

**IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCHES : “B”, BANGALORE**

**BEFORE SHRI N.V.VASUDEVAN, VICE PRESIDENT
AND
SHRI B.R.BASKARAN, ACCOUNTANT MEMBER**

**IT(TP)A No.307(Bang)/2015
(Assessment Year : 2010-11)**

M/s Akamai Technologies India Pvt.Ltd.,
Salarpuria Softzone, 2nd & 3rd Floor, A Wing, Survey No.80/1,
Bellandur Village, Outer Ring Rod, Bangalore-560 103
PAN No.**AAICS 0905J**

Appellant

Vs

The Deputy Commissioner of Income Tax,
Circle-1(1)(1), Bangalore.

Respondent

**IT(TP)A No.200(Bang)/2015
(Assessment Year : 2010-11)
BY DEPARTMENT**

&

**CO No.100/Bang/2015 [in IT(TP)A 200(Bang)2015]
(Assessment Year : 2010-11)
BY ASSESSEE**

**Assessee by : Shri Suryanarayana, Advocate
Revenue by : Shri Muzaffar Hussain, CIT-DR**

Date of hearing : 23-07-2020

Date of pronouncement : 29-07-2020

ORDER

PER N.V.VASUDEVAN, VICE PRESIDENT

IT(TP)A No.307(B)/2015 is an appeal by the Assessee while IT(TP)A No.200(B)/2015 is an appeal by the Revenue. Both these appeals are directed against the final order of assessment dated 30-12-2014 of the DCIT, Circle-1(10(1), Bangalore passed u/s 143(3) r.w.s.144C of the IT Act, 1961 (Act) in relation to AY: 2009-10. The Assessee has also filed Cross Objection in the appeal filed by the revenue. The Cross Objection filed by the Assessee is in support of the order of the CIT(A) and therefore, needs no separate adjudication.

2. The issues that arise for consideration in the cross-appeals and cross-objections pertains to :

- (a) Transfer pricing adjustment ('TP adjustment') of **Rs. 5,62,77,751/-** made by the Transfer Pricing Officer ('the TPO' for short) towards the international transaction of provision of Information Technology Enabled Services ('ITES') to the Appellant's Associated Enterprise ('AE'), which was subsequently enhanced to **Rs. 6,07,73,624/-** in the final assessment order passed by the Assessing Officer ("AO") under Section 143(3) read with Section 144C of the Income-tax Act, 1961 ("the Act");
- (b) Re-computation of deduction claimed under Section 10A of the Act;
- (c) Non-grant of credit of entire TDS deducted on the basis of Form 16A and consequent erroneous levy of interest under Sections 234B and C of the Act; and
- (d) Non-grant of interest under Section 244A of the Act.

3. As far as the issue with regard to Transfer Pricing Adjustment and consequent addition to the total income in respect of an international transaction between the Assessee and its Associate Enterprise is concerned, the facts and circumstances under which the said issue arises for consideration are that the Assessee is a company incorporated under the provisions of the Companies Act, 1956 and is a wholly owned subsidiary of Akamai US. The Assessee is engaged *inter alia* in providing back-office support services (in the nature of ITES) and software development services to Akamai US. During the previous year relevant to the assessment year 2010-11, the relevant international transaction that took place between Akamai US and the Assessee was the provision of back-office support services (in the nature of ITES) to Akamai US at a price of Rs. 61,35,54,428/-. The transaction of rendering ITES to holding company was a transaction with an Associated Enterprise (AE) and was

therefore an international transaction. As per the provisions of Sec.92 of the Act, income from international transaction has to be computed having regard to Arm's Length Price (ALP).

4. On a reference made by the AO, the Transfer Pricing Officer (TPO) passed an order dated 27.1.2014 under Section 92CA of the Act. It is not in dispute between the Assessee and the revenue that the Transaction Net Margin Method (TNMM) was the Most Appropriate Method (MAM) for determination of ALP and that the profit level indicator to be adopted for comparison of the Assessee's profit with that of comparable companies was Operating Profit/Operating Cost (OP/OC). The OP/OC of the Assessee was 16%, which was computed as follows:

Net margin on cost earned by the Assessee :

Operating Income (excluding foreign exchange gain)	Rs.61,35,54,428/-
Operating Cost	Rs.52,89,26,231/-
Operating Profit (Op. Income – Op. Cost)	Rs.8,46,28,197/-
Operating/Net margin (OP/TC)	16.00%

5. The Assessee in it's Transfer Pricing Study (TP study) selected 9 comparable companies whose arithmetic mean of OP/TC was arrived at 18.53%. Since the profit margin of the Assessee was within the permitted (+/-) percentage in terms of provisio to Sec.92C(2) of the Act, the Assessee claimed that the price charged by it in the international transaction was at Arm's Length. The Transfer Pricing Officer (TPO) to whom the determination of ALP was referred by the AO, accepted 4 out of the 9 comparable companies suggested in the TP study by the Assessee as comparable with the Assessee.

