

**IN THE INCOME TAX APPELLATE TRIBUNAL
“A” BENCH : BANGALORE**

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

IT(TP)A No.2751/Bang/2017
Assessment year: 2013-14

M/s. Evolving Systems Networks India Pvt. Ltd., 3 rd Floor, Gurudas Heritage, #59/2, 100 Feet Ring Road, Banashankari II Stage, Bengaluru – 560 070. PAN : AABCE 2761 N	Vs.	The Assistant Commissioner of Income Tax, Circle – 2(1)(2), Bengaluru.
APPELLANT		RESPONDENT

Assessee by	:	Shri. Padam Chand Khincha, CA
Revenue by	:	Ms. Neera Malhotra, CIT(DR)(ITAT), Bengaluru.

Date of hearing	:	22.06.2021
Date of Pronouncement	:	24.06.2021

ORDER

Per N.V. Vasudevan, Vice President

This appeal by the assessee is directed against the order dated 6.10.2017 of ACIT, Circle 2(1)(2), Bangalore (hereinafter referred to as the Assessing Officer, “AO” in short) passed u/s.143(3) read with Section 144C(13) of the Income Tax Act, 1961 (Act) in relation to AY 2013-14.

2. The assessee is engaged in the business of provision of Software Development Services (SWD services), to its wholly owned holding company. In terms of the provisions of Sec.92-A of the Act, the assessee and its wholly owned holding company were Associated Enterprises

("AEs"). In terms of Sec.92B(1) of the Act, the transaction of providing SWD Services to holding company was an "international transaction" i.e., a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises. In terms of Sec.92(1) of the Act, the Any income arising from an international transaction shall be computed having regard to the arm's length price. In this appeal by the assessee, the dispute is with regard to determination of Arms' Length Price (ALP) in respect of the rendering SWD services to the AE.

3. As far as the provision of Software Development services are concerned, the assessee filed a Transfer Pricing Study (TP Study) to justify the price paid in the international Transaction as at ALP by adopting the Transaction Net Margin Method (TNMM) as the Most Appropriate Method (MAM) of determining ALP. The assessee selected Operating Profit/Operating Cost (OP/OC) as the Profit Level Indicator (PLI) for the purpose of comparison. The OP/OC of the assessee was arrived at 18.08% by the assessee in its TP study. The operating income was Rs.15,86,27,520/-. The assessee chose companies who are engaged in providing similar services such as the assessee. The assessee identified comparable companies whose average arithmetic mean of profit margin was

comparable with the Operating margin of the Assessee. The Assessee therefore claimed that the price it charged in the international transaction should be considered as at Arm's Length.

4. The Transfer Pricing Officer (TPO) to whom the determination of ALP was referred to by the AO, accepted TNMM as the MAM and also used the same PLI for comparison i.e., OP/TC. He also selected comparable companies from database. The TPO on his own identified 7 companies as comparable with the Assessee company and worked out the average arithmetic mean of their profit margins as follows:

SI. No.	Name of the taxpayer	OP/OC
1	CG-VAK Software Exports Ltd	20.54%
2	I C R A Techno Analytics Ltd.	17.10%
3	Larsen & Toubro Infotech Ltd.	26.06%
4	Mindtree Ltd. (Seg)	18.19%
5	Persistent Systems Ltd.	28.27%
6	R S Software (India) Pvt Ltd	17.41%
7	Tech Mahindra Ltd (Seg)	18.72%
Unadjusted average		20.90%

5. The TPO computed the Addition to total income on account of adjustment to ALP after providing for negative working capital adjustment, as follows:

<i>Arm's Length Mean Margin on cost</i>	20.90%
<i>Less: Working Capital Adjustment</i>	-6.91%
<i>(As per Annex. B)</i>	
<i>Adjusted margin</i>	27.81%
<i>Operating Cost</i>	13,50,33,970
<i>Arm's Length Price(ALP)</i>	17,25,87,555

<i>127.81% of Operating Cost</i>	
<i>Price Received</i>	<i>15,94,47,578</i>
<i>Variation in Price</i>	<i>1,31,39,977</i>
<i>3% of price received</i>	<i>47,83,427</i>
<i>Shortfall being adjustment</i>	<i>1,31,39,977</i>

The above shortfall of Rs. 1,31,39,977/- was treated as transfer pricing adjustment u/s 92CA in respect of software development segment of the taxpayer's international transactions."

