

**IN THE INCOME TAX APPELLATE TRIBUNAL  
BANGALORE BENCH ' B '**

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

I.T. (T.P) A. No.1320/Bang/2011  
(Assessment Year : 2007-08)

M/s. Northern Operating Services Pvt. Ltd.,  
2<sup>nd</sup> Floor, RMZ Ecospace, Campus IC,  
Sarjapur ORR, Bellandur Vill.,  
Varthur Hobli, Bangalore-560 037.

.... Appellant.

Vs.

Dy. Commissioner of Income Tax,  
Circle 12(2), Bangalore.

..... Respondent.

Appellant By : Shri Ujjwal Tewari, C.A.

Respondent By : Ms. Neera Malhotra, CIT (D.R)

Date of Hearing : 26.10.2016.

Date of Pronouncement : 26.10.2016.

**ORDER**

**Per Shri Vijay Pal Rao, J.M. :**

This appeal by the assessee is directed against the assessment order dt.11.10.2016 passed under Section 143(3) r.w.s. 144C of the Income Tax Act, 1961 (in short 'the Act') in pursuant to the directions of

the Dispute Resolution Panel (in short 'DRP') dt.23.9.2011 for the Assessment Year 2007-08.

2. The assessee has raised the following grounds :

**I. Transfer Pricing**

- 1 The learned Assessing Officer ('Assessing Officer' or 'AO') and the learned Additional Commissioner of Income Tax (Transfer Pricing - II), Bangalore ('Transfer Pricing Officer' or 'TPO') grossly erred in law and facts of the case in determining the Arm's Length Price (hereinafter referred to as 'ALP') of the international transaction of the appellant of ` 364,172,882 received on account of provision of Information Technology Enabled services and proposing a transfer pricing adjustment of ` 56,395,535.
- 2 That on the facts and circumstances of the case, the learned Assessing Officer and the learned TPO erred in rejecting the Transfer Pricing (hereinafter referred to as 'TP') documentation without appreciating the contentions, arguments, and evidentiary data put forward by the Appellant during the course of the proceedings before them, and in doing so have grossly erred:
  - 2.1 in rejecting the comparability analysis carried out in the TP documentation and performing a fresh comparability analysis for determining the ALP by the learned TPO;
  - 2.2 in adopting the arm's length mark up to be 27.69% in respect of the international transaction pertaining to the rendering of Information Technology Enabled Services by the Appellant;
  - 2.3 in completely relying on the unaudited data requisitioned and consequently obtained by taking recourse to the provisions of Section 133(6) of the Income-tax Act, 1961 (hereinafter referred to as 'the Act'), which in many instances are inconsistent with the data disclosed in audited reports;
  - 2.4 in considering 25 percent as the threshold limit for the Related Party Transactions filter as this number is an arbitrary number that has been adopted without any judicial precedence or reasonable basis;
  - 2.5 in not maintaining consistency in applying the filters of rejecting companies with export earnings less than 25% of the total revenue and companies of different year end;