6. The TPO on his own selected 6 other companies as comparable companies with the Assessee. Thus a final set of 10 comparable companies was chosen by the TPO as comparable companies. The

arithmetic mean of profit margin of these companies after and before adjustment towards working capital adjustment was as follows:

Comparables selected by TPO and their arithmetic mean:

Sl. No.	Name of the Company	Mark-up on Total Costs (WC– unadj) (in %)	Mark-up on Total Costs (WC – adj) (in %)
1.	Accentia Technologies Ltd.	43.06	39.17
2.	Acropetal Technologies Ltd. (Seg)	22.27	17.67
3.	E-Clerx Services Ltd.	55.97	52.98
4.	Fortune Infotech Ltd.	22.80	20.05
5.	ICRA Online Ltd. (Seg)	43.39	40.72
6.	Informed Technologies India Ltd.	26.15	25.94
7.	Infosys BPO	31.23	28.68
8.	Cosmic Global Ltd.	14.97	16.20
9.	Sundaram Business Services Ltd.	-12.31	-13.28
10.	Jeevan Scientific Technology Ltd. (Seg)	21.05	37.99
Average		26.86	26.61

7. The Computation of arm's length price by the TPO and the adjustment made (as per the order dated 27.01.2014):

Arm's Length Mean Margin	26.87%
Less: Working Capital Adjustment*	0.23%
Adjusted mean margin of the comparables	26.64%

Operating Cost	Rs.52,89,26,231/-
Arm's Length Price - 126.64% of Operating Cost	Rs.61,35,54,428/-
Price Received	Rs.20,61,11,246/-
Short fall being adjustment u/S. 92CA	Rs.40,74,43,182/-

It may be clarified that the TPO restricted the working capital adjustment at 0.23% though the actual working of working capital adjustment was much higher than 0.23%. If the actual working capital adjustment as computed by the TPO had been allowed then the adjusted mean profit margin of comparable companies for the purpose of comparison with the Assessee's margin would be less than 26.64% computed by the TPO.

8. The Assessee filed application for rectification of certain apparent errors in the order of the TPO in computing the adjustment u/s.92CA of the Act. The TPO passed a rectification order dated 10.2.2014 whereby he computed the adjustment u/s.92CA and consequent addition to the total income at a sum of Rs.5,62,77,751/-, as follows:

Adjustment computed as per the rectification order dated 10.02.2014:

Arm's Length Mean Margin	26.87%
Less: Working Capital Adjustment	0.23%
Adjusted mean margin of the comparables	26.64%
Operating Cost	Rs.52,89,26,231/-
Arm's Length Price - 126.64% of Operating Cost	Rs.66,98,32,179/-
Price Received	Rs.61,35,54,428/-
Short fall being adjustment u/S. 92CA	Rs.5,62,77,751/-

9. Aggrieved by the addition to the total income by the AO in the draft order of Assessment, as was suggested by the TPO, the Assessee filed objections before the Dispute Resolution Panel (DRP) u/s.144C of the Act. The DRP issued directions to the AO to exclude Acropetal Technologies Ltd., E-Clerx Services Ltd., ICRA Online Ltd., and Infosys BPO Ltd., from the list of final comparable companies chosen by the TPO. The DRP also

suo moto directed the exclusion of Sundaram Business Services Ltd., from the list of final comparable companies chosen by the TPO. The DRP did not accept the contention of the Assessee with respect to the exclusion of Accentia Technologies Ltd. The DRP accepted the contentions of the Assessee and directed the AO to treat the gains/loss arising from fluctuation of foreign currency as operating in nature and consequently directed the same to be taken into consideration while computing the margins of the Assessee and comparable companies. The DRP accepted the contentions of the Assessee and directed the AO to recompute the margins of the comparable companies by granting the working capital adjustment on actual basis without any restriction. The DRP also, directed the AO to recompute the margins after rectifying defects pointed out by the Assessee in the computation of some of the comparable companies.

10. It is the plea of the Assessee that as per the directions of the DRP, the TP adjustment ought to be deleted but in the order passed by the AO giving effect to the directions of the DRP i.e., the final assessment order which is subject matter of this appeal, the AO passed the final assessment order dated 30.12.2014 without giving effect to the directions given by the DRP. Consequently, the addition to the total income pursuant to TP adjustment stood enhanced to **Rs. 6,07,73,624/-**.