Thus a sum of Rs.1,31,39,977/- was added to the total income of the Assessee on account of determination of ALP for provision of SWD services by the Assessee to its AE.

6. The Assessee filed objections before the Disputes Resolution Panel (DRP) against the draft assessment order passed by the AO wherein the addition suggested by the TPO as adjustment to ALP was added to the total income of the Assessee by the AO. The DRP gave certain directions. Based on the directions of the DRP, the AO passed the final order of assessment. To the extent the Assessee did not get relief from the DRP, the Assessee has preferred appeal before the Tribunal.

7. At the time of hearing, the learned Counsel for Assessee prayed that ground with regard to excluding 5 comparable companies chosen by the TPO by application of Turnover Filter alone be adjudicated and all other grounds would be academic, hence need not be adjudicated. The Assessee seeks exclusion of the following 5 companies out of the 7 companies retained after the order of the DRP.

- a) Larsen & Turbo Infotech Ltd*
- b) Persistent Systems Ltd.*
- c) Tech Mahindra Ltd*

- d) *Mindtree Ltd*
e) *RS Software India Pvt Ltd*

8. We have heard the rival submissions. As far as ground No.2 raised by the Revenue is concerned the question boils down on application of turnover filter in choosing comparable companies. The turnover of the Assessee is Rs.15.86 Crores whereas the turnover of the 5 companies mentioned above Rs.200 Crores. The turnover of these 5 companies are as follows:

<i>Sl. No.</i>	<i>Comparables</i>	<i>Operating Turnover for FY 2012-13 (INR crores)</i>
1	<i>Larsen & Turbo Infotech Limited</i>	3,609.32
2	<i>Persistent System Limited</i>	996.75
3	<i>Tech Mahindra Ltd</i>	5,595.70
4	<i>Mindtree Ltd</i>	2,361.82
5	<i>RS Software India Pvt. Ltd.,</i>	293.05

9. As far as excluding the companies on the basis of turnover is concerned, the issue has been settled in several decisions of the Tribunal and has been elaborately discussed by this Tribunal in the case of *Autodesk India Pvt. Ltd. v. DCIT in IT(TP)A No.540 & 541/Bang/2013, order dated 06.07.2018*. The Tribunal in this decision after review of entire case laws on the subject, considered the question, whether companies having turnover more than 200 crores upto 500 crores has to be regarded as one category and those companies cannot be regarded as comparables with companies having turnover of less than 200 crores, the Tribunal held as follows:-

“17.7. We have considered the rival submissions. The substantial question of law (Question No.1 to 3) which was framed by the Hon'ble Delhi High Court in the case of Chryscapital Investment Advisors (India) Pvt.Ltd., (supra) was as to whether comparable can be rejected on the ground that they have exceptionally high profit margins or fluctuation profit margins, as compared to the Assessee in transfer pricing analysis. Therefore as rightly submitted by the learned counsel for the Assessee the observations of the Hon'ble High Court, in so far as it refers to turnover, were in the nature of obiter dictum. Judicial discipline requires that the Tribunal should follow the decision of a non-jurisdiction High Court, even though the said decision is of a non-jurisdictional High Court. We however find that the Hon'ble Bombay High Court in the case of CIT Vs. Pentair Water India Pvt.Ltd. Tax Appeal No.18 of 2015 judgment dated 16.9.2015 has taken the view that turnover is a relevant criterion for choosing companies as comparable companies in determination of ALP in transfer pricing cases. There is no decision of the jurisdictional High Court on this issue. In the circumstances, following the principle that where two views are available on an issue, the view favourable to the Assessee has to be adopted, we respectfully follow the view of the Hon'ble Bombay High Court on the issue. Respectfully following the aforesaid decision, we uphold the order of the DRP excluding 5 companies from the list of comparable companies chosen by the TPO on the basis that the 5 companies turnover was much higher compared to that the Assessee.