- 2.6 in not employing the filter of rejecting companies where the employee costs were lesser than 25% of the revenues derived from rendering Information Technology Enabled Services;
  - 2.7 in accepting companies like Infosys BPO and Wipro Limited as comparable companies even though the sales of Infosys and Wipro are driven based on brand developed by them, and in doing so the learned TPO and the learned AO has incorrectly interpreted the adjudication of the Delhi Income Tax Appellate Tribunal (ITAT) ruling in Agnity India Technologies India Pvt. Ltd. (reference: ITA No. 3856(Del)/2010);
  - 2.8 in accepting companies engaged in the provision of software development services, KPO services and other non-Information Technology Enabled services, such as Bodhtree Consulting Limited, e-Clerx Services Limited, ICRA Techno Analytics Limited, Mold-Tek Technologies Limited, and Spanco Limited, which are functionally not comparable to the appellant's business;
  - 2.9 in accepting Vishal Information Technologies Limited, in spite of the fact that 76% of the total operating costs incurred by the company represent data entry charges and vendor payments. The learned TPO further erred in not appreciating the fact that the Company seems to have outsourced the Information Technology Enabled Services to a third party vendor and hence is not comparable to the appellant;
  - 2.10 in accepting companies like Accentia Technologies Limited, e-Clerx Services Limited, HCL Comnet Systems and Services Limited, I-Services India Private Limited, Mold-Tek Technologies Limited, Accurate Data Converters Limited, which have abnormal/fluctuating profit margins. In doing so the learned AO has disregarded the various jurisdictional ITAT rulings in case of SAP LABS India Pvt. Ltd. Vs. ACIT (reference ITANo. 398/Bang/2008), E-Gain Communication Private Limited (reference: ITA No. 1685/PN/07 - Pune);
  - 2.11 in accepting a companies like Bodhtree Consulting Limited and Maple e Solutions Limited without taking into consideration the peculiar economic circumstances surrounding their operations during the year under review;
  - 2.12 in accepting Asit C Mehta as a comparable company having an employee costs lesser than 25% of total sales and also possessing intangible assets;
  - 2.13 in accepting companies having Related Party Transactions exceeding 10% such as Caliber Point Business Solutions Limited, Asit C Mehta Financial Services, Apollo Health Street Limited, Allsec Technologies Limited, HCL Comnet Systems and Services Limited, Informed Technologies India Limited, and R-Systems International Limited; and
  - 2.14 in not accepting Cameo Corporate Services Limited even though the company is functionally comparable with the Appellant.
- 3 That the learned AO and the learned TPO erred in disregarding the use of multiple year data and ought to have accepted the use of contemporaneous data

as per the transfer pricing regulations due to non-availability of current year data in the public domain at the time of preparing the documentation.

- 4 That the learned AO and the learned TPO erred in disregarding the fact that the Appellant has not claimed a deduction or tax benefits under section 10 A of the Act and has not shifted profits. Therefore the adjustment proposed is not called for and is hence misplaced.
- 5 That the learned AO and the learned TPO erred in concluding that the Appellant is exposed to single customer risk without evaluating the business arrangement of the Appellant.
- 6 That the learned AO and the learned TPO erred in not allowing the benefits of market risk adjustment to the Appellant.
- 7 That the learned AO and the learned TPO erred in not allowing the benefit of range of +/- 5% as provided in proviso to Section 92C(2) of the Act to the Appellant, while determining the arm's length price.

## **II. Computation of deduction under section 10A of the Act**

- 1 Reduction of data connection charges incurred in foreign currency from the export turnover
  - The learned AO erred in reducing the amount of data communication charges, amounting to `18,063,776, from the export turnover while computing the deduction under section 10A of the Act on the contention that these expenses are attributable towards providing technical services outside India.
  - The learned AO erred in disregarding the submission made by the Appellant that no part of these data connection expenses was incurred towards providing technical services outside India.
  - Without prejudice to the above, the learned AO erred in reducing sum of `18,063,776 towards data communication charges only from export turnover without reducing the same from total turnover in computing deduction under section 10A of the Act.
- 2 Reduction of travel and conveyance expenses incurred in foreign currency from the export turnover
  - The learned AO erred in reducing travel and conveyance expenses incurred in foreign currency amounting to `3,891,984 from the export turnover for the purposes of computing deduction under section 10 A.

- The learned AO erred in disregarding the submission made by the Appellant that no part of the travel expenses incurred in foreign currency was incurred towards providing technical services outside India and hence, the same should not be reduced from the export turnover of the Company.
- Without prejudice to the above, the learned AO erred in reducing sums of `3,891,984 towards travel and conveyance expenses only from export turnover without reducing the same from total turnover in computing deduction under section 10A of the Act.

3 Reduction of lease line expenses from the export turnover

- The learned AO erred in reducing lease line expenses debited to profit and loss account amounting to `295,041 from the export turnover for the purposes of computing deduction under section 10 A.
- The learned AO erred in disregarding the submission made by the Appellant that no part of the lease line expenses are attributable to delivery of software and services outside India and hence, the same should not be reduced from the export turnover of the Company.
- Without prejudice to the above, the learned AO erred in reducing sums of `295,041 towards lease line expenses only from export turnover without reducing the same from total turnover in computing deduction under section 10A of the Act.