11. In its appeal before the Tribunal, the Assessee has raised the following grounds of appeal viz., **(a)** That the AO erred in upholding the adjustment made by the TPO without giving effect to the directions given by the DRP (Ground Nos. 2 and 3). **(b)** That the TPO erred in not excluding Accentia Technologies Limited from the list of comparables although it fails the test of comparability and the DRP also erred in confirming the same (Ground No. 3A).

12. The Revenue in its appeal has raised the following grounds of appeal:

1. The order of the Dispute Resolution Panel is opposed to law and the facts and circumstances of the case.
2. The DRP erred in directing the TPO to apply 25% employees cost filter and to exclude M/s. Accropetal Technologies Ltd. as the company having less than 25% employee cost filter and it is predominantly engaged in providing services onsite without appreciating that the directions to the AO amounts to setting aside the issue which is outside the purview of the DRP under the provision of Section 144C as the DRP is not empowered to set aside the issue in terms of Section 144C(8) of the Act.
3. The DRP erred in directing the TPO to apply 75% Expert Earning filter consistently for ITES segment 'and to exclude M/s. ICRA online Ltd., M/s. Sundaram Business Services Ltd from comparables of ITES segment without appreciating that the directions to the AO amounts to setting aside the issue which is outside the purview of the DRP under the provision of Section 144C as the DRP is not empowered to set aside the issue in terms of Section 144C(8) of the Act.
4. The DRP erred in directing the AO to exclude M/s. Eclerx Services Ltd., M/s. Infosys BPO Ltd., M/s. ICRA Online Ltd from the list of comparables in ITES segment as being functionally different without appreciating the fact that companies qualify all the qualitative and quantitative filters applied by the TPO.
5. The DRP erred in holding that M/s. Infosys Ltd. cannot be taken as comparable, being functionally different, big brand value by relying on the decision of ITAT Bangalore in the case of Symphony Marketing Solutions India Pvt. Ltd. in ITA No.1316/Bang/2012 and Hyderabad ITAT in the case of Market Tools Research Pvt. Ltd. in ITA No.2066/HYD/2011 and Zavata India Pvt. Ltd. in ITA No.1781/HYD/2011 without appreciating the fact that the company qualify all the qualitative and quantitative filters applied by the TPO.
6. The DRP erred in holding that foreign exchange loss / gain is operating in nature without ascertaining the nexus of the forex gain / loss with the business activity of the taxpayer and without appreciating that such loss / gain though attributable to the operating activity is not derived from the operating activity and.
7. The DRP erred in concluding that forex gain / loss are to be treated as operating in nature without appreciating that though they may be incidental to the operating activity, they cannot be deemed as operating in nature since, they are not critical to operational activities of the business conducted by the taxpayer.

8. The DRP erred in directing the AO to carry out the working capital adjustment as per the actual figures worked out by the assessee without putting any cap on the ground that there is time value of money without appreciating the fact that the TPO had put a cap on the basis of the average cost of working capital of the comparables selected by the TPO and that the accurate details of debtors and creditors of the assessee and the comparables were not available.
9. The DRP erred in directing the AO to follow the ratio laid down by the Hon'ble Court in the case of Tata Elxsi Limited 349 ITR 98 and exclude telecommunication expenses and travel expenses incurred in Foreign currency from the export turnover also while computing the deduction u/s 10A of the I.T. Act, without appreciating the fact that there is no provision in section 10A that such expenses should be reduced from the total turnover also, as clause (iv) of the explanation to section 10A provides that such expenses are to be reduced only from the export turnover.
10. The DRP erred in not appreciating the fact that the jurisdictional High Court's decision in the case of 'Tata Elxsi limited 349 ITR 98 has not been accepted by the department amt, w\ appeal has been filed before the Hon'ble Supreme Court.
11. For these and such other grounds that may be urged at the time of hearing, it is humbly prayed that the order of the DRP be reversed and that of the Assessing Officer be restored.
12. 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”
13. The sum and substance of the grounds of appeal of the Revenue is that
(a) The DRP erred in directing the TPO to apply 25% employees cost filter and to exclude Acropetal Technologies Ltd. as the company fails the filter and is predominantly engaged in providing services onsite without appreciating that the directions to the AO amounts to setting aside the issue which is outside the purview of the DRP under the provisions of Section 144C of the Act as the DRP is not empowered to set aside the issue in terms of Section 144C(8) of the Act. Similarly, the DRP erred in directing the TPO to apply 75% export earning filter and directed to exclude ICRA

Online Ltd., and Sundaram Business Services Ltd. (Ground Nos. 2 and 3)

