by the Ld. Transfer pricing officer.
18. We have carefully considered the rival contentions. Incorrectly taken by the Ld. assessing officer with respect to Kals Information Systems Ltd, Comp U earn India Limited and LGS global Ltd. However before us the annual accounts of those companies are not available and as it is a matter of calculation and to decide whether the foreign exchange gain or loss is required to be excluded or not therefore we set aside this issue to the file of the Ld. Transfer Pricing officer considered the argument of the assessee and Agilent Technologies ( International ) Private Limited V ACIT ITA No 1255/Del/2014 AY 2009-10

then decide the issues concerning the computation of margin of the comparables.

19. The next issue involved in this appeal is that the Ld. assessing officer made an adjustment to the book profit computed under section 115 JB of the Income Tax Act by increasing the transfer pricing adjustment made by the learned transfer-pricing officer. In the draft assessment order passed on 28<sup>th</sup> of February 2013 the Ld. assessing officer did not compute book profit under section hundred and 15 JB of the income tax act. Therefore there was no ground with respect to this before the Ld. dispute resolution panel. However when the final order under section 143 (3) of the income tax act was passed on 30/12/2013 the Ld. assessing officer increased the book profit under section 115 JB of the act of Rs. 389097684/- by a sum of Rs. 21042855/- which is an adjustment upheld by the Ld. DRP. Therefore by ground No. 3 the appellant has stated that Ld. assessing officer has grossly erred on facts and in law by computing book profit after adding transfer pricing adjustment made under the normal provisions of the act.
20. Ld. authorized representative submitted before us that section 115 JB of the income tax is a complete code in itself. The various editions to be made to the book profits are mentioned in various clauses of the explanation to that section. Such kind of adjustment is not mentioned there with respect to the transfer pricing additions to the income of the assessee in normal computation of total income. Therefore he submitted that no such addition can be made on account of transfer pricing adjustment to the book profit of the assessee under section 115 JB of the income tax act. He further stated that the Ld. assessing officer has not mentioned any of the clauses of the explanation under which he is making such an adjustment. He further submitted that Hon'ble Supreme Court in case of Apollo tyres Ltd versus Commissioner of income tax 255 ITR 273 has held that addition or deletions to book profit under section 115 JB of the income tax act shall be restricted to those specified under explanation 1 to that section and the assessing officer is not authorized to make additions beyond those as mentioned in the said explanation. He further stated that that identical issue has been dealt with by Delhi tribunal in M/s cash edge India private limited in ITA No. 64/del/2015 . In view of this he submitted that the addition made by

the Ld. assessing officer to the book profit under section 125 JB of the income tax act is erroneous.

21. The Ld. departmental representative fairly conceded that there is no such adjustment provided under the explanation 1 to section 115 JB of the income tax act however when there is an addition to the normal income of the assessee similar kind of addition may be made while calculating the book profit tax.
22. We have carefully considered the rival contentions and also perused the arguments placed before us in the form of the decision of the coordinate bench in case of M/s cash edge India private limited wherein identical issue has been considered as under:-

*“ADDITION OF TRANSFER PRICING ADJUSTMENT TO MAT*

*33. The final issue for consideration is challenge raised by the assessee to the action of the AO in adding back transfer pricing adjustment of Rs.1,18,93,468/- to income assessed under Section 115JB (MAT).*

*34. In this regard, the learned counsel for the assessee submitted that the AO has added the transfer pricing adjustment of Rs.1,18,93,468/- to the book profits of the Assessee under Section 115JB of the Act without appreciating that book profits of the company cannot be adjusted except as provided in Explanation 1 Section 115JB(2) of the Act and that transfer pricing adjustment is not one of the adjustments contemplated under that Explanation. He placed reliance upon the following decisions to contend that except for adjustments provided in Explanation 1 Section ITA No.64/Del./2015 115JB(2) of the Act, no other adjustment can be made to book profits under Section of the Act :-*

*i. Apollo Tyres: 255 ITR 273(SC) ii. Malayalam Manorma: 300 ITR 251(SC), iii. HCL Comnet Systems and Services Ltd., 305 ITR 409 (SC) and iv. DCIT v. Bisleri Sales Ltd.: 151 TITJ 285 (Mum)(ITAT)*

*35. The Ld. Sr. DR on the other hand supported the order of the AO on the strength of the decision of the Special Bench of the Tribunal in the case of Rain Commodities v. DCIT: (2010) 40 SOT 265.*

*36. We have considered the rival submissions and perused the material on record. It is settled law that except for adjustments provided in Explanation 1 Section 115JB(2) of the Act, no other adjustment can be made to book profits under Section 115JB of the Act. We find that that transfer pricing adjustment is not one of the adjustments contemplated under Explanation 1 Section 115JB(2) of the Act and, therefore, could not have been added back to the book profits under Section 115JB.*

*ITA No.64/Del./2015*

*37. The case-law relied upon by the Ld. Sr. DR i.e. decision of the Special Bench in the case of the Tribunal in Rain Commodities (supra) does not also advance the case of the Revenue. In that case the Special Bench was considering whether the AO can alter the net profits declared by an assessee. The Special Bench has, following the decision the apex Court in Apollo Tyres and HCL Comnet (supra), inter alia, held that the AO cannot travel beyond the net profits declared by the assessee unless*

*(a) it is discovered that profit and loss account is not drawn up in accordance with Part II and Part III of Schedule VI of the Companies Act, or (b) the incorrect accounting policies, accounting standards have been adopted for preparing such accounts and the method/rate of depreciation has been incorrectly adopted for preparation of profit and loss account.*

*38. In the present case there is no allegation is the assessment order much less any finding that either that profit and loss account has not been drawn up in accordance with Part II and Part III of Schedule VI of ITA No.64/Del./2015 the Companies Act, or that any incorrect accounting policies, accounting standards has been adopted for preparing such accounts or that the method/rate of depreciation has been incorrectly adopted for preparation of profit and loss account.*

*39. In view of aforesaid, we hold that the AO erred in adding back the transfer pricing adjustment of the book profits under Section 115JB of the Act. Accordingly, this ground of the appeal raised by the assessee is allowed and the AO is directed to exclude the transfer pricing adjustment, if such adjustment survives, from the book profits computed under Section 115JB of the Act.”*

23. Therefore respectfully following the decision of the coordinate bench on identical issue we hold that the Ld. assessing officer has erred in making an addition to the book profit computed under section 115 JB of the income

tax act by adjustment made by ld. Transfer Pricing Officer on account of arms length price. In the result ground No. 3 of the appeal of the assessee is allowed.

24. In the result appeal of assessee is partly allowed.

Order pronounced in the open court on 29/09/2016.

**-Sd/-**

**(DIVA SINGH)  
JUDICIAL MEMBER**

**-Sd/-**

**(PRASHANT MAHARISHI)  
ACCOUNTANT MEMBER**

Dated: 29/09/2016  
A K Keot

Copy forwarded to

1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR  
ITAT, New Delhi