IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCHES "B" : HYDERABAD

BEFORE SMT. P. MADHAVI DEVI, JUDICIAL MEMBER
AND
SHRI A. MOHAN ALANKAMONY, ACCOUNTANT MEMBER

ITA No.	A.Y.	Appellant	Respondent
400/Hyd/15	2010-11	United Online Software Development (India) Private Limited, HYDERABAD [PAN: AAACJ9549G]	The Deputy Commissioner of Income Tax, Circle-17(2), HYDERABAD
419/Hyd/15	2010-11	The Deputy Commissioner of Income Tax, Circle-17(2), HYDERABAD	United Online Software Development (India) Private Limited, HYDERABAD [PAN: AAACJ9549G]

For Assessee : Shri Ravi Bharadwaj, AR
For Revenue : Shri Y.V.S.T.Sai, CIT-DR

Date of Hearing : 30-01-2020
Date of Pronouncement : 04-06-2020

O R D E R

PER Smt. P. MADHAVI DEVI, J.M. :

The above appeals are filed by both the assessee as well as the Revenue against the assessment order dated 13.02.2015 passed u/s 143(3) r.w.s. 144C of the I.T. Act.

2. Brief facts of the case are that the assessee company is engaged in the business of software development. It filed its return of income for the A.Y 2010-11 disclosing a total income of Rs.2,21,65,000/-. Since the assessee had entered into an international transaction with its AE, the AO referred the

determination of the ALP of international transaction to the TPO. The TPO vide orders dated 24.09.2013 passed an order u/s 92CA of the I.T. Act determining the adjustment towards the ALP at Rs.3,57,69,069/-. In accordance with the TPO order, the AO proposed the draft assessment order dated 24.03.2014 proposing an addition of Rs.3,57,69,069/- towards TP adjustment and also an addition of Rs.6,78,371/- being the disallowance from out of the head repairs to computers and other equipment on the ground that the same cannot be allowed as revenue expenditure. Aggrieved, the assessee preferred its objections to the DRP. The DRP granted partial relief by excluding two companies i.e. M/s Infosys Technologies Ltd and L&T Info Ltd. on the filter of high turnover and brand value, while it confirmed the other companies taken by the TPO. Against the relief granted by the DRP, the Revenue is in appeal before us and against the confirmation of the balance of the draft assessment order, the assessee is in appeal before us. The assessee has raised the following grounds of appeal:

Grounds of Appeal for ITA No.400/Hyd/2015:

Based on the facts and circumstances of the case and in law, the learned Assessing Officer ("AO") / learned Transfer Pricing Officer ("TPO") and the Hon'ble Dispute Resolution Panel ('DRP') erred in:

TRANSFER PRICING MATTERS - Relating to determination of Arm's Length Price ("ALP") under Transactional Net Margin Method ("TNMM") in respect of software services provided to the Associated Enterprises ("AEs")

Rejection of transfer pricing documentation maintained
1. Rejection of the transfer pricing documentation maintained by the applicant in accordance with the provisions of the Act read with the Income-tax Rules,

1962 ('Rules') and making an adjustment of Rs.3,22,58,649 to the international transactions relating to provision of software services to its AE by undertaking a fresh economic analysis during the course of assessment proceedings.

Rejection of use of contemporaneous data and multiple year data
2. Using the single year data (FY 2009-10) of comparable companies selected which was not available at the time of complying with the transfer pricing documentation requirements and rejecting the use of multiple year data in computing the arm's length price of international transactions.

Use of additional filters
3. Inter-alia use of the following additional/modified filters in undertaking the comparative analysis and rejecting comparable companies having:

a) Diminishing revenues;
b) Persistent losses;
c) Different financial year-end; and
d) Export sales less than 75% of the sales.

Selection of comparables
4. Not undertaking an objective comparative analysis and inter alia selecting the following companies as comparable to the software services of the Appellant:

a) Comp-U-Learn Tech India Ltd;
b) E Infochips Bangalore Ltd;
c) KALS Info Systems Ltd;
d) Tata Elxsi Ltd (Seg);

Rejection of comparables
5. Not undertaking an objective comparative analysis and inter alia rejecting the following comparable companies:

a) Akshay Software Technologies Ltd;
b) CG V AK Software and Exports Ltd; and
c) Satyam Computers Services Ltd.

Error in margin computation
6. Computation of net margins of the following companies selected as comparables:

a) Considering Provision for Bad debts as Non-Operating expenses in computing margins for the following companies:

i) E-Infochips Bangalore Ltd;
ii) E-Zest Solutions Ltd;
iii) Kuliza Technologies Private Limited;

b) Computing the net margins of CAT Technologies Ltd by excluding Advertisement expenses written off considering it as inoperative expenses.

c) Not allowing unallocable cost in the computation of net margins for the following:

i) Kals Information Systems Ltd (Seg); and
ii) Tata Elxsi Ltd (Seg).