(b) The DRP erred in directing the AO to exclude ICRA Online Ltd., Infosys BPO Ltd., and Eclerx Services Ltd. as being functionally different without appreciating that the companies pass all the filters (Ground Nos. 4 and 5).;

(c) The DRP erred in holding that foreign exchange loss/gain is operating in nature without ascertaining the nexus of the forex gain/loss with the business activity without appreciating that such loss/gain though attributable to the operating activity is not derived from the operating activity (Ground Nos. 6 and 7). **(d)** The DRP erred in directing the AO to carry out the working capital adjustment without putting any cap on the ground that there is time value of money without appreciating that the TPO had put a cap on the basis of the average working capital of the comparables and that the accurate details of debtors and creditor of the assessee and the comparable were not available (Ground No. 8). **(e)** The DRP erred in directing the AO to follow the ratio laid down in Tata Elxsi Limited and exclude telecommunication and foreign travel expenses from the export turnover without appreciating the fact that there is no provision in Section 10A that such expenses should be reduced from the total turnover also. (Ground No. 9).

14. We shall first deal with the appeal of the Revenue. As far as Ground No.2 raised by the revenue is concerned, the grievance of the Revenue projected in those grounds is that the DRP has set side issue for consideration to the AO/TPO and in terms of Sec.144C(8) of the Act, the DRP has to decide issues before it and cannot set aside issues to AO/TPO. In this regard, we have perused the directions of the DRP and we find that with regard to exclusion of Acropetal technologies at page-16 last paragraph and page-17 first paragraph, the DRP has held that the expenses incurred on on-site provision of ITeS by the Assessee was 64% of the total expenses and therefore the company was to be regarded as one providing onsite ITeS and cannot be compared with a company providing offshore ITeS. Secondly it has held that the employee cost is less than

25% of the total cost of the company. The DRP has observed that in SWD segment of the very same company the TPO had employed a filter whereby companies which has less than 25% of its total cost towards employee cost have to be excluded as SWD services essentially involve and predominantly dependent on employees. The DRP therefore upheld the application of the employee cost filter in ITeS segment also. The concluding observations of the DRP were as follows:

“Accordingly, we direct the Assessing Officer to apply 25% employees cost filter and accordingly exclude Accropetal Technologies Limited”

The above observations of the DRP is a finding that the employee cost of Accropetal Technologies Ltd., is less than 25% of its total cost. However, we find that in form No.35A (form of objection before DRP) the Assessee has raised para 6.4.2 (Page-40 of Form No.35A), the objection for exclusion of this company is only on the basis of functional comparability and revenue recognition method followed by this company. Both the filters employed by the DRP for excluding this company from the list of comparables does not figure in the objection of the Assessee at all. However, this aspect has not been highlighted or taken as a ground of appeal by the revenue in its appeal. Therefore the only ground of appeal of the revenue against the directions of the DRP is that the directions of the DRP amount to a set aside of the issue to the TPO/AO. Since we have come to the conclusion that the directions of the DRP cannot be construed as a set aside of the issue to the TPO/AO, we find no merits in Gr.No.2 raised by the revenue.

15. As far as Gr.No.3 raised by the revenue is concerned, the grievance of the revenue is similar to Gr.No.2 i.e., the the DRP has set side issue for consideration to the AO/TPO and in terms of Sec.144C(8) of the Act, the DRP has to decide issues before it and cannot set aside issues to AO/TPO. The DRP has excluded these two companies by applying the filter of the foreign currency revenue is less than 75% of the total revenue. As far as ICRA Online Ltd., (ICRA) is concerned, the objection of the Assessee

before DRP was that this company was not functionally comparable with the Assessee (vide page-53 of Form No.35-A of objection before DRP). Sundaram Business Services Ltd., inclusion was not contested by the Assessee at all before DRP and the DRP suo motto considered exclusion of this company. In respect of both the companies the specific direction of the DRP is to exclude both the aforesaid two companies. (vide paragraph-2 at page-18 and paragraph-1 of page-19 of the DRP's directions). The revenue is not correct in contending that the issue has been set aside to the TPO/AO contrary to the provisions of Sec.144C(8) of the Act. Since we have come to the conclusion that the directions of the DRP cannot be construed as a set aside of the issue to the TPO/AO, we find no merits in Gr.No.3 raised by the revenue.

16. As far as Gr.No.4 & 5 raised by the revenue are concerned, the Revenue is challenging the exclusion ICRA, Infosys BPO Ltd., and Eclerx Services Ltd.