4 The Appellant places reliance on the recent decision of the Honourable Karnataka High Court in the case of Tata Elxsi Ltd. and others wherein it has been held that if any expenses are to be reduced from the export turnover then correspondingly such expenses should also be reduced from the total turnover. The Honourable High Court observed that:

- Total turnover consists of export turnover and the turnover from the local sales. Export turnover constituted the numerator of the formula provided under section 10A of the Act and it also forms a constitute element of the denominator in as much as the export turnover is a part of the total turnover. Accordingly, if an amount is reduced from the export turnover, the same has to be reduced from the element of export turnover present in the total turnover. In this context, the High Court placed reliance on CIT vs. Gem Plus Jewellery India Ltd. (2011) (330 ITR 175) (Bombay HC).
- Further, High Court observed that, on the basis of principle of parity, there should be uniformity in the ingredients of both the numerator and the denominator of the formula, otherwise it would result in absurdity. It stated

that though there is no definition of the term “total turnover” in section 10A of the Act, there is nothing in the said section to mandate that, what is excluded from the numerator would nevertheless form part of the denominator. The High Court placed reliance on the judgments in the case of ITO vs. Sak Soft Ltd. (2009) (313 ITR 353) (Chennai ITAT, CIT vs. Lakshmi Machine Works (2007) (290 ITR 667) (Bangalore ITAT) (affirmed in the case of CIT vs. Catapharma (India) P. Ltd. (2007) (292 ITR 641) (SC))

### **III. Non consideration of credit of tax deducted at source**

The learned AO erred in not giving total credit of tax deducted at source amounting to `1,041,110.

### **IV. Levy of interest**

The learned Assessing Officer is not justified in levying interest amounting to `10,968,169 under section 234B of the Act. Levy of interest under section 234B is consequential in nature.

The Appellant craves to leave/ to add to / to alter/ to amend/ to rescind/ to modify the grounds herein above or produce further documents, facts and evidence before or at the time of hearing this appeal.

3. At the time of hearing, the learned Authorised Representative of the assessee has stated at Bar that the parties have mutually agreed for application of MAP pursuant to the Indo-US DTAA in respect of the adjustment made in the case of the assessee under Transfer Pricing provisions. The assessee has also filed a letter dt.14.7.2016 wherein the assessee has stated that it has accepted the terms mutually agreed between the competent authorities of India and US and accordingly Asst. Commissioner of Income Tax has passed the order giving effect as per

the terms mutually agreed in MAP Resolution. Thus the assessee has prayed that in lieu of the MAP Resolution the assessee withdraw the grounds pertaining to TP Matter. The Id. DR has not disputed the MAP Resolution in respect of the TP dispute. In view of the facts that the parties have resolved the dispute under MAP and consequently giving effect order has been passed on 12.7.2016, the Ground Nos.1 to 7 of the assessee's appeal are dismissed being withdrawn as a result of MAP Resolution.

4. The next ground is regarding reduction of expenses incurred in foreign currency from export turnover while computing the deduction under Section 10A of the Act.

4.1 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".*

In the light of the above binding precedents, we direct 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.

5. The next ground is regarding non-grant of credit of Tax Deducted at Source (TDS).

6. We have heard the learned A.R. as well as learned D.R. and considered the relevant material on record. The learned Authorised Representative has pointed out that the Assessing Officer has not granted total credit of TDS amounting to Rs.10,41,110. Thus he has

pleaded that the Assessing Officer may be directed to grant the full credit of TDS.

7. On the other hand, the Id. DR has submitted that this is a matter of verification and therefore without verification of fact the claim of the assessee cannot be accepted. Accordingly, we direct the Assessing Officer to verify the correct credit to be allowed to the assessee on account of TDS and then allow the same.

8. The next ground is regarding levy of interest under Section 234B of the Act which is consequential in nature.

9. In the result, the appeal of the assessee is partly allowed.

Order pronounced in the open court on the 26th day of Oct., 2016.

Sd/-  
**(INTURI RAMA RAO)**  
Accountant Member

Sd/-  
**(VIJAY PAL RAO)**  
Judicial Member

Bangalore,  
Dt. 26.10.2016.

\*Reddy gp

Copy to :

1. Appellant
2. Respondent
3. C.I.T.
4. CIT(A)
5. DR, ITAT, Bangalore.
6. Guard File.

By Order

Asst. Registrar, ITAT, Bangalore