Foreign Exchange Loss
7. Not appreciating the fact that foreign exchange loss of Rs.l,30,72,615 is an extraordinary item for the year and hence adjustment should be provided for the same.

Negative working capital adjustment
8. Making a negative working capital adjustment without appreciating the fact that the company does not bear any working capital risks.

Adjustment for risk differences
9. Not adjusting the net margins of the comparable companies taking into account the functional and risk differences between the international transaction of the Appellant and the comparable companies in accordance with the provisions of Rule 10B(1)(e).

CORPORATE TAX ISSUES

10. Disallowing the expenditure incurred towards maintenance and replacement of computer parts and software license considering it as capital expenditure:

11. Non - grant of TDS credit to the extent of Rs. 4,443

12. Adding the refund issued of Rs.31,82,740 to the current year tax demand which was adjusted other years tax demand, where no tax demand was outstanding".

3. In addition to the above grounds, the assessee has also raised the following additional ground of appeal:

> *Additional Ground of Appeal - Transfer Pricing matters*
> *Selection of comparables*
> *13. Not undertaking an objective comparative analysis and inter alia selecting the following companies as comparable to the software services of the Appellant:*
>
> *a) Persistent Systems Ltd;*
> *b) Sasken Communication Technologies Ltd;*
> *c) E - Zest Solutions Ltd;*
> *d) Mindtree Ltd; and*
> *e) Zylog Systems Ltd;*
> *f) Evoke Technologies private Limited;*
> *g) Kuliza Technologies private Limited";*

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

> ***Grounds of Appeal for ITA No.419/Hyd/2015:***
>
> *1. Whether on the facts and in the circumstances of the case, the DRP is justified in rejecting the comparable companies on the ground of exceptionally large scale of operations and thereby ignoring the fact that high or low turnover do not influence the margins of the comparables?*
>
> *2. Any other grounds that may be urged at the time of hearing the appeal".*

5. At the time of hearing, the learned Counsel for the assessee, Shri Ravi Bharadwaj, submitted that the assessee is not pressing grounds 1, 2, 3 & 9 and these grounds are accordingly rejected as not pressed.

6. The learned Counsel for the assessee prayed for admission of the additional grounds of appeal stating that in the additional ground, the assessee is only challenging the comparability of the companies mentioned therein, as

according to him, AO & the DRP have not taken any comparative analysis for selecting these companies. Further, he also submitted that that Persistent Systems Ltd. & Sasken Communication Technologies Ltd. were considered as comparable by the assessee in its TP documentation on the basis of information available about the said companies at that point of time, but, since some more information is available about these companies subsequently, the assessee is now challenging the comparability of these companies also.

7. The learned DR, however, objected to the admission of the additional ground stating that the objections of the assessee are on factual aspects of the comparable companies which were never taken before the AO/TPO or before the DRP and therefore, they cannot be taken at this point of time. In support of this contention, he placed reliance upon the decision of the Hon'ble Karnataka High Court in the case of Pr. CIT Bangalore vs. Softbrands India (P) Ltd reported in (2018) 94 taxmann.com 426 (Karnataka) and the decision of the Hon'ble Andhra Praesh High Court in the case of CIT vs. Begum Noor Banu reported in (1993) 69 Taxmann 565 (A.P).

8. The learned Counsel for the assessee however, submitted that the decisions relied upon by the learned DR are distinguishable on facts and since Transfer Pricing analysis itself is factual, the additional ground raised by the assessee is also factual and the Tribunal being the final fact finding

authority, the Tribunal may admit the same and adjudicate the said ground.

9. Having regard to the rival contentions and the material on record and particularly the admissibility of the additional ground and the decisions relied upon by the learned DR, we find that the Hon'ble Karnataka High Court in the case of Pr.CIT vs. Softbrands India (P) Ltd (Supra) has held that the question as to whether the comparables had been rightly picked or not, filters for arriving at correct list of comparables had been rightly picked or not, do not give rise to any substantial question of law; and unless a perversity in findings of fact in these matters is established before the Hon'ble High Court, no substantial question of law arises for consideration u/s 260A. This finding is, in our opinion, with regard to the maintainability of the appeal before the Hon'ble High Court as the Hon'ble High Court's jurisdiction u/s 260A is mainly on substantial questions of law. Therefore, this decision is not strictly applicable to the admissibility of the additional ground by the Tribunal as the ITAT is the final fact finding authority and the facts relating to most of these companies are already on record. Therefore, there is no prejudice caused to the revenue by admitting the additional ground.