17. As far as exclusion of ICRA is concerned, before the DRP the Assessee sought exclusion of ICRA from the list of comparables on the ground that this company is functionally dissimilar to the Assessee. It was submitted that ICRA is engaged in providing services which are in the nature of KPO services. It provides financial and analytical services and support to clients in the area of Data Extraction, Aggregation, Electronic Conversion of Financial statements, Validation and Analysis, Accounting and Finance, Research and Analytics which are dissimilar to the services rendered by the Assessee. It was submitted that outsourced services segment of the company is engaged in the provision of high end consultancy services which cannot be compared to the assessee who is into provision of low end IT enabled services which are routine in nature. Further, the safe harbour rules clearly distinguish between an ITE service provider and a KPO service provider. The DRP has not considered any of the above objections.

18. Before the Tribunal, the Assessee has brought to our notice that this Tribunal has held that a KPO service provider cannot be compared to an ITE service provider. Reliance in this regard is placed on the decision in the case of *Arctern Consulting Pvt. Ltd. (supra)* IT(TP)A No.195/Bang/2015 & 302/Bang/2015 Order dated 11.08.2017 for AY 2010-11, & in the case of *Outsource Partners International (P) Ltd.* I.T(TP).A No.337/Bang/2015 Order dated 6.2.2017 for AY 2010-11, wherein on identical circumstances, the exclusion of this company came to be upheld/the company was directed to be excluded. The learned DR reiterated the stand of the revenue as reflected the grounds of appeal of the revenue.

19. We have carefully considered the rival submissions. In the case of *Outsources Partners International (P) Ltd.,(supra)*, this Tribunal has adjudicated identical issue and held that this company was not functionally comparable to an ITeS company such as the Assessee and for the reason that this company fails the export earning filter. Respectfully following the said decision, we uphold exclusion of this company from the list of comparable companies for the reasons given in this paragraph.

20. As far as exclusion of Infosys BPO Ltd., is concerned, the said company was excluded on the ground that the company is engaged in providing high-end integrated services, and whereas, the Assessee is engaged in providing low level back-office support services. Further, the company has huge brand name and owns significant intangibles. It is submitted that the brand name that is associated with Infosys Technologies Ltd. has an impact on the business operations of Infosys BPO. Also, during the financial year 2009-10, the company acquired all the outstanding membership interests of McCamish Systems LLC which constitutes a peculiar economic circumstance for which no reasonable adjustment could be made to mitigate its effect on the company's margin. Also, the company has incurred huge selling and marketing expenses and the same has been

increasing year on year. Reliance in this regard was placed on the decision in the case of *Arctern Consulting Pvt. Ltd. (supra)* and *Tesco Hindustan Service Centre (P.) Ltd. (2017)77 taxmann.com 48 (Bangalore)* for AY 2010-11, where in identical circumstances, the exclusion of the company came to be upheld/company was directed to be excluded. The learned DR reiterated the stand of the revenue as reflected in the grounds of appeal of the revenue.

21. We have carefully considered the rival submissions. In the case of Tesco Hindustan Service Centre Pvt.Ltd.(supra) vide paragraph 47 & 48 of its order, the Tribunal upheld exclusion of this company from the list of comparable companies, on the ground of presence of brand value and other factors. Respectfully following the decision of the Tribunal, we uphold the order of DRP excluding this company from the list of comparable companies.

22. As far as exclusion of Eclerx Services Ltd., is concerned, it was submitted on behalf of the Assessee the DRP rightly excluded this company from the final list of comparables as the same is functionally dissimilar to the Assessee. In this regard, it was submitted that the company is functionally dissimilar as it is a KPO engaged in providing data analytics and data process solutions. It provides end-to-end support through the trade lifecycle, including trade confirmation, settlements, transaction maintenance, risk analytics and reporting. The data analytics services being provided by Eclerx is significantly different from the routine ITE services provided by the Assessee. Reliance in this regard was placed on the decisions in the cases of *Arctern Consulting Pvt. Ltd. (supra)* and *Tesco Hindustan Service Centre (P.) Ltd. (supra)*, where in identical circumstances, the exclusion of the company came to be upheld/the company was directed to be excluded. The learned DR reiterated the stand of the revenue as is reflected in the grounds of appeal raised by the revenue.

23. We have carefully considered the rival submissions. In the case of Tesco Hindustan Service Centre (P) Ltd. (*supra*), this company was excluded from the list of comparable companies in the case of a company rendering ITeS similar to the services rendered by the Assessee in this appeal, observing as follows:

“37. *Eclerx Services Ltd.* : In this regard, the Id. counsel for the assessee has contended that this company's function is dissimilar with the assessee company as it provides industry specialised services like data analytics, operations management and audits & reconciliation services which cannot be compared to a BPO or IT Offshoring company. It was further contended that this company has abnormal profits and sales for the year. The Id. counsel further contended that this company was examined by the Tribunal in the case of *Stream International Services (P) Ltd.* (*supra*) and the Tribunal has held that even the company's functions are different, therefore it cannot be considered as comparable, following the order of the Mumbai Special Bench of the Tribunal in the case of *Maersk Global Centres (India) (P.) Ltd. v. Asstt. CIT* [2014] 43 taxmann.com 100/147 ITD 83 (Mum.) (SB). Therefore, this company may be excluded from the list of comparables.