17.8. In view of the above conclusion, there may not be any necessity to examine as to whether the decision rendered in the case of Genisys Integrating (supra) by the ITAT Bangalore Bench should continue to be followed. Since arguments were advanced on the correctness of the decisions rendered by the ITAT Mumbai and Bangalore Benches taking a view contrary to that taken in the case of Genisys Integrating (supra), we proceed to examine the said issue also. On this issue, the first aspect which we notice is that the decision rendered in the case of Genisys Integrating (supra) was the earliest decision rendered on the issue of comparability of companies on the basis of turnover in Transfer Pricing cases. The decision was rendered as early as 5.8.2011. The decisions rendered by the ITAT Mumbai Benches cited by

the learned DR before us in the case of Willis Processing Services (supra) and Capgemini India Pvt.Ltd. (supra) are to be regarded as per incurium as these decisions ignore a binding co-ordinate bench decision. In this regard the decisions referred to by the learned counsel for the Assessee supports the plea of the learned counsel for the Assessee. The decisions rendered in the case of M/S.NTT Data (supra), Societe Generale Global Solutions (supra) and LSI Technologies (supra) were rendered later in point of time. Those decisions follow the ratio laid down in Willis Processing Services (supra) and have to be regarded as per incurium. These three decisions also place reliance on the decision of the Hon'ble Delhi High Court in the case of Chriscapital Investment (supra). We have already held that the decision rendered in the case of Chriscapital Investment (supra) is obiter dicta and that the ratio decidendi laid down by the Hon'ble Bombay High Court in the case of Pentair (supra) which is favourable to the Assessee has to be followed. Therefore, the decisions cited by the learned DR before us cannot be the basis to hold that high turnover is not relevant criteria for deciding on comparability of companies in determination of ALP under the Transfer Pricing regulations under the Act. For the reasons given above, we uphold the order of the CIT(A) on the issue of application of turnover filter and his action in excluding companies by following the ratio laid down in the case of Genisys Integrating (supra).”

10. Respectfully following the aforesaid decision, we hold that the aforesaid five companies should be excluded from the list of comparable companies. We hold and direct accordingly. The learned DR however pointed out that the Assessee did not raise this issue of turnover filter before AO and raised it before DRP in which the turnover limit of Rs.1000 crores alone is mentioned. In our opinion, this will not be very material, as the turnover filter of Rs.200 crores has been applied in several cases by this Tribunal. The Assessee cannot be denied the right to seek its exclusion before the Tribunal and in this regard the learned counsel for Assessee has rightly placed reliance on the decision of the Special Bench of the Hon'ble Tribunal in the case of DCIT v. Quark Systems (P.) Ltd. ([2010] 38 SOT 307 (CHD.) (SB)) for the proposition that the

Assessee cannot be precluded from seeking exclusion of a company selected by it in its TP study, when the company is otherwise not comparable to the Assessee. We therefore direct exclusion of the aforesaid 5 companies from the list of comparable companies.

11. The only other ground pressed was with regard to the action of the TPO in treating provision for bad and doubtful debts as part of non operating expense while computing operating margin of comparables. On this issue, which is raised for the first time, we do not find any grounds raised before the lower authorities and hence this ground does not arise out of the order of the AO and hence dismissed. No other grounds raised in the grounds of appeal as well as the additional grounds were pressed for adjudication as in the opinion of the counsel for the learned counsel for the Assessee, those grounds would become academic.

12. We direct the AO/TPO to compute the ALP in the light of the directions given in this order after affording opportunity of hearing to the Assessee.

13. In the result, appeal of the Assessee is partly allowed.

Pronounced in the open court on the date mentioned on the caption page.

Sd/-
(B. R. BASKARAN)
Accountant Member

Sd/-
(N. V. VASUDEVAN)
Vice President

Bangalore,

Dated: 24.06.2021.

/NS/*

Copy to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore.
6. Guard file

By order

Assistant Registrar
ITAT, Bangalore.