10. In the case of CIT vs. Begum Noor Banu (Supra), the Hon'ble A.P High Court was considering whether the Appellate Tribunal has jurisdiction to grant relief on consideration of an additional ground raised before it by the assessee for the first

time although such ground related to an item of assessment which was not disputed at any of the earlier stages and whether the assessee who returned income from capital gains voluntarily for assessment and never objected to inclusion of that part of income before the AAC. The Hon'ble High Court held that an assessee could not dispute the assessment of tax on capital gains before Tribunal in such circumstances. We find that this decision is also distinguishable on facts because in the case before us, the assessee's objection is that the AO has not conducted objective analysis before taking these companies as comparables and it is purely a factual issue and all the companies against whom objections are raised except the first two companies are the companies taken by the TPO after rejecting the assessee's TP analysis. Therefore, we are of the opinion that this decision is also not applicable to the case on hand and the assessee's additional ground of appeal can be admitted.

11. Coming to the merits of the assessee's as well as Revenue's appeal, we find that the assessee has selected 21 companies its TP study, out of which TPO has accepted 7 companies as comparables. Thereafter, the TPO conducted an independent study and arrived at 19 companies as comparable including the above 7 companies taken by the assessee. These 7 companies include not only Persistent Systems Ltd. and Sasken Communication Technologies Ltd. but also Zylong Systems Ltd. and Mind Tree Ltd., which were also selected by the assessee in its TP Study. Out of the total 19 companies selected by the TPO, now before us, only 5 companies are

accepted by the assessee. Out of the balance 13 companies, the DRP has directed exclusion of two companies i.e. Infosys Ltd and L&T Infotech Ltd on the ground of high turnover as well as brand value.

12. We have gone through the T.P order and also DRP's directions and have also considered the argument of the learned Counsel for the assessee that most of these companies are not comparable to the assessee in the light of the various decisions of the Tribunal in similar cases. We find that the assessee has returned a margin of 9.02% as against the average margin of the final comparables adopted by the TPO at 22.69%. It is the case of the assessee that the decisions of the ITAT on various comparables though cited by the assessee, have not been considered by the authorities below.

13. After hearing both the parties and after considering the rival contentions and since both the parties have tentatively agreed for a remand of the issue to the TPO, we deem it fit and proper to set aside the issues to the TPO for denovo consideration. We make it clear that the TPO shall examine whether the assessee's case is similar to the cases on which he has placed reliance upon and whether thedistinguishable factors for exclusion of the comparables in those cases also existed in the assessee's case. If it is found that the assessee's case is similar and the distinguishing factors exist, then the TPO shall exclude such companies from the final list of comparables and the TPO shall be free to adopt any other

comparable companies if they are so comparable to the assessee.

14. As far as the Revenue's appeal is concerned, we find that the DRP has directed exclusion of these two companies not only by applying the turnover filter but has also held them to be not comparable due to brand value. The TPO shall examine this fact also and if these two companies have brand value, then they shall not be considered as comparable to the assessee.

15. As regards Ground No.6 relating to provisions for bad debts being considered as non-operating expenditure in computing the margin of only 3 companies mentioned in Ground No.6, we direct the AO/TPO to reconsider the same and bring out the reasons for considering the same as non-operating in the case of these three companies only, because the AO/TPO have to follow a uniform and consistent manner in adopting a filter and cannot deviate from the same in respect of some companies.

16. With regard to the sub grounds in Ground Nos. 6, 7 & 8 also, the AO/TPO may reconsider the issue denovo. As regards Ground No.7, we are not convinced that the foreign exchange loss is an extra-ordinary item in the year to the assessee alone. Similar foreign exchange loss would have been incurred by the comparable companies as well and therefore, it is not a

distinguishing factor to be considered for arriving at the ALP of the international transaction.

17. As regards the corporate tax issues are concerned, we find that they are consequential in nature and therefore, the AO may grant consequential relief, if any, to the assessee, in accordance with law. The AO/TPO shall reconsider all the issues denovo in accordance with the law and in the light of precedents on the issue.

18. In the result, both the Appeals of the Revenue and Assessee are partly allowed for statistical purposes.

Order pronounced in the Open Court on 4th June 2020.

Sd/-	Sd/-
(A. MOHAN ALANKAMONY) **ACCOUNTANT MEMBER**	**(P. MADHAVI DEVI)** **JUDICIAL MEMBER**

Hyderabad, dated 4th June, 2020.
Vinodan/sps
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5 CIT-5 Hyderabad 500004
6 The DR, ITAT Hyderabad
7 Guard File

By Order