38. The Id. DR simply placed reliance upon the order of the AO.

39. Having carefully examined the orders of lower authorities in the light of Tribunal's finding in the case of *Stream International Services (P) Ltd.* (*supra*), we find that the profile of this company was examined by the Tribunal in this case and following the order of the Special Bench of the Tribunal in the case of *Maersk Global Centres (India) (P.) Ltd.* (*supra*), the Tribunal held this company to be non-comparable. For the sake of reference, we extract the relevant portion of the order of the Tribunal:—

"(xi) *Eclerx Services Ltd. & Mold-Tek Technologies Ltd.*:-

For both these companies, the Id. Counsel for the assessee stated that these companies are functionally different, therefore, cannot be considered as comparables. We find that the Mumbai Special Bench of the Tribunal in the case of *Maersk Global Centres (India) Pvt. Ltd.* in ITA No. 7466/Mum/2012 has rejected eClerx Services Limited because solutions offered by this company included data analytics, operations, management, audits and reconciliation, metrics management and reporting services. The Special Bench opined that if these functions actually performed by the assessee company for its AEs are compared with the functional profile of M/s eClerx Services Limited and Mold-Tek Technologies Ltd., it is difficult to find out any relatively equal degree of comparability and the said entities cannot be taken as comparable for the purpose of determining ALP of the transactions of the assessee company with its AEs. Facts being identical, respectfully following the observations of the Special Bench (*supra*), we direct that these two entities be excluded from the list of final comparables."

40. Since the Tribunal has examined this issue under similar set of facts, we find no reason to take a contrary view. Accordingly following the order of the Tribunal in the case of *Stream International Services (P) Ltd.* (*supra*), we hold that this

company is not a good comparable and direct the AO/TPO to exclude it from the list of comparables.”

Respectfully following the aforesaid decision, we uphold the order DRP excluding the aforesaid company from the list of comparable companies.

24. Thus Gr.No.4 & 5 raised by the revenue is without any merit.

25. As far as Gr.No.6 & 7 raised by the revenue is concerned, the Revenue has challenged the action of the DRP in directing the AO to consider the gains/loss arising from fluctuation of foreign currency as being operating in nature. In this regard it was submitted that the gains on account of fluctuation in foreign currency has arisen from the international transaction of provision of ITE services. The gains are inextricably related to rendering of the main services and are not derived independently. As the gains relate to the rendering of the main service, the same ought to be treated as operating in nature. Reliance in this regard was placed on the following decisions:

- Assessee's own case for the assessment year 2006-07 ([2016] 74 taxmann.com 188 (Bangalore - Trib.), at para 48)
- SAP LABS India (P.) Ltd. v. ACIT ([2011] 44 SOT 156 (Bangalore) at para 42);
- PCIT v. B.C. Management Services (P.) Ltd. ([2018] 89 taxmann.com 68 (Delhi), at paras 7 and 8);
- PCIT v. Ameriprise India Pvt. Ltd. (Order dated 23.03.2016 passed in ITA No. 206/2016 at paras 3 and 4)

The learned DR reiterated the stand of the revenue as reflected in the grounds of appeal raised by the revenue in this regard.

26. We have carefully considered the rival contentions. The Hon'ble Delhi High Court in the case of PCIT Vs. B.C. Management Services (P) Ltd., (supra) held that foreign exchange gain has to be regarded as part of operating income by following its own order in *Pr. CIT v. Cashedge India*

(P.) Ltd. [IT Appeal No. 279 of 2016, dated 4-5-2016. Respectfully following the said decision, we uphold the directions of the DRP and dismiss Gr.No.6 & 7 raised by the revenue.

27. As far as Gr.No.8 raised by the revenue is concerned, the Revenue is challenging the action of the DRP in directing the AO to grant the working capital adjustment without any restrictions. In this regard, it was submitted on behalf of the Assessee that DRP has rightly held that working capital adjustment must be granted in full without there being any arbitrary and adhoc upper cap or restriction to the same. It was submitted that Rule 10B(3) of the Income-tax Rules, 1962 ('the IT Rules' for short), provides that an adjustment ought to be provided for any differences in the economic factors between the tested party and the comparables. A working capital adjustment is one such adjustment which is to be applied in order to adjust for the differences between the working capital positions of the tested party and of the comparable. The IT Rules do not provide for any cap or upper limit to such adjustments. This position under the Act and the IT Rules is also evident from the OECD Guidelines. Further, there was no basis for the TPO to restrict the adjustment and the Revenue's contention to that extent is ill-conceived. In any event, the restriction is patently not on the basis of the average working capital cost of the companies. Reliance in this regard was placed on the decision of this Hon'ble Tribunal in the case of *ARM Embedded Technologies P. Ltd v. DCIT* reported in [2015] 64 taxmann.com 445 (Bangalore - Trib.) wherein this Hon'ble Tribunal directed grant of the adjustment without putting any restrictions. The learned DR reiterated the stand of the revenue as reflected in the grounds of appeal of the revenue.

28. We have given a very careful consideration to the rival submissions. Similar issue had come for consideration before this Tribunal in the case of *ARM Embedded Technologies P.Ltd.* (supra) and this Tribunal held that working capital adjustment has to be allowed on actual basis without any restriction. The following were the relevant observations:

“24. Now coming to the issue of working capital adjustment, findings of the TPO in this regard as it appears at para 3.7, reads as under :

"3.7 Working Capital Adjustment:

The working capital adjustment is computed as per the formula given in Annexure to the OECD Guidelines, 2009. In this case, the average PLR adopted by SBI, the largest scheduled bank, for short term working capital loans for the relevant FY 2008-09 is considered. The average PLR of 12.50% p.a was adopted by the TPO while computing the working capital adjustment. The working capital adjustment is restricted to the average cost of capital computed at 1.71% in the case of the uncontrolled comparables selected by the TPO. Hence, the working capital adjustment in the case of the taxpayer is allowed as per the calculation in annexure-C or the average cost of capital to the comparables whichever is the least. The detailed discussion on this is given in the Annexure-D to the order. The computation of the working capital adjustment is annexed to this order as Annexure C."

TPO had restricted the cost of capital to 1.71%. Rationality for such an upper limit being placed on working capital adjustment was an issue which had come up before this Tribunal in the case of *Rambus Chip Technologies (India) (P.) Ltd. v. Dy. CIT* [IT (TP) A. 23/Ban/2015, dt. 22.07.2015. Coordinate bench had held as under at para 13 and 14 of its order:

"13. As regards ground No. 3(f), learned counsel for the assessee submitted that the AO/TPO while considering the working capital adjustment, has arrived at the working capital adjustment in the case of the assessee at 5.97%, but while giving effect to the working capital adjustment, has restricted the said adjustment to 1.71% in case of uncontrolled comparables selected by the TPO. The learned counsel for the assessee submitted that the TPO has not given any basis for such restriction of the working capital adjustment. He submitted that the CIT (A) also has not applied his mind to this issue but has summarily confirmed the order of the AO and therefore it has to be set aside.

14. On going through the TPO's order as well as annexure D referred to in the transfer pricing order on working capital adjustment, we find that the AO has not given any basis for restricting the adjustment to 1.71%. In all the cases relating to transfer pricing adjustment, this Tribunal has been directing to give working capital adjustment on actual basis and the TPO having arrived at 5.97% ought to have adopted the same instead of restricting it to 1.71 %. In view of the same, we deem it proper to remand this issue to the file of the AO/TPO for working out the ALP after giving adjustment of working capital as per the calculation of the AO in annexure D annexed to the transfer pricing order. This ground of appeal is accordingly allowed."

25. Accordingly we direct the AO/TPO to correctly work out the PLI of the final comparables after giving due adjustment for the working capital on actual basis. Related ground of the assessee is therefore allowed."

Respectfully following the aforesaid decision, we uphold the directions of the DRP in this regard and dismiss Gr.No.8 raised by the revenue.

29. As far as the appeal of the Assessee is concerned, the same in so far as it relates to Transfer Pricing adjustments are concerned, are projected in Gr.No. 2 and 3 of the Assessee's appeal. It is the plea of the Assessee that the TP adjustment would be 'NIL' if proper effect is given to the DRP's directions. It was submitted that in the event the DRPs directions are given effect to properly, the arithmetical mean of the working capital adjusted rectified margins of the above comparables would be within +/- 5% of the Assessee's margin for provision of the ITE services. Consequently, the international transaction of provision of ITEs services by the Assessee to its AE in FY 2010-11 can be concluded as being at arm's length. It was submitted that the action of the AO in passing the final assessment order contrary to the DRP's directions is erroneous and unsustainable. It was submitted that the directions issued by the DRP are binding on the AO in terms of Section 144C(5) of the Act and therefore the same ought to have been given effect to. The final assessment order passed contrary to the binding directions of the DRP would render it null and void. Reliance in this regard was placed on the following decisions:

- Software Paradigms Infotech (P.) Ltd. v. ACIT ([2018] 89taxmann.com 339, at paras 3.3.1 and 3.3.2);
- Flextronics Technologies (India) Pvt. Ltd. v. ACIT (Order dated 31.12.2018 passed by the Hon'ble Tribunal in IT(TP)A No. 832/Bang/2017, at paras 9 and 10); and
- July Systems and Technologies Pvt. Ltd. v. DCIT (Common order dated 31.10.2018 passed in IT(TP)A NO. 368/Bang/2016 and others at paras 15 and 16).

We are of the view that a direction to the AO/TPO to follow the directions of the DRP on all aspects dealt with the revenue's appeal and other directions of the DRP, would be just and sufficient. We hold and direct accordingly. Gr.No.2 & 3 of the Assessee's appeal are accordingly treated as allowed for statistical purpose.

30. We shall now take up for consideration corporate tax issues in the Revenue's appeal, which is projected in Grds.No.9 & 10 of the revenue's

appeal. These grounds of appeal arise under the following facts and circumstances. While computing the deduction u/s.10A of the Act, the AO noticed that during the relevant assessment year, the Assessee had incurred telecommunication charges and travel expenses in foreign exchange currency in respect of Sec.10A unit which was not reduced from the export turnover while computing deduction under section 10A of the Income Tax Act, 1961. The AO therefore excluded the aforesaid sum from the export turnover without excluding them from the total turnover. As a result, the deduction claimed u/s.10A of the Act by the Assessee was allowed at a lesser sum than what was claimed by the Assessee. It was the plea of the Assessee in the appeal against the assessment order before the CIT(A) that at all times during the relevant previous year, it was engaged in development of computer software and not in rendering any technical services. Communication expenses and travel expenses were incurred not for export of computer software outside India and therefore the exclusion from export turnover as done by the AO was not correct. Without prejudice to its contention that the aforesaid sums should not be excluded from the export turnover while computing deduction u/s.10A of the Act, the Assessee has also made an alternate prayer that expenses that are reduced from the export turnover should also be reduced from the total turnover and in this regard has placed reliance on the decision of the Hon'ble Karnataka High Court in the case of *CIT v. Tata Elxsi Ltd [2012] 349 ITR 98 (Karn)* wherein it was held that while computing deduction u/s.10A of the Act expenses that are reduced from the export turnover should also be reduced from the total turnover. The DRP accepted the alternate prayer of the Assessee to exclude the expenses in question both from the export turnover and total turnover while computing deduction u/s.10A of the Act. CIT(A) however upheld the order of the AO.

31. Taking into consideration the decision rendered by the Hon'ble High Court of Karnataka in the case of *CIT v. Tata Elxsi Ltd [2012] 349 ITR 98 (Karn)*, we are of the view that communication charges and expenses incurred in foreign exchange should be excluded both from export turnover and total turnover. We are of the view that as of today, law declared by the Hon'ble High Court of Karnataka which is the jurisdictional High Court is binding on us. Moreover, the order of the Hon'ble Karnataka High Court has been upheld by the Hon'ble

Supreme Court in the case of CIT v. HCL Technologies Ltd. in Civil Appeal No.8489-98490 of 2013 & Ors. dated 24.04.2018. The grounds are decided accordingly dismissed.

32. The other corporate tax grounds that remain for consideration are Gr.No. 4 & 5 in the Assessee's appeal. Vide these grounds, the Assessee has challenged the actions of the AO in (i) not granting full credit of TDS deducted and consequently levying interest under Section 234B and C of the Act; and (ii) not granting interest under Section 244A of the Act, contrary to the directions of the DRP. We are of the view that these grounds are factual in nature and therefore the AO must be directed to verify the same and grant them/rectify the same in accordance with law. We hold and direct accordingly.

33. The cross objection of the Assessee being purely supportive of the order of the CIT(A) vis-a-vis the grounds of appeal raised by the revenue. Since the appeal of the revenue, the CO also is dismissed as supportive and requiring no adjudication.

34. In the result, appeal by the Revenue is dismissed, while the appeal by the assessee is treated as allowed for statistical purpose while the Cross Objection of the Assessee is dismissed.

Order pronounced on 29th day of July, 2020.

Sd/-

(B.R.BASKARAN)
ACCOUNTANT MEMBER

Sd/-

(N.V.VASUDEVAN)
VICE-PRESIDENT

Bangalore
Dated : 29-07-2020

*am / Desai S Murthy

Copy to :

1. The Assessee
2. The Revenue
3. The CIT concerned.
4. The CIT(A) concerned.
5. DR
6. GF

By order

Asst. Registrar